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FSA Mortgage Market Review
Full Package of Reforms
CP 11/31

Response by the Building Societies Association

Introduction

1. The Building Societies Association (BSA) represents mutual lenders and deposit takers in the UK including all 47 UK building societies. Mutual lenders and deposit takers have total assets of over £375 billion and, together with their subsidiaries, hold residential mortgages of over £235 billion, 19% of the total outstanding in the UK. They hold more than £250 billion of retail deposits, accounting for 22% of all such deposits in the UK. Mutual deposit takers account for 34% of cash ISA balances. They employ approximately 50,000 full and part-time staff and operate through approximately 2,000 branches.

2. The BSA welcomes the opportunity to comment on the proposed full package of reforms. This response is the result of significant consultation with BSA members over recent months.

3. Generally we do not believe that there is a need for wholesale changes to conduct of business rules at this time. There is not a culture of widespread irresponsible lending in the UK mortgage market. Where there has been evidence of consumer detriment the BSA believes that this was not a result of an inadequate rulebook, rather it was a result of a lack of effective supervision of the firms involved.

4. The FSA, through its supervisory enhancement programme, has taken significant steps to improve its supervisory regime. It now takes a more intrusive approach than in the past and we believe that this is a more appropriate way of preventing consumer detriment.

5. There has also been changes to prudential rules in recent years that ensure that lenders are setting aside significantly more capital when lending to higher risk segments of the market. We believe that the impact of both these prudential changes and the supervisory regime should be fully assessed prior to determining what, if any, rule changes need to be made.

6. The market has largely self corrected and much of the lending that the FSA is concerned about is not a feature of the current market. We accept that steps need to be taken to prevent these practices from returning when the market picks up but we believe that there is sufficient time for the FSA to fully assess the landscape and it should not rush to implement wholesale changes.

7. It is also vital that the cumulative impact of all of the proposed regulatory initiatives are fully assessed. Given the fragile economic conditions the FSA cannot risk unintended consequences as a result of insufficient analysis.

8. Whilst we believe that many of the rules are sensible and are likely to deliver the intended outcomes, there is a significant risk that lenders will be very cautious in their implementation of the rules. This is to be expected until the supervisory landscape is clear. There is already evidence of the industry taking a much more cautious approach to interest only lending as lenders are unclear how these loans will be judged in retrospect. Our message here is to proceed with caution.

Executive Summary

Affordability assessment

- We have consistently agreed with the principle that all mortgage applications should be assessed on the applicant's ability to repay the loan. Borrowers should be required to provide accurate and genuine information about their income to their lender. An affordability assessment omitting this will be of limited benefit.

- We remain concerned that the proposals will have a significant impact on self employed borrowers. We would urge the FSA to monitor the impact on self employed borrowers in light of the proposed requirements and issue further guidance for firms to ensure that self employed borrowers are not adversely affected by the proposals.

- We welcome the shift in the FSA's approach to the expenditure assessment. The original proposals in CP 10/16 were far too prescriptive and were at risk of transferring responsibility for affordability onto the lender and reducing the responsibility of the borrower.

- The revised proposals in CP 11/31 represent a much more proportionate approach to affordability and provide the lender with a sound framework on which to base their affordability assessment, whilst taking account of the individual circumstances of the borrower, recognising customers will flex their income. We are therefore supportive of the proposals and they reflect the general approach to affordability by many BSA members already.

- We welcome the clarification from the FSA that it does not expect lenders to 'crystal ball gaze' when assessing future changes to income. The revised rule in this respect is much clearer and proportionate.

- We remain concerned about the risk of conflict with existing discrimination legislation and impending legislation relating to age discrimination in services under the Equalities Act 2010.

- We would urge the FSA and the Government Equalities Office (GEO) to work together to produce some coherent guidance for firms in relation to the interaction of affordability requirements under the MMR and the Equalities Act 2010. This will ensure that lenders are not inadvertently being required to breach the Act in order to comply with MCOB, or vice versa.

Transitional arrangements

- In our view, by seeking to protect 'trapped' borrowers, the prescriptive eligibility requirements significantly reduce the ability for lenders to assist these borrowers. The proposals themselves are complex and do not fit easily into an underwriting process.

- Rather than seek to rework the draft rules, we believe a better approach is for the FSA to allow lenders to develop an exceptions policy. This would be suited to each lender's individual lending policy and strategy and agreed with their supervisor. The exceptions policy will allow a lender to consider lending to a borrower who is unable to demonstrate affordability as a result of the MMR.

- This approach will allow lenders the flexibility to consider the individual circumstances of the borrower and allow them to make a sensible lending decision.

Interest Only

- We accept that in the past there has been some lax lending practices by some firms in relation to interest only lending, where the repayment strategy was not adequately assessed. However, we do not believe that this was widespread practice and therefore much of the concern is borne out of perceived consumer detriment, which has not and may not yet materialise.

- We would also question how the FSA truly views interest only. Currently it is not clear what the FSA expects in terms of an interest only market. It has recognised that the market expanded in the run up to 2007, as a result of a more general relaxation in lending policy and has since reduced again. However, it does not seek to confirm whether it prefers interest only as a niche product, or as a legitimate mainstream offering, causing uncertainty amongst firms as to what the regulator is really expecting in terms of a lending strategy for interest only.

- In our view the FSA needs to be clear as to how it views the interest only market so that firms can operate in a certain regulatory environment. Without this, firms could be reluctant to continue to offer interest only, causing detriment to those consumers who manage their interest only loan appropriately.

Distribution and Disclosure

- The BSA has been supportive of moving mortgage advising and selling away from being solely focussed on recommending or providing information on a product. A mortgage is the single biggest financial decision an individual will make and therefore we believe the advising and selling process should be focussed on holistic financial advice and/or information to ensure the mortgage is appropriate.

- It is disappointing that the FSA has not sought to review the mortgage market from this perspective and instead has made the process more product focussed and further reduced the choice for the consumer as to how they manage their personal circumstances, by proposing to move to a fully advised market.

- The definition of advice, given in the CP is also too simplistic and does not adequately define the point at which the sale commences. We are concerned that the shift away from a personal recommendation will lead to the whole advice process being rejected rather than just the final product that is presented to the customer. We do not see how this would work in practice and therefore would question whether this is the right approach.

- We are concerned that the focus of the CP is very much on the intermediary, with lenders being viewed as an after thought. This is a criticism we raised in our response to CP 10/28 and it is disappointing that this has not been taken on board. Of particular concern is the lack of regard for lenders with a limited product range, where advice would be inappropriate and impractical.

- The BSA believes that there is a risk that consumers may become less engaged if they are forced to take advice even if they don't require it. They may pay less attention and have less interest in the mortgage process on the assumption that they will be provided the best mortgage for their circumstances. At a time when the Government is implementing major reforms through the Universal Credit regime with the objective of putting consumers in control of their finances, this proposal seems to be at odds with the Government's policy.

- Consumer choice is vitally important and many consumers will be able to make an appropriate decision for themselves, either on a pure execution only basis, or by obtaining some factual information, through a non advised sale. The FSA recognises that the mortgage market has worked well for the majority of consumers, therefore we would question whether moving to a fully advised market is really what is needed to enhance consumer protection.

