CP14/06 - Regulated fees and levies: Rates proposals 2014/15

This response is submitted on behalf of the Association of Mortgage Intermediaries (AMI). AMI is the trade association representing over 80% of UK mortgage intermediaries.

Intermediaries active in this market act on behalf of the consumer in selecting an appropriate lender and product to meet the individual consumer's mortgage requirements. Our members also provide access to associated protection products.

Our members are authorised by the Financial Conduct Authority (FCA) to carry out mortgage and insurance mediation activities. Firms range from sole traders through to national firms and networks, with thousands of advisers.

AMI welcomes the opportunity to respond to FCA's consultation paper on Regulated fees and levies: Rates proposals 2014/15.

Overview

We continue to see an increase in the overall cost of regulation for the financial services industry, which we consider to be excessive in the wider economic context.

The FCA has set out a revised funding requirement of £446.4m. In addition to this the PRA budget for 2014/15 is £227.2m. This gives a combined total funding requirement across the industry of £673.6m. Prior to the twin peaks separation, FSA's final budget for 2012/13 was £559.8m. This means we have seen a 20% increase to costs of financial services regulation in just 2 years. Such an increase over such a short period of time does not seem justifiable given the economic conditions that most businesses are still operating under. Furthermore, it means that the industry is currently paying nearly £0.5bn just for conduct regulation. Our member firms consider this to be excessive and unacceptable.

In addition to the costs incurred directly from FCA's fees and levies, the cost for firms of delivering on compliance requirements continues to be significant. Whilst these costs can be burdensome for all sizes of firms we remain concerned about the impact on smaller brokers, in particular from the largely hidden cost of section 166 reports. FCA must be transparent about how section 166 costs are absorbed by firms and should publish clear details of the frequency of use and the related costs across the various categories of firms.

FCA continues to apportion the majority of its costs across the main fee-blocks. This is clearly a relatively simple methodology for distributing costs but it does not focus on those firms that present the greatest risks to FCA's key objectives:

- To secure an appropriate degree of protection for consumers
- To protect and enhance the integrity of the UK financial services system
- To promote effective competition in the interests of consumers

AMI is strongly of the view that the FCA should be tasked with reducing its annual budget or at worst its budget should be capped with any increases limited by the rate of consumer price inflation or less. Having such cap in place would not just provide greater certainty for regulated firms but it would also help the FCA to be more efficient by encouraging it to prioritise its resources to meet its budget, rather than setting its budget based on its needs. Effective cost controls should be a driver to producing good outcomes in line with its core objectives. This would limit regulatory creep and ensure that the focus is clearly on the areas of greatest consumer or systemic risk. Organisations without clear cost controls are rarely cost-effective in the way they operate. The FCA expects such focus and clarity in the firms it regulates and it should be no different.

AMI expects that the fees to cover the Consumer Credit regime will need significant refinement from these early draft proposals as the regime, as proposed, gives rise to a number of glaring inconsistencies and unfair elements.

Fee structure review

We are extremely disappointed that the review of FCA's fee-block allocation has been closed with the outcome being that the current format remains unchanged

We accept that the FCA must consider the impact and limitations of any changes and that the alternative proposals of using UK regulated income would have produced inconsistencies and difficulties for some groups of firms. However, the current methodology is not without its own limitations, as was demonstrated in our discussions with the FCA. In light of what was discussed in the report, the current method appears to leave intermediaries paying a disproportionally higher degree of the costs. We consider that the lobbying undertaken by larger entities has done smaller firms a severe dis-service in blocking reform.

We still believe that FCA's current allocation method unfairly apportions too much of its indirect costs across all fee blocks and does not adequately apply sufficient direct costs to individual fee-blocks, in particular where the more significant systemic risks apply. We request that FCA continues to regularly review its fees structure.

Main issues

<u>FCA</u>

Under the current proposals mortgage brokers would see a 3.2% increase in the annual funding requirement allocated to their fee-block (fee-block A18). This would see an increase from £15.2m in 2013/14 to a proposed figure of £15.7m for 2014/15.

