Association of Mortgage Intermediaries' response to FCA CP21/36

A new Consumer Duty

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.

Our view

AMI remains supportive of the intention behind these proposals and welcomes clarifications made by the FCA in this second consultation paper; notably confirmation that it does not apply retrospectively, that no Private Right of Action (PROA) will attach to the Duty and the further detail that has been provided around scope. AMI is keen to continue to engage with the FCA and other stakeholders as work on the Consumer Duty develops.

We represent mortgage advice firms that we consider already work well in partnership with the manufacturing lenders and insurers. We see this regulatory realignment as significant additional work for a sector that has low inertia, low levels of substantive complaints and is highly competitive.

<u>Cost of implementation and extent of consumer harm in the mortgage market</u>

We are concerned that the consultation does not quantify the extent of harm that currently exists in retail markets, nor does it provide evidence on how the new Consumer Duty would have prevented harms of the past. With the Cost Benefit Analysis (CBA) estimating high one-off and ongoing costs to industry of £2.4bn and £176.2m respectively, this is a significant cost. We continue to believe that the costs of these proposals, which will have to be passed onto consumers through higher charges, far outweigh any potential benefits to consumers from the mitigation of harm delivered by these current proposals.

Implementation period

We feel given the significance of the Consumer Duty and the work that will be required by mortgage intermediary firms on an individual basis, as well as the work in conjunction with lenders to meet the price and value and products and services outcomes, a longer implementation period of two years, with an additional 12 month transitional period for distributors under the products and services and price and value outcomes, is essential. We include our justification for this throughout our response.

In addition, we are concerned by the combined impact of work required in this consultation and the activity caused by the work on the Appointed Representative regime (CP21/34: Improving the Appointed Representatives regime), on top of the on-going work from the GI and pure protection fair value activity (PS21/5 and PS21/11). In all firms we represent, changes will have to be driven by the same risk and compliance teams. We do not consider this to have been adequately considered and assessed and clear priorities established by the FCA.

It is unreasonable for the FCA to state that the draft rules and non-Handbook guidance published as part of CP21/36 provide enough clarity to allow firms to begin implementation. The Consumer Duty requires significant investment from our member firms in terms of time, money and resources. Firms must have confidence that the changes they are making adhere to the new requirements; however, they will not have absolute certainty until the finalised rules are published. We therefore request the FCA does not factor in the seven months between publication of the second consultation and final rules when considering a suitable implementation time period.

Risk of consumer financial exclusion

This consultation has raised concerns amongst members of the risk of consumer financial exclusion. It is our view that the FCA should be required to consider financial inclusion as part of its policy proposals. We have fed back our views on this as part of the response to the HMT future regulatory framework consultation and also include comments on the impact of FCA policy proposals on financial exclusion as part of this response. A nine month implementation period will exacerbate the issue, as firms could become more risk averse as they navigate the requirements in a short space of time. A two year implementation period, with a 12 month transitional period for distributors on products and services and price and value outcomes, should help reduce this risk.

FOS interpretation

It is important the FCA works closely with FOS on interpretation of the Consumer Duty to ensure that FOS does not take a broader interpretation than the FCA intended. FOS must remain independent and adjudicate as an alternative dispute resolution (ADR) service, rather than take a legalistic view that we have seen of late. We see a close working relationship between FOS and FCA as vital due to the outcomes based nature of the proposals and the level of uncertainty this will place on our member firms. We believe this is best facilitated through an FCA and FOS forum and for a feedback loop to be created to share insight with the wider industry.

The Consumer Duty comes at a time when FOS is proposing to significantly reduce the number of free cases available to a firm to three. As the Consumer Duty is outcomes based there is scope for wider interpretation. Maintaining the number of free cases at 25 will support both firms and consumers as published Ombudsman decisions on matters relating to the Consumer Duty will help provide firms with greater clarity on interpretation and expectations, in turn driving firms to improve consumer outcomes. Conversely, a reduced number of free cases may drive more firms to settle at the £750 case fee, potentially resulting in fewer Consumer Duty based complaints reaching Ombudsman stage. This would reduce the insight available to industry on how the Consumer Duty is interpreted and applied by FOS. With the FCA describing the Consumer Duty as iterative, we view access to past Ombudsman decisions as a crucial part of the process and ask the FCA to consider raising the risk of reducing the number of free cases with FOS directly, as we do not feel this has been adequately considered.

Understanding the gaps between TCF and the Consumer Duty

Further FCA case studies representing good and poor practice that span a wider range of markets, to include mortgage intermediary examples, would be welcomed. It would also be beneficial for the FCA to articulate the gaps between what was expected under TCF versus expectations under the new Consumer Duty by providing examples that demonstrate in various industry scenarios the difference between what a firm may have done under TCF that would not fulfil their obligations under the Consumer Duty. We see this as important to aid firms' understanding around the indicated paradigm shift from previous to new obligations.

We would also like to see the FCA run industry interactive pre and post implementation workshops for both trade bodies and firms. These operated well when the Mortgage Market Review (MMR) and the Mortgage Credit Directive (MCD) were introduced and we would like to see the same approach with the Consumer Duty.

Supervision and enforcement of the Consumer Duty

We remain of the view that increased and robust FCA supervision and enforcement is key to the success of the Consumer Duty. The SM&CR is designed to hold Senior Managers more accountable and responsible for their conduct and actions. However, we are yet to see widespread evidence of the FCA holding senior individuals to account within "poor" performing firms. We are concerned that firms engaging in practices the Consumer Duty is trying to prevent (such as sludge practices and leveraging consumer behavioural or cognitive biases for their own gain) are likely to continue undeterred, whereas well run, responsible firms will do all they can – and more – to ensure compliance. It is therefore important for the FCA to fully utilise existing regulation and regulatory powers, such as the SM&CR, to achieve the intended aims and benefits of the Consumer Duty. We are not confident this is being done at present.

AMI believes the FCA needs to increase 'feet on the ground' supervision to supervise and enforce the Consumer Duty effectively. FCA Supervisors need to experience and appreciate the culture of a firm, its employees and senior management and gain a deeper understanding of the application of these new rules and guidance in live environments and how this influences and drives consumer outcomes. The FCA's current proposals on supervision and enforcement will monitor firms based on outputs and not necessarily outcomes. 'Feet on the ground' supervision would show clear intent from the FCA in line with its aim to become a more assertive regulator.