Objectives of the MMR

9. The BSA has consistently supported the FSA's quest for a market based on consistent, responsible lending and borrowing. The mutual sector has consistently performed considerably better than other lenders in terms of treating customers fairly and customer satisfaction. Independent research published by the BSA in March 2010[1] demonstrates that building societies provide better service and have customer satisfaction levels superior to banks.

[1] http://www.bsa.org.uk/docs/consumerpdfs/customerservice.pdf

10. Mutual lenders also account for lower arrears, proportionately, than other mortgage lenders reflecting their prudent lending practices and pragmatic forbearance measures.

11. The BSA does not argue to maintain the status quo and we accept that there were some instances of poor practice displayed by a minority of lenders during the peak of the market. On the whole we believe that the majority of mainstream lenders acted responsibly. The financial crisis that we have endured in recent years is not a result of widespread irresponsible mortgage lending in the UK.

12. The FSA stated in its original discussion paper (DP 09/3) that the primary objectives of the MMR are to ensure we have a mortgage market that works better for consumers and is sustainable for all participants.

13. The BSA strongly supports these objectives. We did have concerns with the past proposals and we were unconvinced that the MMR would achieve its objectives. The proposals outlined in CP 11/31 represent a welcome shift in direction by the FSA and we agree that most of the proposals are likely to deliver the intended outcomes.

14. Overall we remain of the belief that the MMR should be aiming to:

- Promote responsible borrowing by raising financial capability. Empowering borrowers to take ownership of their personal finances and enable them to make well informed decisions;
- Promote best practice to raise standards across the industry and ensure better outcomes for consumers including consumer choice, transparency and TCF goals;
- Promote competition in the mortgage market, enabling lenders of all business structures, to compete on a level playing field and provide the range of products required to service all appropriate sections of the market;
- Promote product innovation to meet the demand of a diverse and ever evolving customer base. A wide range of products and providers is necessary to ensure consumers have choice of product and price; and
- Ensure lenders have flexibility to support their customers when they need to, for example, when they are experiencing financial stress, and ensure sensible outcomes are delivered.

15. We believe that generally the proposals will achieve these outcomes, except for 'empowering borrowers to take ownership of their finances'. We believe that the proposals relating to advised sales and the verification of interest only repayment strategies do not fully empower consumers. They seem to imply that many consumers are unable to make sound financial decisions for themselves. More worryingly they may give consumers the erroneous impression that the lender is ‘taking care of it’. The proposals may actually detach consumers from the process and deter them from taking control of their finances by appearing to transfer much of the responsibility onto the lender.

16. We also have concerns with the proposed transitional arrangements, as we do not believe these will work in practice.

Direction of the MMR

17. The BSA has had a number of significant concerns regarding the overall direction, purpose and impact of the MMR. Key amongst these were:

- The wider impact on the economy and housing market and how the proposals interact with wider Government ambitions and policy
- A firm shift apparently removing responsibility away from borrowers, and placing disproportionate and unreasonable responsibilities solely on the lender.
- The interaction with existing and planned macro-prudential reforms.

- Potential conflict with regulatory reform initiated at European level.

18. The shift in FSA policy, supported by the detailed cost benefit analysis has alleviated some of these concerns. However, the timing of implementation must still be considered carefully and we stand ready to support the FSA in order to get this right.

19. In terms of macro prudential reform, we do believe there is still the potential for it to conflict with conduct reform. Particularly if the new Prudential Regulation Authority (PRA) is able to use loan to value (LTV) and loan to income (LTI) as a macro prudential tool. Placing limits on these variables could prevent lenders from servicing consumer demand. We would urge caution in how the PRA and Financial Conduct Authority (FCA) policies interact in this respect as macro prudential levers to curb lending may well have a detrimental impact on those borrowers who need to remortgage or move home to support their personal circumstances. This in itself could give rise to significant consumer detriment.

20. The EU Directive on Credit Agreements Relating to Residential Property (CARRP) still has the potential to impact on the changes proposed in this consultation. The FSA states that the uncertainty around timing and the form of the CARRP proposals is not a reason for delaying the proposals in this consultation. This position needs to be considered carefully. We recognise that the UK market needs regulatory certainty and therefore pressing ahead with the MMR, will provide firms with clear expectations as to what is expected from them by their regulator.

21. However, the uncertainty is not completely removed if firms are likely to be required to make further changes once the Directive is finalised. We would maintain our position that the implementation of the MMR must take account of the Directive and the FSA needs to be prepared to delay its reforms and implement all the measures at the same time in order to prevent significant unnecessary costs.

Section 3
Responsible Lending

Affordability Assessment: Verification of income

22. We have consistently agreed with the principle that all mortgage applications should be assessed on the applicant's ability to repay the loan. Borrowers should be required to provide accurate and genuine information about their income to their lender. An affordability assessment omitting this will be of limited benefit.

23. We welcome the fact that the FSA has been clear from the outset that it does not propose to prescribe how lenders verify an applicant's income. As recognised in the CP, lenders must have the flexibility to innovate and meet the needs of different market segments.

(i) Self employed borrowers

24. We remain concerned that the proposals will have a significant impact on self employed borrowers. We agree that self employed borrowers whose business is still relatively young, will have to wait to provide a track record of income, but there is a concern about the impact on self employed borrowers with an established business.

25. The FSA has recognised that self employed borrowers may take longer than salaried employees to gather a track record of income to meet lenders' requirements, due to the timings of accounts being prepared and published after year end.

26. We welcome the revised proposal to allow projections of income to be considered where they form part of a credible business plan and also to allow lenders flexibility in determining acceptable evidence.

27. We would urge the FSA to monitor the impact on self employed borrowers in light of the proposed requirements and issue further guidance for firms to ensure that self employed borrowers are not adversely affected by the proposals.

(ii) 'Human intervention'

28. We welcome the decision not to proceed with a requirement for human intervention in the application process. In our response to CP 10/16 we were not convinced of the merits of requiring human intervention where income is verifiable electronically, as it would add little value to the overall underwriting approach.

(iii) Fraud prevention

Q1 Do you agree that lenders should detail how they incorporate anti-fraud controls into their affordability assessments in their responsible lending policy?

29. Anti fraud policies are usually held separately and contain the information referred to in the CP regarding fake documentation, fraud indicators and fraud detection systems. We do not agree that stating this information in the lending policy is necessary to ensure that firms consider anti fraud measures as part of their application process.

30. Incorporating anti fraud policies and/or techniques into a lending policy could result in this information becoming available to unscrupulous individuals. Anti fraud measures are usually held confidentially within firms to ensure that they remain robust and there is no opportunity for the rules to be circumvented.

31. We believe that lenders are capable of ensuring that appropriate anti fraud controls are implemented into the assessment of affordability and therefore see no reason for FSA to be prescriptive as to where this is documented.

(iv) Assessment of income

Q2 Do you have any comments on our income proposals?

32. We remain supportive of the proposals to allow lenders flexibility when assessing income and welcome the additional guidance in respect of the factors the lender should take into account.

33. We would question the definition of 'earned' income as this would imply that income from maintenance, alimony or state benefits would not be considered acceptable. As the proposed assessment of expenditure would require the lender to take account of child care costs, it seems illogical that they could not take account of maintenance payments which may offset this expenditure.

34. The definition therefore needs to either take account of these forms of income, or allow for flexibility, with clear guidance provided to lenders.

Affordability Assessment: Expenditure

Q3 Do you agree with this approach to expenditure? Do you have any comments on the categories of expenditure? Do you have any practical concerns about implementing this approach?