The number of mortgage brokers who are eligible to cover the costs within the fee-block is estimated to increase next year but only very slightly from 5,238 to 5,283, an increase of just 0.9%. The tariff data has increased from £0.9bn to £1bn. This would lead to a decrease in the individual tariff rate of 1.9%.

In the current market most mortgage brokers will also hold an insurance permission. Under FCA's latest proposals those holding an insurance permission will see an increase in the annual funding requirement for the insurance fee-block from £25.1m to £25.9m, an increase of 3.2%.

The number of firms in the A19 block is expected to increase slightly from 12,522 to 12,749, an increase of 1.8%. However, the increase in the tariff from £14.8bn last year to £15.2bn for 2014/15 means a 0.6% increase in the tariff rate for those firms contributing to the A19 fee-block.

We welcome the retention of the £1,000 minimum fee. We see it as an essential that smaller firms are not priced out of the financial services industry due to spiralling regulatory costs. FCA has stated that 42% of firms will pay the minimum fee, which is broadly the same as last year. However as many smaller firms operate under the network (appointed representative) structure, they are exposed to increasing fees as part of a larger whole.

Mortgage brokers will not see a significant change to the total fees they are charged for holding the permissions relating to A18 and A19 but firms will ultimately focus on the total cost from the final invoice that arrives on their desks. However, since mortgage brokers became regulated in 2004 they have seen the cost of regulation rise significantly. The smallest mortgage broker firms would have seen the cost of regulation double since 2004. The larger mortgage brokers have seen costs increase 3.5 times during the same period. It is important to remember that in this period the number of brokers have reduced from a high of 30,000 to around 12,000 today. The level of gross lending has also reduced. This means that fewer brokers are funding a higher proportion of regulatory cost. We consider that a smaller, more professional and experienced sector should not be shouldering an ever increasing cost burden. In the appendix at the end of our response we show the increase in costs for typical small broker and a large firm and it can be seen that FCA costs continue to rise significantly.

We would have expected to see that the split between the PRA and the FCA would have allowed FCA to focus on a more appropriate risk measure based on the capacity of the industry to fund regulation, rather than the need to fund the regulator itself.

The manner by which FCA apportions its indirect costs to fee-blocks is still a concern. FCA should place a greater focus on direct costs to ensure that where possible costs are paid by the fee-blocks which generate the cost.

Consumer Credit

We welcome the application of the income thresholds to the fees calculation for consumer credit. However, we are concerned that mortgage brokers could be caught by the requirements to hold a consumer credit permission because of the core mortgage activities they already undertake, or more worryingly due to imprecise drafting around Buy-to-Let transactions making them the only part of the chain captured under regulation. In undertaking these consumer credit activities mortgage brokers derive no income that will be able be ascribed to their consumer credit activities. This would leave brokers in the invidious position of having to pay the consumer credit annual minimum fee, which is distinct from the minimum fee on their other permissions, for an activity they make no income from. We cannot think of any other part of FCA's fees and levies regime where such a policy is put in place. It would seem fundamentally at odds with the findings made in FCA's funding review with respect of turnover being a sufficiently valid indicator of regulated activity.

We need to see a revised position of no eligible income, no fee, or a consolidation so that their mortgage minimum fee also covers the consumer credit permission.

FOS

We welcome the continuation of last year revised approach to FOS's funding. Those firms that use FOS the most should pay the majority of its costs. We support the retention of the 25 free cases and the relatively low levy is reflective of the limited exposure mortgage brokers have to FOS.

MAS

We welcome the decision to hold the cost of the Money Advice Service at £43m. Under its new funding model, which considers usage, outcomes and the FCA's levy, mortgage broker firms will see costs increase from £1m to £2.2m.

We welcome the revised approach to the way MAS's fees are collected. It is essential that MAS's fees are apportioned in an appropriate manner. The original method of allocating fees based solely on the FCA's fee blocks clearly did not meet MAS's needs. However, it is essential that MAS's funding structure is continually reviewed to ensure that the correct apportionment of costs is applied across the three tiers of the new structure.