Questions

Q1: Do you have any comments on the proposed scope of the Consumer Duty?

We are grateful the FCA has confirmed that the scope of the Consumer Duty will follow the definition of retail clients in the relevant sectoral Handbook and therefore will not apply to unregulated buy-to-let mortgage contracts or commercial mortgages. However, section 2.36 of the draft non-Handbook guidance states that the Consumer Duty applies to authorised firms conducting ancillary activities, with ancillary activities referred to as 'unregulated activities in connection with, or for the purposes of, regulated activities'. Does this therefore inadvertently capture a scenario where a mortgage intermediary firm, as an example, arranges a regulated mortgage and an unregulated buy-to-let (i.e. commercial buy to let) for the same customer? We would be grateful for clarification. This is necessary as we are not certain this meets the direction of travel in the expansion of scope being considered as part of the two Appointed Representative consultations being conducted by Treasury and FCA.

We agree the Consumer Duty should apply to all firms that can influence material aspects of the design, target market or performance of a retail financial services product or service. We also agree that the Consumer Duty should apply to both prospective and actual retail customers. This should help embed behaviours and culture throughout a firm and across all its activities.

We are supportive of the FCA's draft rules which confirm where firms already meet existing product governance rules, these will tend to establish compliance with their obligations under the products and services and price and value outcome. The rules as drafted avoid some duplication of work for applicable products and services. For the mortgage intermediary sector, firms involved in GI and pure protection are already subject to the enhanced product governance in PROD 4 for these products and services. However, as the Consumer Duty goes further than the requirements under PROD 4, firms will still need to ensure they are meeting the Consumer Duty as a whole on these products and services. This will require further work by firms to build on existing frameworks.

We consider that, broadly, firms in the mortgage sector are adhering to the "duty", but there will be significant effort and cost in building systems and controls to evidence this. We ask the FCA to be mindful of this when considering our request for an extended implementation period.

Q2: Do you have any comments on the proposed application of the Consumer Duty through the distribution chain and on the related draft rules and non-Handbook guidance?

We welcome confirmation that all authorised firms would need to comply with the Consumer Duty for retail business for their own activities and therefore would be responsible only for their own activities and would not need to oversee the actions of other firms in the distribution chain. However, please also refer to our comments to question 10.

We do not agree with the FCA's assertion in the consultation that it would generally expect firms with a direct relationship with the customer to have the greatest responsibility under the Consumer Duty. We feel this statement risks diluting the obligations of manufacturers, particularly under the price and value and products and services outcomes where many of the requirements are manufacturer led and distributors will rely on the quality of these value assessments to make their own judgements around fair value. We feel it would be more appropriate for FCA to use the word 'greater' rather than 'greatest'.

Following the introduction of TCF, AMI, CML and IMLA worked together to create the 'Working Together' document, an industry guide to lender and intermediary accountabilities and responsibilities in mortgage sales and servicing. The guidance aligns with the FCA's current requirements and relevant Handbook rules and sets out good market practice, with the aim that the relationships in which lenders and intermediaries are engaged deliver good customer outcomes. The 'Working Together' document does not consider commercial relationships between lenders and intermediaries; these are the subject of separate legal agreements between the parties reflecting their own circumstances.

AMI envisages the 'Working Together' document will be updated by AMI and respective parties to reflect manufacturer and distributor obligations under the Consumer Duty. However, we cannot commence this work until we have complete certainty on finalised FCA rules and guidance. We feel a nine month implementation period is insufficient time for this task to be carried out, given the need to involve other trade associations and members from each respective trade association to provide input and guidance. Member firms will only be able to provide valuable insight and contributions, particularly on the products and services and price and value outcomes, once they have assessed and applied the final rules and guidance at individual firm level.

Q3: Do you have any comments on the proposed application of the Consumer Duty to existing products and services, and on the related draft rules and non-Handbook guidance?

AMI agrees that the Consumer Duty should not apply retrospectively. This is an important point as firms should only be judged on their conduct and behaviour from the date the rules come into force.

We are supportive of the FCA's comments (2.26 draft non-Handbook guidance) that firms would not be expected to apply rules that are not relevant for closed products or services. It is important that firms are afforded the flexibility to apply the Consumer Duty to closed books in a proportionate manner.

Q4: Are there any obstacles that would prevent firms from following our proposed approach to applying the Consumer Duty to existing products and services?

We ask for clarification on the extent of a distributor's responsibilities with closed products and services. The draft rules are clear on the requirements placed on manufacturers, for example 2A.3.5 R (1) requires manufacturers to view their products through the lens of the cross-cutting rules but is less clear with regard to intermediaries (acting as distributors) that have existing customers with a closed book product. Further guidance on this in the draft non-Handbook guidance would be appreciated.

We agree with the FCA's assertion that the products and services and price and value outcomes cannot be so easily applied on a forward-looking basis to existing contracts that are no longer being sold or renewed.

We ask the FCA for clarification on expectations for both manufacturers and distributors with regards 'superseded' products, such as a critical illness policy sold years ago where products may have progressed (i.e. through upgrades) but existing policies are not under regular review. With protection products assessed on a customer's health and pre-existing medical conditions, firms may not be able to amend existing contracts without implications on a customer's insurance cover. For example, a customer may have incepted cover on a critical illness policy 15 years ago and in this period claimed on the policy and received a pay-out. However, if the same insurer moved the policy to a new contract this could result in the application of an exclusion, resulting in a poor customer outcome.

There are also occasions where an Appointed Representative (AR) closes and customers may not be picked up by another network. Does the responsibility under the Consumer Duty lie with the network that was the principal firm at the time the product was sold to the customer?

Dependent on the extent of application to distributors, it is likely that the biggest obstacle under this section is the nine month implementation period.

Q5: Do you have any comments on the proposed Consumer Principle and the related draft rules and non-Handbook guidance?

We agree with the proposed Consumer Principle ("a firm must act to deliver good outcomes for retail clients") as it sets a clear, higher standard than under Principles 6 and 7. We raised concerns in our first consultation response that a Principle based on best interests could inadvertently create a fiduciary duty.