35. We welcome the shift in the FSA's approach to the expenditure assessment. The original proposals in CP 10/16 were far too prescriptive and were at risk of transferring responsibility for affordability onto the lender and reducing the responsibility of the borrower.

36. The proposals also did not take account of how individuals manage their finances and amend expenditure over time, including from the point the mortgage is taken out. We were concerned that the proposals worked for remortgage customers, where in theory the only change to expenditure will be the mortgage commitments. They did not work for home movers.

37. The revised proposals in CP 11/31 represent a much more proportionate approach to affordability and provide the lender with a sound framework on which to base their affordability assessment, whilst taking account of the individual circumstances of the borrower, recognising customers will flex their income.

38. We are therefore supportive of the proposals and they reflect the general approach to affordability by many BSA members already.

39. We do have some concerns as to how the proposals work within the context of income multiples, which we explain in more detail in our response to question 10.

(i) Future interest rate increases

Q4 Do you have any comments on our proposed approach to assessing affordability against future interest rate increases?

40. We remain supportive of the principle that the interest rate should be stress tested, and this is already undertaken by many lenders.

41. We welcome the shift away from the original proposal for the FSA to publish a guideline rate, as this would not work as intended in practice, as we explained in our response to CP 10/16.

42. We are supportive of the principle that the lender should take account of market expectations, to ensure that the rate is adequately stressed and we agree the forward sterling rate or similar is a good benchmark on which to base the stress test.

43. We welcome the proposal that the stress test should not be based on rates which are fixed for 5 years or more.

44. We also welcome the clarification with regards to how often lenders will need to change the rate, with the FSA acknowledging that changing this on a daily basis in reaction to market events, or reassessing pipeline business each time the market expectations change is not practical.

45. We do have some concerns as to how the stress test works within the context of income multiples and we explain this in detail in our response to question 10.

Q5 Do you agree with our assumption that 90% of lenders already apply a stress test?

46. We do agree with the assumption that 90% of lenders already apply a stress test. We agree this should form part of the affordability assessment and therefore it is unlikely to have a significant impact on lenders existing processes.

Q6 Do you think that lenders are currently applying a stress test of a similar degree to the test we propose?

47. We agree that lenders are currently applying a stress test similar to that proposed and in most instances this is likely to be a higher standard than that proposed.

48. We do have some concerns as to how the stress test works within the context of income multiples and we explain this in detail in our response to question 10.

(ii) Maximum mortgage term

Q7 Do you have any comments on our proposal to drop the requirements that affordability should be assessed on a maximum term of 25 years?

49. We support the decision to drop the requirements for affordability to be assessed on a maximum term of 25 years.

50. We remain of the belief that the customer's individual circumstances must take priority. An extended term for young and/or first time buyers is a legitimate way of managing affordability. In our response to CP 10/16, we felt that this restriction would serve as an unnecessary barrier for some borrowers.

(iii) Credit impaired borrowers

Q8 Do you have any comments on our proposals to protect credit impaired borrowers?

51. We agree that an additional affordability buffer is not an appropriate measure to protect credit impaired borrowers. As we stated in our response to CP 10/16, we do not believe that a buffer will serve as a useful tool in ensuring vulnerable customers are protected and instead, will serve to widen financial inequalities by preventing many customers from accessing home finance.

52. We do support the principle of ensuring that credit commitments are repaid as intended, we elaborate on this further in our response to questions 12 and 13.

(iv) Right to Buy

Q9 Do you think our proposed enhanced sales standards will provide adequate protection for right to buy consumers? Are further measures required?

53. We do not believe that any further measures are needed specifically for Right To Buy (RTB) customers, therefore we agree that the enhancements made to sales standards overall, will provide better protection for RTB customers as a result. We are also supportive of the requirement for these to borrowers to always receive advice, as we explain in our response to section 5.

54. We further believe that the bigger question for prospective RTB borrowers is 'should we exercise our right to buy or would we be better remaining as tenants' rather than 'what is the most appropriate mortgage product?'. Therefore we believe that further advice and information is needed to support the customer in making that initial decision. The examples cited in the CP support this view, as arguably some of these borrowers may not have proceeded to buy their property if they had fully understood the risks.

55. We believe that this needs to be considered carefully, not only in the context of regulation, but also by Government as part of its implementation of the Housing Strategy.

(v) Income Multiples

Q10 Do you think income multiples could work under our proposed rules? If not, why not?

56. We do believe that income multiples could work under the proposed rules. However, we would question how the FSA would envisage them working in practice.

57. A number of building societies primarily use income multiples, with credit commitments deducted from the gross income. Analysis of the lending policies of building societies shows that 51% of the sector use this approach to affordability, 11% use income multiples only, 14% use income multiples, credit commitments and household expenditure and 24% use an affordability assessment only.

58. Many mutuals use income multiples or a hybrid of income multiples and affordability. This ensures that the assessment can be conducted easily, is transparent for consumers and removes the likelihood of human error by inconsistent interpretation of information.

59. We would argue that the use of income multiples under all these approaches would still be valid under the proposed rules. However, it is not clear as to how explicit the FSA expects the proposed expenditure assessment and stress test to be, as this could conflict with how lenders apply income multiples currently.

Income Multiples, with credit commitments deducted from gross income

60. Under this approach, the lender will deduct credit commitments from the borrower's gross income and then apply a multiple to determine the maximum borrowing. The multiple is set on the basis that it accounts for taxation, reasonable household expenditure and a stressed interest rate.

61. It is not clear from the proposals whether the assessment of household expenditure and the stressed interest rate can continue to be factored into the multiple in this way. It is also unclear whether the multiple can continue to be applied to the gross income rather than net, again as general deductions for taxation are factored into the multiple.

62. The analysis below demonstrates the outcome of using an income multiple, with credit commitments deducted from the gross income as well as the outcome of using an expenditure assessment and then applying a multiple. In our view this demonstrates that

income multiples, which take account of taxation, reasonable household expenditure and a stressed interest rate, deliver the outcomes that the FSA expects.

Affordability - Income multiple assessment

Applicant 1: Gross Income £25,000
Applicant 2: Gross Income £20,000

Credit Commitments
Credit card: Balance £1,000
Credit card: Balance £2,500
Personal loan: Monthly payment £157.33

Total annual payment to credit commitments: £3357.96

Total income: £45,000 minus credit commitments £3357.96 = £41,642.04

£41,642.04 x income multiple of 3 = **Total maximum loan of £124,926.12**

Notes
Credit card balance: Use 3.5% of the balance, multiplied by 12 to give the annual payment

Affordability - Expenditure assessment

Applicant 1: Gross Income £25,000 Net income £19,532
Applicant 2: Gross Income £20,000 Net income £16,132

Credit Commitments
Credit card: Balance £1,000
Credit card: Balance £2,500
Personal Loan: Monthly payment £157.33

Total annual payment to credit commitments: £3357.96

Expenditure - per month

House keeping	£208
Ultilities inc water	£288
Tele/communications	£24.60
Council tax	£89.20
Insurance	£21.20
Transport	£295.20
Clothing	£90.40
Household goods	£126.80
Health	£26.00
Recreation	£277.20
Total:	£1446.60 - Annual = 17,359

Total income: £35,664 minus credit commitments £3357.96 minus expenditure £17,359 = £14,947 divided by 12 = Monthly net income of £1245.

