Association of Mortgage Intermediaries

Association of Mortgage Intermediaries' response to FCA DP18/09:
Fair pricing in financial services

This response is submitted on behalf of the Association of Mortgage Intermediaries (AMI) and the Association of Finance Brokers (AFB). AMI is the trade association representing over 80% of UK mortgage intermediaries. AFB sits within AMI and represents second charge (formerly secured loan) brokers.

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. AMI members also provide access to associated protection products. AFB members also provide access to unsecured products.

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

Response

Whilst we understand the diagnostic work that has led to the publication of this paper and acknowledge the focused work that the FCA is carrying out in the general insurance market, we do not think it is appropriate to extrapolate these concerns by considering remedies across all sectors without specific research and sufficient justification. The mortgage market has undergone substantial and continued regulatory change over the last five years. There is a real risk that further changes to a market which has only been able to recently start innovating will result in widespread consumer detriment as firms amend their business models or exit the market entirely. Thematic reviews, the Mortgages Market Study and continued supervision have found that the mortgage market is generally working well for consumers. The remedies that are being taken forward as part of the Study are addressing the few areas which are negatively impacting a small proportion of consumers.

We are concerned about the continued focus on price driving regulatory change rather than consideration of suitability and consumer needs. The remedies proposed would drastically change a well-functioning mortgage market which would ultimately lead to a disproportionate level of consumer harm that is not outweighed by the benefits. Consumers currently benefit from the wide range of options and features that different mortgage products offer and by restricting these there will be a significant proportion of customers either paying more for a suitable product or not being able to access a suitable product at all, compared to the proportion of customers that would benefit. For example, given the popularity of two year fixed products, any requirement that the initial term should be a specified length will only cause consumers who need a shorter term to be forced into a longer contract. A consumer might need a short initial term because they plan to move house in the near future. Exiting during an initial term usually gives rise to an early repayment charge, which is not only one reason why a consumer might remain on a Standard Variable Rate (SVR), but is one way in which consumers will be penalised for no longer being able to access a suitable product with a shorter initial term.

The very specific interplay between the capital requirements on lenders, their risk appetite and limitations on their lending capacity needs to be embraced. Whilst we appreciate the conduct issues and risks of consumer detriment debated in this paper, the significant dependence on prudential issues in the mortgage market needs to be considered. Additionally as the housing and mortgage market is such a significant economic factor, any interventions need to be carefully measured in a wider macro consideration.

It is not necessary for the FCA to become a product regulator, however it should enforce their existing rules around the responsibilities of providers when designing products and their target market, reiterated in the treating customers fairly outcomes, with regard to product manufacturers being more prescriptive on the need or not for advice.

We support increasing engagement with consumers so that they understand their financial products and services. We are concerned that the paper focuses on consumers being able to compare products themselves. It can be more appropriate for consumers to receive guidance or advice on certain products, particularly for long-term products such as mortgages and pensions where they will interact with these on an infrequent basis. Customer needs will change as will product characteristics during the contractual life of these products therefore the need to have the safeguard of advice is even more acute but also particularly for vulnerable consumers.

It cannot be ignored that lenders are already contacting trapped borrowers and offering to switch them to cheaper products. We would support increased prompts going forward for customers nearing the end of their initial mortgage term and for those who remain on the SVR. These information disclosures should include the need to obtain advice and how they can seek this from an intermediary. Lenders are restricted to advising on their own products and some customers who remain on SVR may not be aware that there are other options available to them. Intermediaries consider products from across multiple lenders when recommending a suitable mortgage. Making consumers aware of intermediaries and increasing prompts would mirror the annuity market where customers are encouraged to consider the open market option.

Questions

Q1. Do you agree with our six evidential questions to help assess concerns about fairness of individual price discrimination cases? Are there any other questions that are as, or more, important than the ones listed? If so, what are they?

We agree in principle, however this should not be considered in isolation. We refer to our comments made elsewhere.