The draft non-Handbook guidance makes it clear that Principle 12 does not mean that individuals will always get good outcomes, or always be protected from poor outcomes. We feel this point should be part of the FCA's Handbook guidance under 2A.1 (Application and purpose). What constitutes a 'good outcome' is subjective and this therefore ought to be included in the FCA Handbook guidance to prevent ambiguity over the extent of a firm's responsibility and to make the FCA's expectations clear from the outset.

We ask the FCA for clarification as to how FOS would view the FCA non-Handbook guidance when assessing a complaint. As the non-Handbook guidance is a guide to the FCA's view on how Principle 12 and PRIN 2A should be complied with, we believe FOS should be required to take it into consideration as part of its complaints assessment. For example, section 3.0 of the draft non-Handbook guidance expands on expectations around 'reasonable application' of the Consumer Duty. This is important in the event of a complaint and we are concerned that without consideration of non-Handbook guidance, FOS could take a stricter interpretation than intended on whether a good customer outcome had been achieved. As an example, a mortgage adviser recommends a five year fixed rate to a customer on a tight budget that is looking for stability, however mortgage rates fall considerably within the five years. The recommendation allowed the customer to meet their financial objectives (to live in the property) and avoided causing foreseeable harm (monthly payment stability for five years within the customer's budget) but it could be argued, without due consideration given to non-Handbook guidance as drafted, that they may have received a better outcome from a two year product.

Q6: Do you agree with our proposal to disapply Principles 6 & 7 where the Consumer Duty applies?

Yes, given that PRIN 12 places higher standards on firms then it makes sense for PRIN 6 and 7 to disapply as the requirements under the Consumer Duty go much further than existing requirements.

We assume that where PRIN 6 is disapplied this also results in the disapplication of the Treating Customers Fairly outcomes. However, it is not clear in the consultation and draft rules. We therefore ask the FCA to make this explicit in the final rules to avoid any confusion.

We ask the FCA to make clearer its expectations on how the Consumer Duty interacts with TCF (i.e. in situations where PRIN 6 disapplies). For example, will firms be expected to "unwind" TCF frameworks, processes and controls or is the intention that firms should build on their TCF existing work to ensure they meet their obligations under the Consumer Duty and achieve and evidence good customer outcomes?

Q7: Do you agree with our proposal to retain Handbook and non-Handbook material related to Principles 6 and 7 should remain relevant to firms considering their obligations under the Consumer Duty?

No, we do not agree. Principles 6 and 7 and the TCF outcomes are embedded within firms' processes, behaviours and cultures and by retaining the Handbook and non-Handbook material related to Principles 6 and 7, risk causing confusion for customers and firms over the purpose and intent behind the Consumer Duty. It creates a layering of regulation which is unhelpful.

Handbook related examples include MCOBS section 3A.2.1 which requires firms to communicate in a way that is fair, clear and not misleading and MCOBS 11.5.1 which requires firms to treat customers fairly. A non-Handbook example includes the FCA's finalised guidance for firms on the fair treatment of vulnerable customers that refers to PRIN 6.

It has been suggested the FCA may make Handbook changes (e.g. to MCOBS) and publish these as part of the Consumer Duty Policy Statement and final rules. In no circumstances should this be allowed to happen; **any wider Handbook amendments must be subject to full and proper industry consultation before changes are made.**

We believe a full review of the Handbook and associated documentation is sufficiently urgent to require a longer implementation period of two years. This will allow the FCA to carry out a review of the Handbook and associated documentation efficiently and fairly, rather than a review taking place in a piecemeal fashion and without appropriate industry engagement and consultation. With the Consumer Duty representing a 'paradigm shift' it is only appropriate for the FCA to ensure it too commits to full and thorough implementation.

Q8: Do you have any comments on our proposed cross-cutting rules and the related draft rules and non-Handbook guidance?

AMI is grateful that the FCA has removed 'all reasonable steps' from the foreseeable harm and financial objectives rules as we were concerned that this would result in firms focusing more on processes rather than outcomes, resulting in significant documentation by firms to achieve compliance.

It is our view that out of all the cross-cutting rules, the 'avoiding foreseeable harm' rule is likely to be the most subjective, particularly should a complaint arrive at FOS. We believe the draft rule (2A.2.5 R) must be amended to read 'a firm must avoid *causing* foreseeable harm to retail customers' as this reflects the FCA's comments in the consultation that firms should be both proactive and reactive to avoid causing harm *where it is in a firm's control to do so*. We query why throughout the policy statement the FCA includes the word 'causing' but in the draft rules this is notably absent.

With the word 'causing' omitted, this rule as drafted does not clearly articulate to firms and consumers that a firm does not have a responsibility to prevent all harms and risks creating unreasonable expectations and misinterpretation by FOS. By making this change it should clarify that accountability rests with the firm creating the harm, as opposed to others involved in manufacture or distribution that could be linked vicariously. Not doing this risks making PII prohibitively expensive, or potentially unobtainable, for distribution models.

Draft guidance 2A.2.8 G states that a firm which is involved with the provision of a product at a point in time and without an ongoing relationship with the retail customer does not need to act to avoid harm which only later becomes foreseeable. We feel this lacks precision and the FCA should more clearly articulate what it means by an ongoing relationship for firms that distribute multiple products. For example, a mortgage intermediary firm could arrange a mortgage for a customer on a five year fix and would not be required to review the mortgage product but may contact the customer within the five year period for example to review the customer's protection cover. Would this then capture the firm under 2A.2.7 G, requiring the firm to act to avoid foreseeable harm in respect of both the mortgage and protection product(s)? If this was the case, then this would create an unreasonable expectation and liability on advisory distribution firms.

We agree with the FCA's addition of the word 'support' to create the draft rule '*a firm must enable and support retail customers to pursue their financial objectives*', as this is better aligned to the advice role of mortgage intermediary firms. However, we are concerned with the extent of a firm's obligations under this cross-cutting rule. It is unclear in the drafted rules whether a mortgage intermediary firm as an advice firm would be required to support customers to achieve financial objectives outside of a firm's scope of service and/or permissions. We would appreciate clarification.