Interest rate stressed at 8% gives a **total maximum loan of £159,500.**
This is the equivalent of the income multiple being 4.47

Notes
Credit card balance: Use 3.5% of the balance, multiplied by 12 to give the annual payment
Net income after tax and national insurance deductions
Expenditure taken from ONS data based on a two adult household with no children

63. If it is the FSA's expectation that the proposed expenditure assessment and interest rate stress should be an explicit assessment, with the multiple applied to the net income after these deductions, this will be a change to current practice for a number of firms, as a result, income multiples would not work under the proposed rules.

64. We would welcome clarification from the FSA as to how it expects income multiples to work under the proposed affordability rules.

Other responsible lending issues

Q11 Do you have any comments on our proposal to require lenders to take into account information about future changes to income and expenditure?

(i) Foreseeable changes to circumstances

65. We welcome the clarification from the FSA that it does not expect lenders to 'crystal ball gaze' when assessing future changes to income. The revised rule in this respect is much clearer and proportionate.

66. We remain concerned about the risk of conflict with existing discrimination legislation and impending legislation relating to age discrimination in services under the Equalities Act 2010.

67. The requirement for lenders to 'make reasonable enquiries' to ascertain information about changes to income and expenditure could result in the lender directly, or indirectly discriminating against the protected characteristics under the Act. Of particular concern, is the approach to assessing maternity pay and child care, which was also highlighted in a recent report 'Women and banks' by Professor Noreen Hertz.

68. In order to ensure that the lender is complying with the Act as well as with the regulatory requirements, we believe that it should be explicit within MCOB that when assessing foreseeable changes to circumstances, firms should take account of the protected characteristics under the equalities Act 2010. We believe that the FSA has a positive duty to act with regards to equalities legislation and this would be a helpful inclusion into the rules.

69. We also believe the FSA should provide guidance in respect of the definition of 'reasonable enquiries' and the way in which a customer should be questioned, to ensure that the lender does not indirectly discriminate by asking inappropriate questions in order to comply with FSA requirements.

70. We would therefore suggest that the guidance states that lenders should ask the question as follows:

'Are you aware of any future changes to your circumstances that are likely to impact your ability to meet your monthly mortgage repayments?'

71. The lender will then act upon the response to the question in accordance with their lending policy. If the borrower answers 'no', the lender will not be expected to undertake any further questioning and will have been deemed to have satisfied the regulatory requirement.

(ii) Lending into retirement

72. We welcome the revised approach to assessing lending into retirement. In our response to CP 10/16 we proposed that the amount of evidence the lender should obtain, should vary depending upon the time until retirement. We believe this is a proportionate approach to assessing income into retirement.

73. However, we remain concerned with the proposal for the lender to take the state retirement age as the default age for retirement. We recognise the FSA's desire to have some form of benchmark for lenders however; we are not convinced that the use of the state pension age is the right option. This is not necessarily an indicator of when an individual will retire, only when their state pension becomes payable. As such it may not be most suited to the customer's circumstances and it could conflict with the age discrimination laws under the Equalities Act 2010.

(iii) Guidance for firms on the Equalities Act 2010.

74. We would urge the FSA and the Government Equalities Office (GEO) to work together to produce some coherent guidance for firms in relation to the interaction of affordability requirements under the MMR and the Equalities Act 2010. This will ensure that lenders are not inadvertently being required to breach the Act in order to comply with MCOB, or vice versa.

75. The BSA, along with the CML has met with the GEO which is very willing to engage on this issue. A joined up approach between the industry, the FSA and GEO would be welcomed.

(iv) Credit commitments becoming due during the term

76. We agree with the proposals that lenders should take account of credit commitments, which may become due during the term. We also welcome the flexibility provided, to allow lenders to decide how best to factor this into the affordability assessment.

(v) Debt consolidation

Q12 Do you agree that to ensure these proposals work, we should define a credit impaired consumer? Do you agree with our proposed definition?

77. We do agree that there needs to be a definition of credit impaired in order for this proposal to be proportionate and the proposed definition is adequate.

Q13 Which option do you prefer? Option 1, where the lender would be required to take reasonable steps to ensure that debts to be consolidated are repaid? Or option 2 where the lender would be required to assume that debts to be consolidated remain outstanding for the purposes of assessing affordability? If you disagree with both options, what do you suggest as an alternative?

78. Our preference is for option 1, whereby the lender must take steps to ensure the debts are repaid only where the mortgage is not affordable if they were not repaid.

79. This was the approach we suggested in our response to CP 10/16. Many of our members report that they already have processes in place to repay creditors, both for a remortgage and further advance, where the affordability assessment passes only on the basis that the debts are repaid. Where the affordability assessment would pass if the debts were not repaid, the lender is typically content for the customer allocate the funds.

80. We believe this is a sensible approach and would minimise the administrative burden upon lenders. Furthermore it would still allow customers to take charge of their finances, which is fundamentally important.

81. We also believe it is important to understand that requiring the lender to undertake this process does not prevent the borrower becoming over indebted in the future, as some may decide to take on further unsecured borrowing.

Systems and Controls

Q14 Do you agree with our proposals to strengthen lenders' systems and controls around responsible lending?

82. Aside from our comments with regards to integrating fraud controls, as per our response to question one, in principle we have no issues with the factors that should be incorporated into lending policy.

83. We would, however, urge a note of caution. Lending policy is intended to be a functional document, setting out the lending requirements applied by underwriters and other staff within lenders. Overloading the policy with internal audit controls, record keeping requirements and other monitoring, runs the risk of lending policy losing its intended objective.

84. Most lenders already document the factors outlined in the CP within separate documents. These may already be 'Board approved' but they are referenced in lending policy, not necessarily included. This ensures that the overall package of policy and procedures is documented, but in a way which is practical for the business.

85. As a result we see no reason for a prescriptive approach setting out where the systems and controls are documented, as long as firms have them documented in a way which is coherent. We would recommend that the draft rules are amended to allow for this manner of flexibility.

86. We would also question the explicit need for the policy to be signed off at Board level. Many lenders operate sub committees of the main board that deal with specific technical issues. For example, the risk committee may manage the overall risk strategy and would review the lending policy. It may be a conduct committee, which ensures that the company is complying with conduct regulation, of which lending policy is an integral part. Where these committees operate with clear terms of reference and where they have been granted delegated authority from the Board, we would see no reason why this would not be considered acceptable.

87. We would therefore recommend that the draft rules are amended to take account of this structure.

Transitional arrangements

Q15: Do you have any comments on our proposed transitional arrangements? Do you think they will be sufficient to address risks to consumers? Will they create any additional risks to consumers?

&

Q16: Do you think that there is sufficient protection for mortgage borrowers who are 'trapped' with their current lender? If not, what additional protection do you suggest?

88. The BSA has stated consistently since the publication of DP 09/13 in October 2009 that we are concerned about the impact the proposals will have on many existing borrowers. We have been concerned that many existing borrowers, already successfully meeting their mortgage payments, would find it difficult under the proposed rules, to remortgage in the future, or in some instances get a new mortgage at all. This remains a real area of concern for the BSA and for many consumers.

89. We therefore welcome the FSA providing suggested parameters to ensure these consumers are able to refinance in the future.

90. However, we do not believe that the prescriptive approach outlined in the CP is the right way forward. We do not believe the proposed rules will deliver the intended outcome. As such, if these rules were to be used at all by lenders, they are likely to be applied to existing borrowers only and not to borrowers remortgaging from other lenders.