Q2. Where consumers who shop around get good deals but those inert ones not shopping around do not, what factors should determine whether this trade-off is fair? In particular, to what extent are the following factors relevant:

- **a) The scale of the price differential between consumers?**
- **b) The characteristics of the consumers who are affected? In particular, is it only unfair when it is vulnerable consumers who lose out, or is it also unfair when non-vulnerable customers lose out? Can it also be unfair even when the vulnerable benefit?**
- **c) The reasons why existing consumers do not switch to a better deal?**
- **d) The transparency of firms' pricing practices?**

Consumers should be aware of when a higher reversion rate will apply to their mortgage payments, and reminders whilst they continue on a reversion rate for a period of time could help increase engagement. Vulnerable consumers should not be switching products without advice.

There can be a number of reasons why consumers remain on a reversion rate, including lack of awareness of advice or other products, an unwillingness to enter another contract due to a foreseeable change in circumstances or because of a short remaining mortgage term, or if their circumstances or regulation has changed since they took out the mortgage which makes them ineligible for another product. Given that the small proportion of trapped borrowers has directly resulted from changes in the affordability rules and that this issue is being addressed by the industry in conjunction with the FCA, we do not believe any remedies are warranted in the mortgage market.

Q3. To what extent is it appropriate for firms to target and tailor their pricing approach to consumers who are not likely to respond to future price rises? Does the answer depend on the techniques that firms use to achieve this (eg through predictive modelling, product design, communication with the consumer)? Please provide reasons to support your answer.

Whilst mortgages have many features, the vast range of products matches the greatly differing and complex needs and circumstances of consumers. Because there is also often a choice of suitable products, prices are competitive. By delivering this wide range of products based on such variables as loan-to-value, individual risk profile, employment characteristics or type of property, the rate can be varied according to risk meaning there is less cross-subsidisation. Advisers are essential in finding the most suitable product for consumers, who should not be expected to do this themselves. Therefore we cannot see a need to simplify the product itself, which would only marginalise a segment of the market as their needs would not be met. This could also lead to less differential pricing which would be detrimental to low risk consumers.

Q4. What should we expect firms to do to help reduce the cost to consumers of shopping around and, if necessary, switching to another provider, in particular with respect to:

- **a) helping consumers understand their choices**
- **b) the amount of effort required to make their choice**
- **c) not discouraging switching or shopping around**
- **d) being transparent about pricing and what factors are used to determine pricing**

Please provide reasons to support your answer.

This has been covered elsewhere in our response.

Q5. What should longstanding consumers be able to expect of their provider when they become inactive in that particular market? In particular what should be expected of:

- **a) the support the provider gives their customers to ensure they are making informed product choices?**
- **b) the default outcome in the event of prolonged inactivity (eg contract renewal, contract termination, or automatic switching to a different product)?**
- **c) the maximum price differential they are paying relative to the best available rate for that provider? Please provide reasons to support your answer.**

Suitability is the foundation of regulated advice, not price. Nuanced conversations about customers' needs and circumstances are key to an adviser's recommendation of a suitable product. Needs should not mean the cheapest product. Any automatic switching without advice would significantly increase the risk that a consumer will be worse off, and this would be more acute for those that are vulnerable.

Q6. On the discussion on potential remedies in this paper:

a) **Do you agree with the types of remedies that we have set out? If not, please explain which type of remedy you disagree with and why.**
b) **Are there other types of remedies that we should consider that do not fit into these categories? If so please explain them and what adverse effect you think they would remedy, mitigate or prevent.**
c) **Are there particular examples from other sectors, or other countries, that you think we should consider to inform our approach? If so, please provide detail and references where possible.**

We only support information disclosures as a potential remedy in the mortgage market, for reasons set out elsewhere in this response. These should make consumers aware of intermediaries so that their existing lender is not perceived to be the only option, as this may be a reason for their inertia. This could include signposting to the proposed independent directory of mortgage brokers.