For example, if a mortgage intermediary has mortgage, GI and protection permissions and a customer stated that one of their financial objectives was to protect their family financially should they pass away, we can see how a prudent firm, based on the concept of reasonableness, would be required to enable and support the customer in pursuing this because they have the regulatory permission to engage in this product. Whereas a customer could, as an example, have a financial objective to hold sufficient funds in retirement, meaning the mortgage must be cleared, but would a firm be required to enable and support the customer on the pensions savings aspect?

We envisage this is not the FCA's intention given its comments that this cross-cutting rule does not require firms to go beyond what is reasonably expected by consumers in the delivery of their service.

However, we would be grateful for clarification from the FCA on the expectations under this rule and this ought to be made explicitly clear in the Handbook and non-Handbook guidance, with relevant case study examples. It is important that this new rule will continue to permit firms to work within their current disclosure as is currently allowed. The new rules must facilitate the limitations that firms are able to currently apply to limit the scope of their service and the range of providers they engage with, provided this is adequately disclosed and understood. It should be clear that a firm is responsible for providing good outcomes within the limits of the permissions they hold and the products a firm provides advice on within its regulatory scope.

We would also welcome clarity from the FCA on the extent of a firm's obligations to enable and support a customer to pursue their financial objectives that relate to a product that falls within its scope of service. If a mortgage intermediary firm has an insurance distribution permission and is aware of a customer's financial objective that relates to particular insurances (such as GI or protection) but due to circumstances cannot assist, would the firm be required to signpost to a firm that can help? Would the firm that signposted a consumer to another firm or referral service (such as BIBA 'Find a Broker') be responsible if the consumer received a poor outcome i.e. how far does the responsibility go? We consider this risks imposing a liability that could reduce the permissions firms hold, limit competition and reduce choice for consumers.

Intermediary advice firms also require clarity on where the boundary lies on any product meeting their reasonable expectations during its life. If due to actions of the provider it veers away from an expected outcome, is responsibility solely with the provider? Does the distributor hold an on-going monitoring responsibility?

We agree that an additional cross-cutting rule that focuses on vulnerable consumers is not necessary. We feel the FCA's approach to require firms to embed consideration of vulnerable consumers throughout the customer journey is the right one, as this should ensure that firms do not focus on vulnerable consumers in isolation but consider the changing nature of consumer vulnerability.

Q9: Do you have any comments on our proposed requirements under the products and services outcome and the related draft rules and non-Handbook guidance?

AMI highlighted in its response to the FCA's first consultation that this is a fundamental change for the financial services industry. Having reviewed the draft rules, we are still of this opinion and believe that the products and services outcome, along with the price and value outcome, has the potential to have the greatest impact on the mortgage sector out of all the four outcomes.

We are concerned that manufacturers (such as lenders) may reduce the number of intermediaries used to distribute their products due to the enhanced regulatory responsibility and oversight placed on them. Manufacturers may favour larger intermediary firms, which could dramatically alter the distribution landscape in the mortgage sector. This will impact competition as firms may no longer be whole of market, limiting consumer choice and resulting in greater segmentation of skill sets amongst firms.

It could also cause wider unintended consumer harm for example many smaller Directly Authorised mortgage intermediary firms are run by individuals from an ethnic minority who set up their firms as they did not feel they fitted in within larger firms (as highlighted in AMI's 2021 Diversity, inclusivity and equity Viewpoint[1]). Many of these firms also serve consumers within the local community from an ethnic minority background and therefore the loss of these smaller firms could reduce consumer choice and increase the risk of financial exclusion.

Manufacturers may reduce the numbers of products, as marginally profitable products become commercially unviable due to the breadth and depth of the products and services requirements at individual product level. We are concerned this could result in reduced competition and innovation and risks consumer financial exclusion. Distributors, particularly smaller intermediary firms, may be forced

[1] Final-Viewpoint-DI-Report.pdf (a-m-i.org.uk)

to reduce the number of lenders on panel, given the obligations required under draft rules 2A.3.19 R and 2A.3.22 R (as examples) which apply to every product distributed by the intermediary firm. If this occurred, it may reduce consumer choice and increase the risk of financial exclusion.

We consider that the mortgage distribution sector and their lender partners are already exemplars in the way they work together to deliver good products and ensure poor advisers are removed from the industry. AMI would state that if we are concerned about the impact of these proposals on our sector, then others will have to see a seismic change in relationships. We do not consider the consultation sufficiently measures the likely impacts on the number of products and players in the distribution chain that will occur from these changes.

The products and service outcome (and price and value outcome) are the outcomes that will benefit most from an iterative implementation process. Firstly, it will take time for manufacturers and distributors to apportion their responsibilities under the Consumer Duty. Secondly, this outcome is largely manufacturer led, as distributors are reliant on manufacturers supplying information to inform their own value assessments and meet their obligations as distributors. It will require manufacturers and distributors to work closely together and is viewed by our members as an extensive undertaking as they distribute products from a significant number of lenders (for many intermediary firms this in excess of fifty) and lenders tend to have more granular products compared to, for example, insurance manufacturers.

To enable firms to understand and implement the rules as drafted ahead of a final implementation date, it is our view that a longer implementation period of a minimum two years is necessary, with a 12 month transitional period applied to distributors. A transitional period is essential under this outcome as distributors are reliant on manufacturers to supply information on the product, its target market and its intended distribution strategy first before they can meet their own obligations. By staggering the implementation deadline between manufacturers and distributors it provides a clear demarcation of deadlines and reduces the risk of manufacturers supplying relevant information to the distributor at or near the implementation deadline (potentially reducing the time distributors have to take the manufacturer's information and ensure products are distributed appropriately). It is also not a level playing field to provide GI and pure protection firms with a transitional period (under PS21/5) but not include this for other retail financial services sectors that are captured as part of these proposals. A transitional period of 12 months should apply in addition to our suggestion for a 'core' implementation period of two years.

Our members have experience of the enhanced product governance requirements applying to GI and pure protection products, which has required manufacturers and distributors to work together in a similar manner. Based on this insight, we believe a timeframe of less than two years is too tight for this work to be co-ordinated and implemented effectively.

Q10: Do you have any comments on our proposed requirements under the price and value outcome and the related draft rules and non-Handbook guidance?

We are grateful for the FCA's clarification that fair value is more than just price; this is an important point as advice firms assess overall suitability of a product and the re-wording of the outcome from *fair value* to *price and value* should help encourage firms to consider the relationship between price and benefits of a product.