91. This does not help resolve the issue for consumers whose lender is no longer offering new products, or those who wish to refinance to a cheaper rate.

92. We do not believe it is appropriate to apply the arrangements to interest only loans and we therefore see the arrangements solely for those borrowers unable to demonstrate affordability as a result of the MMR proposals.

Q17: Do you think the eligibility requirements are appropriate? Should we allow these transitional arrangements to be used where the new monthly payment is higher?

93. We do not believe that the eligibility requirements are appropriate. We believe they do not take adequate account of the individual circumstances of the borrower and would not deliver the intended outcome.

94. Whilst we understand the rationale for requiring the monthly payment to be the same or lower, this is not workable in practice, particularly in a market of rising interest rates. It also does not take account of borrowers who may wish to move from a variable to a fixed rate, which would increase the monthly payment marginally, but would give them greater financial stability. Such borrowers would be preventing from making a sensible change to their mortgage.

95. We also understand the rationale for not permitting additional borrowing (with the exception of essential repairs). However, this may have an adverse impact on borrowers needing to relocate for employment purposes or where there is a transfer of equity.

96. We do not believe it is practical for the lender to ascertain whether any additional borrowing (apart from essential repairs) has been taken out during the life of the loan. As there is no limit on the number of times the arrangements can be applied, this may involve requiring evidence from a number of lenders. This will be time consuming and may result in the borrower incurring additional costs if previous lenders charge for a reference in order to provide this information.

Q18: Should we allow the transitional arrangements to be used where there is a material change to the mortgage, such as the removal of a borrower following a divorce? How could gaming be prevented?

97. We do agree that there has to be some consideration of how material the change to the mortgage is. Many lenders will already consider a transfer of equity following a relationship breakdown, therefore we would question why there needs to be specific eligibility criteria to allow firms to continue to do this.

98. Ultimately we do not believe that prescriptive rules will work in practice and we believe a better approach is to allow lenders to have flexibility within their own lending policy.

Q19: Do you think these arrangements will be practical to implement? How could they be improved or simplified?

99. In our view, by seeking to protect 'trapped' borrowers, the prescriptive eligibility requirements significantly reduce the ability for lenders to assist these borrowers. The proposals themselves are complex and do not fit easily into an underwriting process. There is also a question as to how such borrowers would be given advice or information regarding their eligibility, as the use of the transitional arrangements is not specifically included in the distribution proposals.

100. Rather than seek to rework the draft rules, we believe a better approach is for the FSA to allow lenders to develop an exceptions policy. This would be suited to each lender's individual lending policy and strategy and agreed with their supervisor. The exceptions policy will allow a lender to consider lending to a borrower who is unable to demonstrate affordability as a result of the MMR.

101. This approach will allow lenders the flexibility to consider the individual circumstances of the borrower and allow them to make a sensible lending decision.

102. We agree that the draft rules should state some basic parameters for developing an exceptions policy and we would suggest the following:

- The exceptions policy only apply when the borrower enters into a new contract
- The mortgage must have been originated prior to the MMR coming into force
- The borrower must be able to demonstrate affordability by having a good payment history
- The lender is not aware of any information which means that the borrower will not be able to make the monthly mortgage payment.
- The borrower should have access to a range of products which are not created especially for customers who are eligible under the exceptions policy.

103. The specific lending parameters, will then be determined by each individual lender.

Q20: Do you agree that the draft rules on responsible lending in the draft *Mortgage Market Review (Conduct of Business) Instrument 2012*, reflect the stated policy intention?

104. As we have explained, we do not believe the transitional requirements work in practice, therefore the draft rules are unlikely to result in the stated policy intention being achieved in practice.

Section 4
Interest Only Mortgages

General Comments

105. We accept that in the past there has been some lax lending practices by some firms in relation to interest only lending, where the repayment strategy was not adequately assessed. However, we do not believe that this was widespread practice and therefore much of the concern is borne out of perceived consumer detriment, which has not and may not yet materialise.

106. We understand the FSA has concerns and is seeking to understand the extent of the issue by conducting a thematic review into past lending. This review should inform the regulator on the extent of the perceived problem and should assist lenders in managing customers who may not be able to repay the loan at the end of the term.

107. However, despite this work not being complete, the FSA is pressing ahead with rule changes for new lending, despite not fully understanding the extent and nature of issues it is trying to fix. As a result, the FSA could find it is fixing the wrong problem. We would therefore strongly urge the FSA to bring both pieces of work together, to ensure that the rules for new lending will address past problems, as well as providing firms with clear guidance on managing customer's who do not have a suitable repayment strategy, following the post completion review.

108. We would also question how the FSA truly views interest only. Currently it is not clear what the FSA expects in terms of an interest only market. It has recognised that the market expanded in the run up to 2007, as a result of a more general relaxation in lending policy and has since reduced again. However, it does not seek to confirm whether it prefers interest only as a niche product, or as a legitimate mainstream offering, causing uncertainty amongst firms as to what the regulator is really expecting in terms of a lending strategy for interest only.

109. In our view the FSA needs to be clear as to how it views the interest only market so that firms can operate in a certain regulatory environment. Without this, firms could be reluctant to continue to offer interest only, causing detriment to those consumers who manage their interest only loan appropriately.

Interest only as an alternative to renting

110. We agree with the FSA comments in the CP that lenders generally do not have an appetite for a specific product to allow consumers an interest only loan as an alternative to renting. However, there is still a question regarding the right to security of tenure, which an interest only mortgage may provide.

111. In the past to achieve security of tenure, an individual would need to be in social housing or become a homeowner. With the shift in current Government policy away from social housing being 'for life' this housing option will no longer provide the security of tenure for some that it has done in the past.

112. The private rented sector has always been short term in its nature, with longer term leases used rarely in the UK. The English Housing Survey 2011 published by the Government in 2012 shows that the private rented sector has grown significantly and continues to grow. Data for 2010-11 shows that the private rented sector accommodates 16.5% of households in England, compared to 15.6% in 2009-10 and 10.1% in 2001[2]. This is supported by the continued growth in buy to let (BTL) lending. At the end of 2011, BTL mortgages accounted for 13% of the total outstanding mortgages in the UK[3].

[2] The English Housing Survey 2011 http://www.communities.gov.uk/documents/statistics/pdf/2084179.pdf
[3] Source: CML Press release February 2012 http://www.cml.org.uk/cml/media/press/3144

113. The private rented sector can provide tenants with good quality accommodation, in areas that they wish to live at a price that they can afford. However, with most operating on a 6 to 12 month assured shorthold tenancy, this can mean frequent moves and upheaval in finding new accommodation. For a proportion of the market this works, but for some, such as those with families, the lack of secure tenure can be very stressful.

114. Therefore in order to obtain stability and purchase a home in the area the individual wishes to live, at a level they can afford, why should interest only not be an option? We recognise this will not work for all and it is not necessarily a decision for the regulator. However, in our view the Government has a responsibility to ensure that appropriate housing is available, that meets the demand of the population, creating vibrant and cohesive communities. Further work must be undertaken to provide people with greater security of tenure if home ownership is not attainable.