Although mortgage brokers overall funding of MAS remains small in comparison to other sectors, brokers have seen a significant rise in costs compared to last year's funding model. We consider that the longer term funding of MAS should not be levied on the industry, but whilst it is being funded by industry under the current arrangement the recovery should come for the fee blocks which benefit from its work.

MAS must be an accountable body and demonstrate value for money and therefore it should be subject to regular audits by the National Audit Office (NAO). We are extremely concerned about the way MAS uses its almost unlimited funding. Citizens Advice would be a more appropriate place to allocate such levels of funding and would ultimately yield better outcomes for consumers.

MAS has clearly been able to fund an extensive advertising campaign and has been attracting a large number of consumers to its website. However, it is debatable what outcome this has achieved. Had MAS not been operating in this space many consumers would have instead ended up speaking to a mortgage broker firm who would have actually been able to help the consumer with regulated advice. We understand that MAS's activities have now left it with a large number of mortgage related leads that it cannot, at this time, deal with effectively or fairly apportion to mortgage brokers. It has to be questioned why MAS is doing this, what outcome is it trying to achieve, are they the right outcomes and are they really being meet or is it simply meeting the targets it has set itself? A large marketing budget, used efficiently, will undoubtedly attract consumers to an organisation's website, however, if that website does not actually really help the consumer then what is it actually achieving?

<u>FSCS</u>

We would request that in the future all FSMA related fees and levies are contained within this annual consultation. Firms need to be aware of the full proposed costs. We believe that in the interest of transparency FCA should commit to including all related fees and levies in one consultation.

FSCS's fees remain a significant cost on the FCA invoice that mortgage brokers receive.

Value for money

Given the revenue collecting powers of the FCA it is essential that it provides value for money and that there are procedures put in place to independently check its funding. AMI continues to support the use of the Nation Audit Office to check FCA's spending.

There are no triggers or incentives for FCA, FOS, FSCS or MAS to reduce their costs. We believe that it essential that regulatory dividends exist for firms.

Cap

FCA has been able to set its budgets in relation to the resources it requires, unlike the companies it regulates it does not have to consider its budgets and then prioritise the work it will undertake.

Many other regulators are subject to caps or restrictions on their budgets. This helps to ensure that they are focused in the activities they undertake. We believe that FCA should be subject to similar caps on funding. A focused approach to regulation which is balanced against priorities and based on a defined budget could produce better outcomes than the current approach.

In particular we have noted over recent years significant growth in some support functions and would question their relevance and if they are appropriate for an industry funded regulator. We have noted apparent increases in the numbers of staff employed in areas such as internal communication, corporate communications, the press office, public affairs and government affairs. We are concerned about the necessity of such a large teams, what they are tasked with undertaking, and what the objective is. We are concerned about what they add in terms of value for money.

Accordingly we would ask for details on the historic and current numbers employed in these areas, together with their departmental budgets so that the industry can be confident that this is in their best interest.

<u>AMI's response to FCA regulated fees and levies: Rates proposed 2014/15</u>

Q1: Do you have any comments on the proposed FCA 2014/15 minimum fees and variable periodic fee rates for authorised firms?

We consider the overall level of fees to be excessive and punitive for our member firms. We support the retention of the minimum. It is essential that smaller firms with low income are not priced out of the Financial Services industry by the over-burdensome impact funding FCA.

We consider that there should only be one minimum fee to cover all advice permissions. There should not be a separate minimum fee for consumer credit.

Q2: Do you have any comments on the proposed FCA 2014/15 minimum fees and periodic fee rates for fee payers other than authorised firms?

No comment

Q3: Do you agree with our proposed FCA fee rates for consumer credit firms?

No. We welcome the decision to apply thresholds based on income. We are concerned that second charge mortgage brokers are still unclear as to how they will be regulated under the long-term mortgage regime. As such it is significantly difficult for them to plan what their regulatory costs will be for the foreseeable future.