Paragraph 6.34 of the draft non-Handbook guidance states that the firm at the end of the distribution chain has responsibility to ensure consumers do not receive poor value. Whilst distributors are required to consider minimum information as part of understanding the value assessment (draft rule 2A.4.9 R), the non-Handbook guidance as drafted goes beyond the rules, creating ambiguity. In our view, the responsibility to ensure fair value should apply equally to manufacturers and distributors and the extent of this responsibility should rest with each part of the chain, on areas they can influence and control. This draft non Handbook guidance text seems to be at odds with the FCA's clarification that firms are

generally responsible only for their own activities and would not need to oversee the actions of other firms in the chain.

Under 6.38 of the draft non-Handbook guidance the example states that 'when considering whether a mortgage offers fair value, firms should consider the overall price of a mortgage including any initial discounted rate, fees and charges and the reversion rate applicable at the end of a fixed rate period'. Whilst this example is provided in the context of the 'consumer support' and 'consumer understanding' outcomes we are very concerned that the FCA has effectively prescribed what firms should consider under fair value for mortgage products; whereas the draft rules intentionally allow firms to make their own assessments as to what constitutes fair value using minimum considerations that are more general than in the example (e.g. 2A.4.7 R). Firms should not be required to consider a reversion rate (such as SVR) as part of fair value assessments. As this example is not appropriate, we request it is removed from the non-Handbook guidance.

Mortgage intermediary firms are required, under FCA rules, to apply the 'cheapest rule' when there is more than one product available to the customer that suits their needs. Then, if the cheapest of these products is not recommended, the firm must ensure that the reasons for this have been explained to the customer and evidence of the reasons for recommendation must be maintained on file. The price and value requirements apply another layer of regulation that mortgage intermediary firms will need to integrate into existing frameworks and processes, factor into advice and evidence and monitor on every sale. We would also question whether the FCA 'cheapest rule' is still appropriate given that fair value refers to more than just price and risks creating conflicting messages between firms and consumers.

We remain concerned that the price and value requirements could result in firms reducing the number of products in their ranges to ensure they can undertake value assessments for each of their products to the standard the FCA requires. This could reduce choice for consumers and have the unintended consequence of stifling innovation and competition and increases the risk of consumer financial exclusion. Mortgage intermediary firms play an important role in providing access to financial services (e.g. to mortgage and insurance products) and therefore a contraction in the number of manufacturers and/or number of products available will have an adverse effect on the solutions a firm is able to provide to consumers.

We do not consider the cost of evidencing these assessments through regular rigorous processes has been adequately factored into the costs and reduction in competition. These changes will make it significantly harder for new entrants to make inroads into established markets.

AMI member firms involved in GI and pure protection business have experienced the FCA's enhanced product governance fair value rules relating to GI and pure protection products (PROD 4). As part of this work, both manufacturers and distributors are required to share information to assess fair value. Equipped with this insight, we are concerned that in the mortgage space where intermediary firms tend to deal with a higher number of lenders with a higher ratio of products compared to the insurance space, smaller mortgage intermediary firms may be overly burdened by information supplied by the manufacturer (required under draft rule 2A.4.21 R and to meet requirements as a distributor under draft rule 2A.4.8 R).

The FCA gives assurances that its rules are designed to be proportionate but we feel the requirements under the price and value outcome disproportionately affect smaller firms, particularly when we consider the proposal for a nine month implementation period. Smaller firms do not have the same level of resources and infrastructure as larger firms to be able to effectively manage this. There is no mention of a transitional period for the price and value outcome in the consultation nor the draft rules, whereas under the GI and pure protection enhanced product governance requirements (PS21/5) firms have until 30 September 2022 to apply the updated approval process under PROD 4. It is not a level playing field to provide GI and pure protection firms with a transitional period but not include this for other retail financial services sectors that are captured as part of these proposals.

We feel the solution is to apply a longer implementation period of two years, as this would allow the mortgage industry to work collectively to plan and communicate timeframes and avoid a situation where smaller firms are inundated. The price and value outcome should have a transitional period applied, giving distributors 12 months from the date the rules come into force to achieve full compliance.

This is necessary under this outcome as distributors are reliant on a manufacturer's value assessment to meet their own obligations. Our member firms have experience of the enhanced product governance requirements that came into force on GI and pure protection products and are concerned that without a transitional period applying to distributors, there is the risk that manufacturers provide information at or near the implementation deadline and therefore distributors are not provided sufficient time to carry out their own value assessments. This is by no means a reflection on the processes and procedures of manufacturers, rather the complexities of this outcome which will require a one-to-one approach between a manufacturer and distributor. Manufacturers will be unable to take a homogeneous approach, as the nature of the proposed requirements will require them to review individual contract/commercial agreements with distributors. We have seen this first-hand as part of fair value assessments in the GI and pure protection space where product manufacturers (insurers) have approached distributors (intermediaries) on an individual basis to request information and where necessary, review contracts. When we consider on the mortgage side there are circa 100 lenders and circa 5,000 mortgage intermediary firms, the scale of the task and time needed to complete is considerable.

A transitional period should apply in addition to our suggestion of a 'core' implementation period of two years.

Q11: Do you have any comments on our proposed requirements under the consumer understanding outcome and the related draft rules and non-Handbook guidance?

We agree with the proposal to re-name this outcome 'consumer understanding', as this clearly differentiates the outcome from Principle 7.

We do not feel the FCA has adequately considered how the consumer understanding outcome will operate in the mortgage intermediary market. In the mortgage market it is the solicitor and not the mortgage intermediary that will go through the mortgage contract with the customer (compared to other intermediated markets such as insurance where typically the insurance broker would highlight policy exclusions and onerous provisions). The mortgage intermediary would not see the mortgage contract document. We therefore ask for clarification on who in the distribution chain is primarily responsible for this outcome.

The FCA has made it clear in the consultation and draft non-Handbook guidance that firms will not be expected to verify that all individual consumers have in fact understood the information provided by a firm. We agree with this approach, as it would be too onerous and difficult to achieve in practice. However, we are concerned that this is contradicted by draft rule 2A.5.7 R which requires firms when interacting directly with a retail customer on a one-to-one basis to check the retail customer understands the information, particularly if the information is reasonably regarded as key information, such as where it prompts that retail customer to make a decision (section two of the draft rule).