Homeownership for people with long term disabilities

115. There is also a much smaller segment of the market where interest only as an alternative to renting, is already offered as a specific product. This is shared ownership for people with long term disabilities (also known as HOLD), which is part of the Government's HomeBuy scheme operated by the Homes and Communities Agency (HCA).

116. Under this scheme, a home will be specially adapted for the needs of the individual and often purpose built for them. The individual will then purchase the property on a shared ownership basis, with the mortgage element taken out on interest only. The mortgage is then paid via Support for Mortgage Interest for the term of the loan. There is no specific repayment strategy other than the property being sold back to the housing association once it is no longer needed. The scheme is very small, since its launch in 1999, it has assisted approximately 1,000 people[4], the majority of which were through small building societies.

117. The scheme is designed to provide the individual with security of tenure and also gives them a home fit for their needs. We would urge the FSA to consider how such schemes can continue to apply under the proposed interest only loans, to ensure that these individuals are not excluded from homeownership.

Q21 What is your view on our approach to assessing affordability for interest only mortgages?

118. We agree with the proposals put forward in CP 11/31, as they provide the right balance when assessing affordability.

119. In our response to CP 10/16 we raised a concern that a blanket approach to assessing all loans on a capital and interest basis would be inappropriate and particularly for those borrowers on interest only over a short term who would be impacted most by such an approach.

120. We are pleased the FSA has taken this feedback on board and has developed a flexible framework, which allows for affordability to be assessed on an interest only basis where there is evidence of a repayment strategy. We also agree that if the repayment strategy requires the customer to make a continuing financial commitment, this should also be factored into affordability. This practice is already widely adopted by BSA members.

Q22 Do you agree that we should apply a consistent approach to regulating interest only across the board and that we should not adapt our approach according to different consumer types?

121. We do agree that a consistent approach to regulating interest only is the right way forward and that this should not be adapted for different consumer types.

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[4] Official statistics are not reported via the Homes and Communities Agency. This figure has been obtained by My safe Home www.mysafehome.info

122. We agree with the FSA view that the individual assessment of consumer circumstances is more important than defining broad consumer types. We also believe this is a much simpler way to regulate. Defining consumer groups and developing rules around each group would be complex, difficult to apply in practice and unlikely to deliver effective outcomes.

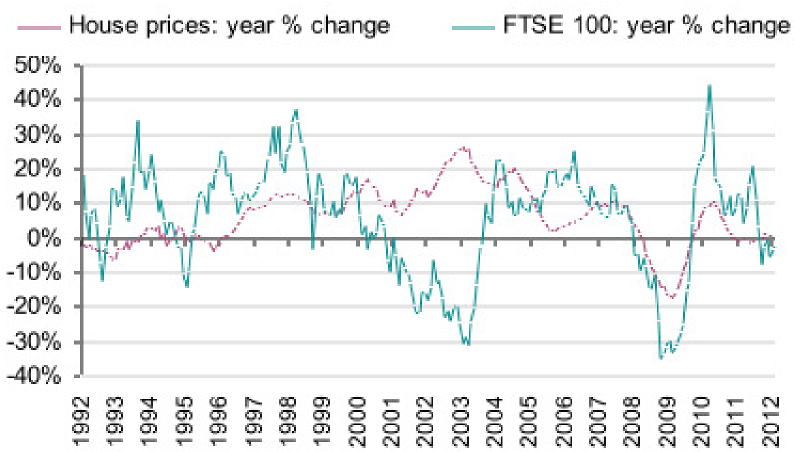
Q23 Do you agree with our non prescriptive approach to repayment strategies, or do you have any comments on this approach?

123. We welcome the decision not to develop a prescriptive approach, for the reasons recognised by the FSA in the CP. It would be difficult to capture all relevant repayment strategies in a manner which was flexible, so that regular rule changes to update the list are not needed, as well as ensuring the list itself was comprehensive enough to capture a broad enough spectrum in order to not adversely impact on customer choice.

124. We are therefore supportive of the approach to allow lenders to consider repayment strategies according to the individual circumstances of the customer and to make an assessment as to whether the plan is believable.

125. We agree that purely speculative strategies should not be accepted, such as uncertain inheritance, or reliance on a lottery win. However, we would question whether a reliance on house prices is truly an example of speculative strategies.

126. The graph below shows how house prices have performed in comparison to the stock market since 1992[5].



127. This shows that there has been less volatility in house prices when compared to the stock market over the same period. As such, we do not agree this is necessarily any more speculative than using a stocks and shares ISA, or other investment product, both of which are considered to be acceptable under the MMR.

128. We accept that over a short term, reliance on house price growth does become more speculative in its nature, but over the longer term it is less so. We would therefore argue that a strategy which relies upon future house price growth, in order for the customer to attain sufficient equity to repay the loan upon sale, should be considered as valid strategy, where it is credible for them to do so, such as when it is over a period of 10 years or more.

129. As such, this would then become the lender's discretion as to whether this approach is believable and it would be the lender's decision whether to accept the strategy, rather than the regulator banning this option outright.

[5] Sources: Nationwide, ONS

Q24 Do you agree that lenders should be free to set their own appropriate controls around repayment strategies?

130. We do agree that lenders should be free to set their own controls around repayment strategies. Each individual lender will have a different lending strategy and appetite to risk, therefore it is appropriate that they are able to amend their lending policy accordingly. However, we have seen recently that the actions of some lenders in respect of interest only policies has had a knock on effect to the rest of the market. Examples of recent publicised changes are as follows:

Halifax

Acceptable plans

Endowment
Stocks and shares ISA
Unit truts/open ended investment companies
Investment bonds
Stocks and shares
Pension
Sale of other residential property

Unacceptable Plans

Repayment plans CANNOT be accepted if they include the name of anyone NOT named on the mortgage. Your client can use more than one repayment plan to cover their total interest only amount. In this case, please send the relevant evidence for all repayment plans.
The following are NOT acceptable repayment plans:

Sale of main residence.
Sale of other commercial property.
Sale of non property assets
Inheritance
Bonuses.

Further restrictions have been placed on some of the plans, such as ISA/OEIC/Investment Bond, where the value of the investment is compared with the amount of interest only lending required, taking into account the remaining term of the mortgage and future market volatility. The valuation assigned to the investment is 80% of the current value which must be greater than £50000

Woolwich

The maximum loan to value (including any reserve) allowed on an interest-only basis is 75%. If your client requires borrowing over 75% the entire mortgage must be taken on a repayment basis. The maximum term for an interest only mortgage is 25 years and cannot extend into retirement.

The Barclays Group requires **all** customers who take an interest-only mortgage to have in place a repayment plan for their loan on completion of the advance. Unless using sale of property to be mortgaged, we require the repayment vehicle to have been in place for 12 months. The Barclays Group will consider one, or a combination of the following as acceptable repayment plans for interest only mortgages:

- An existing endowment policy
- An existing stocks & shares ISA
- A existing unit trust
- An existing investment plan/bond
- Sale of property to be mortgaged (maximum LTV 66% and must have equity of at least £150k in the property. This cannot be used in conjunction with another repayment vehicle)

Where your client wishes to use any other method of repayment to repay the interest-only amount other than the acceptable repayment plans detailed above, this is **not** acceptable.

In all instances **(including fast track cases)** details of the repayment vehicle must be captured at application stage. The only exception is where sale of property is to be used as the repayment vehicle, in which case we require a plausibility check to be carried out.