As with first charge mortgage brokers, some second charge mortgage brokers will not derive any income for some consumer credit permissions. These were only held to meet OFT's loose requirements. This could see some seconds charge mortgage brokers incurring significant new costs disproportionate to the risk they generate.

Furthermore there should only be one minimum fee not a separate consumer credit one. Although this could still be tiered for certain sectors.

Q4: Do you agree with our proposed ombudsman service levy rates for consumer credit firms?

We are still unsure at this stage whether second charge mortgage brokers will be considered as consumer credit firm under CC2 or as mortgage brokers under industry block 16.

We would prefer the application of a simple flat fee. This approach works well for first charge mortgage brokers in industry block 16. The ombudsman service already applies a variable charging structure through the case fee system. We see no reason why two variable funding lines need to be applied.

Q5: Do you agree with our proposed Money Advice Service levy rates for consumer credit firms?

We welcome the provision of a £10 minimum fee in line with other parts of the industry.

Q6: Do you have any comments on our definition of the 'credit-broking merchant discount'?

No comment

Q7: Do you have any comments on the proposed method of calculating the tariff rates for firms in each fee block towards the CJ levy and our proposals for how the overall CJ levy should be apportioned?

We welcome the decision to freeze the flat levy for mortgage brokers at £85. The insurance mediation levy has produced a small increase but we welcome the retention of the £100 minimum fee.

Q8: Do you have any comments on the proposed 2014/15 Money Advice Service levy rates for money advice?

We welcome the decision to hold the cost of the Money Advice Service at £43m. Under its new funding model, which considers usage, outcomes and the FCA's levy, mortgage broker firms will see costs increase from £1m to £2.2m.

We welcome the revised approach to the way MAS's fees are collected. It is essential that MAS's fees are apportioned in an appropriate manner. The original method of allocating fees based solely on the FCA's fee blocks clearly did not meet MAS's needs. However, it is essential that MAS's funding structure is continually reviewed to ensure that the correct apportionment of costs is applied across the three tiers of the new structure.

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Q9: Do you have any comments on the proposed 2014/15 Money Advice Service levy rates for debt advice?

No comment.

AMI
19.05.14

Appendix

A small firm with £50k Mortgage and £30k insurance income

Regulatory Fees and Levies: 2005/2006 (final)

Financial Services Authority Periodic Fee:	£750.00
Financial Services Compensation Scheme Levy:	£20.44
Financial Ombudsman Service Levy:	£100.00
Total Fee	**£870.44**

Regulatory Fees and Levies: 2012/2013 (final)

Financial Services Authority Periodic Fee:	£988.00
Money Advice Service Periodic Fee:	£10.00
Financial Services Compensation Scheme Levy:	£711.77
Financial Ombudsman Service Levy:	£145.00
Total Fee	**£1,854.77**

Regulatory Fees and Levies: 2014/2015 (draft)

Financial Conduct Authority Periodic Fee:	£1000.00
Money Advice Service Periodic Fee:	£10.00
Financial Services Compensation Scheme Levy:	£406.87
Financial Ombudsman Service Levy:	£185.00
Total Fee	**£1,601.87**

A larger firm with £2m Mortgage and £1m insurance income

Regulatory Fees and Levies: 2005/2006 (final)

Financial Services Authority Periodic Fee:	£14,018.00
Financial Services Compensation Scheme Levy:	£535.65
Financial Ombudsman Service Levy:	£100.00
Total Fee	**£14,653.65**

Regulatory Fees and Levies: 2012/2013 (final)

Financial Services Authority Periodic Fee:	£22,849.20
Money Advice Service Periodic Fee:	£3,407.10
Financial Services Compensation Scheme Levy:	£24,909.70
Financial Ombudsman Service Levy:	£422.00
Total Fee	**£51,588.00**

Regulatory Fees and Levies: 2014/2015 (draft)

Financial Conduct Authority Periodic Fee:	£33,982.22
Money Advice Service Periodic Fee:	£4,562.40
Financial Services Compensation Scheme Levy:	£14,334.46
Financial Ombudsman Service Levy:	£602.30
Total Fee	**£53,481.38**