Mortgage intermediary firms, in most circumstances, would always deal with a customer on a one-to-one basis and therefore we have interpreted that this rule could potentially apply to all of their communications. We strongly disagree with rule 2A.5.7R as drafted. It is impractical, especially as mortgage intermediaries have to use a prescriptively worded ESIS produced by the manufacturer and as noted in our previous comment, do not discuss the mortgage contract with the customer. It unfairly places a standard of care on firms that goes beyond general expectations under the Consumer Duty.

It also risks unintended consequences that conflict with the objectives of the Consumer Duty, such as by introducing a moral hazard where customers do not take responsibility for their own actions and decisions, introducing unnecessary friction into the advice process and increasing mortgage intermediary firms' PII premiums and terms due to the open-ended nature of the requirement. There is the potential for significant ramifications at FOS level should a customer complain that it did not understand or challenges the firm that it did not go far enough to check their individual understanding. This risks placing a burden of proof of understanding on firms that will be prohibitive.

We are concerned that the draft rules and guidance are more subjective than existing regulation. We are concerned with the higher bar placed on firms to ensure that their communications are likely to be understood by the average retail customer intended to receive the communication. We feel this is a difficult assessment for mortgage intermediary firms to make, particularly when these firms deal with a range of different customers and therefore their customer base is so broad.

Draft rule PRIN 2A.7.2 requires firms, in the context of an "average retail customer" to consider a particular retail customer's needs or characteristics, including characteristics of vulnerability. We do not feel the use of the phrase "average retail customer" is appropriate, as it encapsulates such a broad spectrum of customers that firms will find it difficult to determine an "average retail customer". In addition, as firms are already required to ensure they deal properly with those with vulnerability, we are unclear as to the value of this addition.

In our response to the FCA's first consultation we highlighted improvements could be made to FCA mandated communications. We feel that all mandated FCA communications should be reviewed by the FCA to ensure, where possible, they aim to meet the requirements of the consumer understanding outcome. For example, the required explanation of the FCA cheapest rule, particularly where the product designated as the 'cheapest' by the FCA's rule, is often not actually the cheapest product for the consumer. This often results in a mortgage intermediary firm calculating the 'cheapest' product in two different ways to both comply with the rule and calculate the 'true cost' of the product over the incentive term. This can cause confusion amongst consumers. Another example is the ESIS, which is viewed by many as harder for consumers to understand compared to the KFI. Although the Consumer Understanding outcome encourages firms to think more widely about the purpose of their communications and the outcomes they are focused on, the extent to which firms can do this will be hindered by existing requirements and regulations.

Q12: Do you have any comments on our proposed requirements under the consumer support outcome and the related draft rules and non-Handbook guidance?

We are supportive of the objectives under this outcome. However, we ask the FCA to clarify who is primarily responsible for the consumer support outcome where an intermediary is involved and there is a distribution chain. In the mortgage intermediary market, the intermediary is responsible for the advice but the manufacturer (lender) is responsible for the servicing of the mortgage. We request the FCA expands its case studies to provide examples of how the consumer support outcome might be applied in the mortgage intermediary market and its expectations of intermediary firms, as current examples are limited to direct to customer models.

Our interpretation is that this would require manufacturers to support intermediaries in the same way they would support a customer. For example, if a customer is using a mortgage intermediary to review their options at the end of the initial term the lender would need to provide the product transfer options to the adviser and would not be able to solely require the customer to contact the lender directly. Otherwise, based on our interpretation, this could be seen as an unreasonable barrier to a customer exercising its rights or options in relation to the product or could be seen to be inhibiting the customer from pursuing their financial objectives (should the customer want advice from a mortgage intermediary firm).

There are examples of some lenders allowing a customer to terminate a fixed rate loan before the end of the incentive period by transferring to a new loan without paying the early repayment charge (ERC). This initial mortgage may have been advised by an intermediary and the "costs" amortised over the full term of incentive period. The new loan is often deemed to be "execution only", with the ERC not able to be waived if the initial advising intermediary becomes involved. We would like clarity that where a lender offers such terms then it should be open to consumer representatives, not just direct.

Q13: Do you think the draft rules and related non-Handbook guidance do enough to ensure firms consider the diverse needs of consumers?

We feel the rules are sufficiently adequate to ensure firms consider vulnerable customers and the diverse needs of consumers with different characteristics.

Please also refer to our comments to question 14.

Q14: Do you have views on the desirability of the further potential changes outlined in paragraph 11.19?

We do not feel it is necessary for the FCA to make more explicit reference to diversity and inclusion within each of the main elements of the Consumer Duty. However, our member firms would benefit from guidance on the interaction between diversity characteristics and the FCA's existing definition of vulnerability.

It is challenging for firms to go further with diversity and inclusion as they may not have the necessary expertise within the business. We would expect the FCA to evolve its thinking and expectations of firms on diversity and inclusion in its forthcoming consultation paper and it should therefore not seek to go further as part of its Consumer Duty work. We are concerned that based on the FCA's draft non-Handbook guidance (paragraph 2A.1.6) firms may blur socioeconomic and D&I factors with vulnerability, which is both unhelpful and potentially discriminatory.

As a trade body representing mortgage advice firms we are committed to the benefits consumers receive from the advisory process. A proper fact find and documented sales process with good literature or call recording ensures the vulnerable are properly assessed and supported. Where this fails the full weight of FCA, FOS and FSCS is there to support. We remain concerned by those who use the rules to circumvent advice and the support processes via shortcuts or use of non-advised or execution only to avoid liability. This applies in both manufacturing and distribution. We have always supported that those with vulnerable characteristics would benefit from an advised process with the appropriate protections.

Q15: Do you agree with our proposal not to attach a private right of action to any aspects of the Consumer Duty at this time?

Yes, we agree. We remain of the view that a private right of action is unnecessary as there are many existing ways for consumers to seek redress, at no cost to the consumer: through complaints to firms, to the Ombudsman and to the Compensation Scheme.

Q16: Do you have any comments on our proposed implementation timetable?

As highlighted throughout our response, AMI is of the opinion that a nine month implementation period is too short. We believe a minimum two year implementation period is necessary, with an additional 12 month transitional period for distributors under the products and services and price and value outcomes Please refer to our answers to consultation questions 9 and 10 for further explanation as to why we feel this is essential.