Santander

We allow interest only applications provided there is an acceptable source of funds to repay the capital at the end of the mortgage:

- For pure interest only mortgages the maximum term is 25 years
- If any of the loan is taken on an interest only basis, the maximum LTV for the overall loan is 50%

For applications with or without a funded investment vehicle, we will assess affordability on a capital and interest repayment basis and assume a repayment period of 25 years minimum. If the actual mortgage term selected is longer than 25 years with a funded investment vehicle, the longer term will be used.

Existing Abbey mortgage customers on an interest-only basis moving home may port their existing products and may also increase their borrowing up to 50% LTV on the new property.

Existing Abbey mortgage customers who have any part of their existing loan on an interest only basis can port their product(s) to a new property, subject to certain conditions:

- the new overall LTV is over 50% and less than or equal to 75%;
- any part of the new mortgage is remaining on an interest-only basis;
- the loan amount on interest only stays the same or reduces; and
- the overall lending is the same amount as the existing loan or less, no top-up allowed.

Nationwide

Interest Only and Part Repayment applications will be limited to a maximum LTV of 50%
Applications which exceed 50% LTV will only be considered on a Repayment basis.

Coventry

For first time buyers the only payment method is repayment (capital and interest). Interest only mortgages are not acceptable. Where there is an element of interest only the loan amount is restricted to £500,000. Any loans above £500,000 must be on a repayment basis only.

Where any element of the loan is interest only, these are restricted to 50% LTV. Any loans above 50% LTV must be on a repayment basis.

131. In our view, we do not see these lenders purely managing lending risk, but rather interest only polices have been tightened due to the uncertainty with regards to future regulation and future regulatory intervention in the interest only market. The difficulty with interest only is that potential consumer detriment only becomes apparent over the longer term. Therefore what may be a credible strategy at the start of the loan, may not turn out to be sufficient to repay the capital towards the end. As such lenders are concerned that action could be taken retrospectively, despite appropriate controls being in place at the time the loan was taken out.

132. A survey of BSA members supports this assertion.

BSA Member Survey[6]

Has your interest only policy changed since 2009?

Yes 86% No 14%

In what way has your policy changed? Please confirm the main change:

Reduction in LTV	71%
Restrictions on repayment strategies	29%

Do you have any plans to make further changes to your interest only policy?

Yes 72% No 28%

What are the likely changes and expected timescales for those changes

Reduce LTV	20%
Withdraw from Interest only	60%
Restrictions on repayment strategies	40%

[6] Survey from a cross section of BSA members in March 2012, which represents approximately 56% of the mutual sector

What has been your main reason for making changes to your interest only policy?	
Regulator view/MMR proposals	63%
Demand	13%
Reaction to other lenders policies	24%

133. The survey indicates that the biggest concern for lenders currently is the uncertainty surrounding the FSA's view of interest only loans. It is clearly this which has been the main driver for changes being made to lending policies, with action by other lenders also a significant factor.

134. The issue of regulation and the potential for retrospective regulation is a significant concern to lenders and it could result in more lenders pulling back from the market for this reason. This would present challenges to those borrowers who already have interest only loans and wish to refinance, therefore resulting in further consumer detriment.

Q25 What is your view of our proposals for lenders' interest only policies?

135. Overall we support the proposals that lenders should outline clearly the parameters under which interest only mortgages are accepted, the controls in place and the overall lending appetite.

136. We do have some concerns with the proposal for the lender to take account of property prices in the area the property is situated in. This makes the assumption that the customer will remain in the area once they sell the property, which may not be the case, therefore we would question how relevant this is.

137. This also assumes that once the customer sells the property they would look to purchase another one. The CP refers to the lender considering whether it is reasonable to expect the property to have the potential to repay the capital and also enable the borrower to buy a cheaper property to live in, without having to rely on house price increases. However, we would question why the lender should default to this assumption, if the customer states that this is not their intention.

138. This proposal effectively requires the lender to assume the customer will always remain in homeownership, but this is not always the case. If the customer confirms it is their intention to either move away from the area and/or exit homeownership entirely, then the lender should be able to take account of this within their lending policies.

139. We would also question the explicit need for the policy to be signed off at Board level. Many lenders operate sub committees of the main board that deal with specific issues. For example, the risk committee may manage the overall risk strategy and would review the lending policy. It may be a conduct committee which ensures that the company is complying with conduct regulation, of which lending policy is an integral part. Where these committees operate with clear terms of reference and where they have been granted delegated authority from the Board, we would see no reason why this would not be considered acceptable.

140. We would therefore recommend that the draft rules are amended to take account of this structure.

Q26 What are your views on our approach to requiring lenders to assess the repayment strategy prior to entering into the mortgage?

141. It is right that the lender should assess that there is the potential for the repayment strategy to repay the loan, but the repayment of the mortgage is ultimately the responsibility of the customer.

142. We are still concerned that the approach by the lender to ensuring that the strategy has the ability to repay the loan, could be interpreted as the lender 'approving' that the strategy will perform and this could have consequences should this not be the case.

143. However, the need for the lender to maintain a clear and detailed record on a case by case basis, including the justification for the decision made, should mitigate the potential for the lender to be held liable for the future performance of the strategy.

144. We also remain concerned that some lenders will be unable to assess complex investment structures or pension plans in detail as they do not have the necessary in house expertise. The FSA should be mindful that some lenders may decide not to accept such strategies as part of their lending policy, which could place them at a competitive disadvantage to larger lenders that have the ability to utilise expertise from other areas of their business. The FSA needs to be mindful it is not creating an unfair playing field for smaller lenders in this respect.

Q27 What is your view of our proposals for the ongoing management of interest only loans? Do you foresee any practical issues?

145. We are supportive of the principle that the lender should check that a repayment strategy is in place during the term and we welcome the shift in policy away from checking the performance of the strategy.

146. The ability for the lender to approach this in a flexible way is welcome and we agree that the natural contact points during the term may make it easier for firms to engage with their customers.

147. As we have pointed out previously we are concerned that lenders may not have staff that are qualified to assess complex investment structures or pension plans. We would therefore recommend that where the repayment strategy is more complex, the lender is able to recommend that the customer seeks specialist advice to ensure the strategy is still on track. This will ensure the customer is clear that the lender is not responsible for the performance of the strategy, whilst ensuring the lender has acted responsibly in requiring the customer to review their strategy in detail.

148. We also agree with the proposed procedures for undertaking the review, in particular the steps the lender will consider if there is no longer a reasonable expectation that the repayment strategy will repay the mortgage. However, we are disappointed that the FSA has not sought to provide any clear guidance to firms as to what action they may take. The FSA has acknowledged this concern in paragraph 4.75 of the CP and so it is disappointing that further guidance has not been given.

149. We are aware of the thematic work which is currently being undertaken to assess if their is an issue with under performing repayment strategies of existing interest only mortages and we look forward to seeing the findings of this review. We are hopeful that the FSA will publish guidance to firms as a result of this review, which will clearly set out the regulatory expectation in managing customers without a repayment strategy. This should be incorporated into MCOB, rather than as a separate piece of guidance.

Q28 Do you have any comments on the proposed changes to the glossary term, or the consequential changes?

150. We have no issues with the proposed changes to the glossary term. It is helpful that the various definitions are tidied up and replaced with one. We agree that ‘repayment strategy’ is the most appropriate phrase to use.