With the application of the customer's best interest rule in the Mortgage Conduct of Business Sourcebook (MCOBS) and the Insurance Conduct of Business Sourcebook (ICOBS); the requirements emanating from the Insurance Distribution Directive (IDD); and the enhanced GI and pure protection product governance requirements from the FCA's GI pricing work, mortgage intermediary firms are likely to satisfy, or be closer to satisfying, obligations under the Consumer Duty compared to some other financial services sectors. However, all mortgage intermediary firms will have further work to do to meet and evidence the new standard expected even if they feel they are already meeting the 'spirit' of the rules. Intermediaries that distribute products already subject to enhanced product governance rules (such as GI and pure protection, distributed by the majority of our members) will still need to undertake further work to examine where the differences lie between PROD 4 and requirements under PRIN 2A.

Overall, the breadth and depth of the Consumer Duty is extensive, with the interconnection between the cross-cutting rules and four outcomes adding layered thinking that will take time for firms to navigate and embed. It is a detailed suite of measures that is more extensive and, in some areas, more prescriptive than TCF which will take considerable time and investment from firms to digest, understand and apply to achieve the desired outcomes. Now that the FCA has provided draft rules we have a better understanding of the extent of work that will be required within the mortgage intermediary sector to ensure that firms meet their new obligations.

To provide specific examples, our member firms will, at a minimum, need to:

- Review and interpret the new rules, guidance and non-Handbook guidance and examine against existing rules. Currently the whole of the PRIN Handbook is around 40 pages yet draft PRIN 2A ("the Consumer Duty") in isolation is circa 30 pages, with additional Handbook material bringing the total of new material to circa 50 pages – this highlights the extent of change to the FCA rulebook. Firms will not have certainty on the final rules and guidance until the Policy Statement is published.
- Carry out a gap analysis to assess against existing policies and processes and determine where further work is required.
- Set up and run internal projects. This will involve IT projects that take considerable time and resource to execute.
- Undertake considerable work to ensure the four outcomes are met. In AMI's view the greatest amount of work for our member firms will stem from the products and services and price and value outcome where intermediaries (as distributors) will need to work with lenders to share and obtain information (products and services outcome) and understand the value assessment and outcome for every product they distribute (price and value outcome).
- Review customer communications and documentation.
- Consider resourcing needs and, if necessary, recruit further staff in what is a competitive and candidate driven recruitment market.
- Decide which MI is required to monitor, assess and evidence consumer outcomes. This is likely to involve the creation of new MI.
- Implement system changes.
- Communicate changes with staff.
- Train staff on the components of the Consumer Duty, how this differs to TCF and their obligations and responsibilities under the new Conduct Rule.
- Provide training and support for Senior Managers to ensure they understand their obligations.

- Make changes to Senior Manager's Statements of Responsibility and responsibility maps.
- Apply appropriate training to certified persons.

In addition, the Consumer Duty work carried out by firms will, for firms that operate as networks, take place at the same time as work that flows out of FCA CP21/34: Improving the Appointed Representatives regime and the ongoing work related to FCA PS21/3 Building operational resilience. Both the Consumer Duty and the AR regime review are significant pieces of regulatory work that will require extensive resources from the same business areas. We feel an extended implementation timeframe of two years, with a 12 month transitional period on price and value and products and services outcomes, is necessary to help alleviate pressure on firms. We are concerned that a shorter implementation period will result in both manufacturers and distributors limiting their panels as a short-term risk averse approach whilst they understand, interpret and apply the Consumer Duty requirements (in particular the price and value and products and services outcomes). This could, at least in the short-term, reduce consumer choice and competition.

If we compare other regulatory requirements that have links to or cross-over with the Consumer Duty, firms had:

- A total of 16 months from publication of the policy statement until the end of the 12 month transition period on GI and pure protection fair value requirements (PS21/5).
- Seven months on vulnerable customers guidance (guidance consultation was issued in July 2020 and finalised guidance issued in February 2021).
- 12 months to implement operational resilience requirements, with a three year transitional period to remain within impact tolerances. Like the Consumer Duty, this was also described as an iterative piece of work.
- 18 month implementation period on the Mortgage Market Review.

It is also important to note that:

- Treating Customers Fairly was introduced by the FSA in July 2006 but the FSA set a target for firms to have reached at least the 'implementing' stage of their TCF work in a substantial part of their business by the end of March 2007. Only once that deadline had passed did the FSA begin, in 2008, to monitor firm's MI and carry out firm specific and thematic supervision. This meant that firms had eight months to start their implementation work whereas the FCA is suggesting nine months for full implementation of the Consumer Duty.
- Since TCF was implemented, we have seen considerable product, service and technological developments that will influence and impact a firm's review of the work required to meet its obligations under the new Consumer Duty.

It is therefore clear that nine months is disproportionate when considering the entire suite of measures under the Consumer Duty and the FCA's expectations that this represents a "paradigm shift" in retail financial services.

We also feel that a two year implementation period, with a 12 month transitional period on price and value and products and services outcomes, will provide the FCA with more time to gather insight from other regulatory areas that have been implemented or will be implemented over the next 12-24 months. For example, the Senior Manager and Certification Regime, enhanced product governance requirements applicable to GI and pure protection, vulnerable customers and strengthening the AR regime. These areas of regulation need time to embed and for the FCA to be provided the opportunity and time to monitor and supervise in the early stages.

To provide a specific example, the Consumer Duty 'price and value' and 'products and services' outcomes have cross over with the rules and guidance in force in the GI and pure protection markets.

Firms in these markets have until 30 September 2022 to achieve full compliance with the enhanced product governance and fair value requirements We are of the opinion that the FCA needs two years to review the effectiveness of these measures and to share insight that will benefit the wider financial services industry. Otherwise, we risk the layering of regulation without proper and full assessment of interconnecting areas and miss the opportunity to apply 'lessons learned'. This type of insight is likely to prove invaluable when we consider that the FCA expects implementation of the Consumer Duty to be an iterative process and will ultimately help drive better consumer outcomes.

Q17: Do you have any comments on our proposed approach to monitoring the Consumer Duty and the related draft rules and non-Handbook guidance?

It is important that the FCA does not rely on data to monitor and supervise the Consumer Duty and that this is backed up with robust 'feet on the ground' supervision of firms.

It is positive that firms will not be required to submit data to the FCA; we feel this is a proportionate approach and helps to ensure that firms do not view the Consumer Duty as an MI led, 'tick box' exercise. We agree with the FCA's approach not to mandate the data collected by firms, as firms should be able to take a proportionate approach based on the size, scale and complexity of their business, the products and services they offer and their customer base.

However, it will take time for firms to develop a data strategy and ensure systems and controls are in place to collect and monitor an appropriate level of data. A nine month implementation is an inadequate timeframe to carry out IT system changes, particularly when the Consumer Duty is still at consultation stage and therefore firms cannot begin to plan and execute IT projects as final details are unconfirmed.

We are concerned that smaller firms, whilst they may already meet elements of the Consumer Duty, are likely to lack the infrastructure and resources to evidence how they are monitoring consumer outcomes. It would be useful for the FCA to provide in the Policy Statement and as part of the implementation period case studies of MI that different sized firms have used and subsequent action taken, to help firms gain perspective on the extent of the FCA's expectations. It is particularly difficult for smaller firms to interpret what "good" looks like in this area.

We ask for clarification that firms will not have to collect consumer data on protected characteristics to take account of the diverse needs of their customers. This type of data is classed as special category data under UK GDPR and therefore has strict controls over collection and use. Is the FCA asking firms to collect data on a customer's sexuality, disability, ethnicity etc as part of its proposals? AMI would question the need to collect and store details such as the sexuality of customers who apply for a mortgage.

The draft rule 2A.8.5 R states that firms must regularly monitor consumer outcomes. We feel the FCA should develop its non-Handbook guidance to provide examples of the consumer and product types where a more regular review may be necessary.

We agree with the FCA's proposal to require a firm's board or equivalent governing body to review and approve an annual assessment. However, we question how this would work in practice for sole trader firms run by one individual who effectively would be "marking" their own work.

Where beneficial, for some sectors it might be required that the FCA prescribes new responsibilities under the Senior Manager regime. This might be a way of delivering a degree of granularity for those areas that the FCA sees as higher risk and is reflective of the purpose and aims of the SM&CR.

We agree that the FCA should communicate findings to industry and stakeholders on how firms are embedding the Consumer Duty in the implementation period. Only a few AMI member firms have access to a dedicated FCA supervisor (who they only have due to their dominant parent company). We therefore ask the FCA to confirm how it plans to engage with these firms during implementation and post-implementation. We are concerned that AMI member firms are unaware of the individuals within

their portfolio supervision team and this severely limits the FCA's ability to gather insight directly from industry. With the FCA asking firms to invest heavily, it is crucial that the FCA plays its part and supervises and enforces the Consumer Duty more robustly than it has in the past.

The FCA has not stated in this consultation whether it will carry out a post-evaluation of the effect of the Consumer Duty on the industry. Given the substantial investment required by firms, we feel the FCA should commit to this review and confirm in the Policy Statement when this will likely take place.

Q18: Do you have any comments on our proposal to amend the individual conduct rules in COCON and the related draft rule and non-Handbook guidance?

We agree with the inclusion of a new conduct rule relating to the Consumer Duty. We are pleased to see that the draft rules include guidance on how the scope of a person's job and their seniority may affect the scope of their duty under the new conduct rule, as this helps ensure proportionality.

Q19: Do you have any comments on our cost benefit analysis?

In our opinion the Cost Benefit Analysis (CBA) does not quantify the extent of harm that currently exists in retail markets nor does it provide evidence on how the new Consumer Duty would have prevented harms of the past. We do not see how the FCA can conclude that the Consumer Duty will be net beneficial.

We agree with the FCA's assumption that firms will incur higher one-off costs compared to ongoing costs. However, we are concerned with how much this could potentially cost the mortgage intermediary sector. The FCA has estimated that for large firms it will cost between £600,000 and £1.4m, medium firms between £191,000 and £648,000 and small firms between £7,000 and £26,000. This is significant money for mortgage intermediary firms to spend at a time when regulatory costs are increasing overall. A longer implementation period will allow firms, particularly smaller firms, to stagger the one-off costs over an extended time period.

We are concerned that ongoing costs could spiral when we consider the FCA's estimations that industry had already incurred annual costs of £1.4bn in approach treating customers fairly[2]. Based on this knowledge, we also believe the FCA's estimation that ongoing annual costs to industry could be in the range of £74.0m to £176.2m is too low.

We request that the FCA commits to reviewing costs with industry both pre and post implementation, as part of a "two way" iterative process. Due to the significant costs that will be incurred by firms, we ask that if costs look too onerous versus the perceived benefits the FCA should be required to re-consider and withdraw sections of its requirements.

We do not feel the FCA has fully acknowledged the potential cost to consumers. Mortgage intermediary firms are facing increased regulatory costs; for example, a principal firm that operates as a network will, at the same time as implementing the Consumer Duty, be faced with costs arising out of the FCA's work on the AR regime, whilst smaller firms will feel more acutely the impact of an increase in FCA minimum fees this year. There are also increased FSCS, FOS and PII costs that affect firms of all sizes. These pressures could result in firms increasing their advice fees.

Given the significant costs of the Consumer Duty and the resources and infrastructure required to implement, we may see directly authorised firms decide to join a network. It is important that the FCA does not view the Consumer Duty in isolation; it must be reviewed alongside other significant pieces of regulatory work, notably the FCA and HMT consultations on the Appointed Representatives Regime.

[2] Impact Assessment: FG21/1: Guidance on the fair treatment of vulnerable customers (fca.org.uk)

Q20: Do you have any other comments on the draft non-Handbook guidance?

We refer to comments made in previous questions.

Q21: Can you suggest any other examples you consider would be useful to include in the draft non-Handbook guidance?

We would like to see the FCA expand the number of case studies and poor and good examples, as this is not as comprehensive as the FCA's vulnerable customers guidance. It would be beneficial for the FCA to cover a wider range of financial services sectors and to includes case studies that relate to small, medium and large firms. We would specifically like to see more case studies that relate to mortgage intermediaries or at the very least, the mortgage market.