Q29 Do you have any comments on the draft interest only rules set out in the draft *Mortgage Market Review (Conduct of Business) Instrument 2012* at Appendix 1? Do you think the rules reflect the stated policy intention.

151. We have no specific comments on the draft rules, other than the points raised previously with regards to the checking of the repayment strategy during the term. We believe the rules reflect the stated policy intention.

Section 5
Distribution & Disclosure

General Comments on Advised Sales

152. The BSA has been supportive of moving mortgage advising and selling away from being solely focussed on recommending or providing information on a product. A mortgage is the single biggest financial decision an individual will make and therefore we believe the advising and selling process should be focussed on holistic financial advice and/or information to ensure the mortgage is appropriate.

153. It is disappointing that the FSA has not sought to review the mortgage market from this perspective and instead has made the process more product focussed and further reduced the choice for the consumer as to how they manage their personal circumstances, by proposing to move to a fully advised market. This is exacerbated further by removing the requirement from the intermediary to assess affordability. A holistic approach to advice would see this as an integral part of the process, but instead it has been removed and replaced with a requirement for the intermediary to take account of the lender's affordability requirements and simply check that the consumer is likely to fit within those parameters.

154. Whilst we appreciate the rationale that some consumers may assume they have been given advice, when they have not, this is not in itself sufficient justification to require all consumers to receive advice.

155. The BSA believes that there is a risk that consumers may become less engaged if they are forced to take advice even if they don't require it. They may pay less attention and have less interest in the mortgage process on the assumption that they will be provided the best mortgage for their circumstances. At a time when the Government is implementing major reforms through the Universal Credit regime with the objective of putting consumers in control of their finances, this proposal seems to be at odds with the Government's policy.

156. Consumer choice is vitally important and many consumers will be able to make an appropriate decision for themselves, either on a pure execution only basis, or by obtaining some factual information, through a non advised sale. The FSA recognises that the mortgage market has worked well for the majority of consumers, therefore we would question whether moving to a fully advised market is really what is needed to enhance consumer protection.

157. The definition of advice, given in the CP is also too simplistic and does not adequately define the point at which the sale commences. We are concerned that the shift away from a personal recommendation will lead to the whole advice process being rejected rather than just the final product that is presented to the customer. We do not see how this would work in practice and therefore would question whether this is the right approach.

158. We are concerned that the focus of the CP is very much on the intermediary, with lenders being viewed as an after thought. This is a criticism we raised in our response to CP 10/28 and it is disappointing that this has not been taken on board.

159. Of particular concern is the lack of regard for lenders with a limited product range, where advice would be inappropriate and impractical.

160. We are concerned that the proposals capture back office staff involved in amending the terms of an existing contract, such as repayment type, term and product. This was specifically excluded from the Approved Persons regime, therefore we would have a situation where such staff would be required to give advice, but not be approved persons.

161. In addition, we do not believe that adequate analysis has been undertaken on the costs to a lender of moving to a fully advised market. We have undertaken some analysis with our members and we would urge the FSA to factor this into its own analysis to ensure the full impacts are understood.

162. Overall, we believe that better disclosure would solve many of the issues highlighted in the CP. Simple changes to the way in which the service is disclosed from the outset would allow the customer to make an informed choice, without forcing them through a process which they do not want or need.

Moving to a fully advised market

163. We have a number of concerns with the proposals as they stand, which are explained in detail below. However, fundamentally we do not agree that all consumers need advice, nor do we agree that any spoken or interactive dialogue would necessarily constitute advice. The FSA should review how non advised sales could continue, perhaps under a different label such as 'information only'.

164. We agree that there are some vulnerable consumers who should always be given advice, but we do not believe that there needs to be a blanket approach. In our view this is too simplistic and would not provide the consumer with any added protection, but would create significant upheaval to lenders, at a significant cost.

165. We do not believe that the current disclosure on the KFI is sufficient to ensure the consumer is aware of the service they have received and therefore it is this that has resulted in some consumers believing they have received advice, when they have not. Making the statement on the service received clearer, both on the KFI, but also orally at the start of the sale would in our view deliver better outcomes for the consumer. We have made some recommendations towards the end of this section, in relation to our proposed revisions to the sales process, which includes proposed disclosure.

166. We disagree with the assertion in the CP that it is immaterial whether the intermediary recommends a product or the customer chooses for themselves. The Perimeter Guidance is clear as to what is advice and what is information. This is not an immaterial distinction, hence our view that disclosure has not been adequate to make this clear to the consumer.

167. The consumer must be able to make an informed choice about the service they will receive. Therefore regardless of whether or not non advised sales remain, the customer must be able to make a choice at the start of the sale without having to receive advice and then reject it.

Interactive sales and the definition of advice

168. Notwithstanding our views on the approach to the consumer being able to choose the service they receive from the firm, we have specific concerns with the proposed definition of advice as stated in the CP.

169. We understand the simplicity of stating that advice commences once there is a spoken or interactive dialogue between the firm and the customer during the sale. However, we do not think this works in practice .

170. The difficulty with having such a simple approach, is that it is not clear at what point the sale commences.

171. The approach of using a spoken or interactive dialogue as the catalyst for advice commencing, may work where the customer is obtaining a mortgage through an intermediary, as the decision to approach an intermediary is usually on the basis of making a formal enquiry about obtaining a mortgage, but it does not work if the customer is contacting their lender, as this may be on a more informal basis.

172. For example, a customer could make an enquiry in a branch, or by telephone about the lender's current mortgage rates. The customer has no firm intentions as to whether they wish to obtain a mortgage from the lender, they are only interested in what is on offer. They wish to go away and think about it and they might come back to have a more detailed

discussion at some point, and they might do this with a number of different lenders. If the proposed rules are taken literally, the branch or telephone staff could not disclose this factual information without the customer going through the advised sale route for every lender they contact.

173. The rules need to be clear that the advised sale process commences once the customer makes a formal enquiry about taking out a mortgage and wishes to obtain detailed information about the merits of the products available and whether they are eligible for those products. This approach would, in our view, ensure that the rules work in practice.

Impact on lenders' staff

174. As we have stated previously we are concerned that the CP does not fully take account of the impact on lenders from a practical perspective, nor does it consider the specific costs that will be incurred, along with the wider implications of requiring all staff to provide advised sales.

175. We are concerned that the CP broadens the scope of staff that would be captured by the advice proposals, despite the Approved Persons near final rules explicitly excluding some lender staff from that regime. We are also concerned as to how the proposals work for lenders who offer a limited product range.

(i) Variations to the mortgage contract involving no new monies

176. The Approved Persons regime explicitly excludes lenders' staff involved in changes to the contract which involve no new monies being advanced. This includes the addition or removal of a party to the mortgage, rate switches, term extensions and changes to the repayment method. It also removes the switching of a mortgage contract from unregulated to regulated, again as long as no new monies are advanced.

177. The proposals in the CP, do not exclude such transactions from the advised sale requirements, which would lead to a perverse situation where lender advisors would be required to provide advised sales, but not be approved persons.

178. This also raises the issue of how the advised sale requirement interacts with forbearance. Is it the intention of the FSA that these would also have to be advised? If not how does the FSA intend to make the distinction between the two? It is not as simple as using the proposed 'payment shortfall' definition in Chapter 6 of the CP, as forbearance can be applied as a preventative measure, therefore there may be no obvious indicator to allow the distinction.

179. We would argue that the need to provide advice should be proportionate to the changes being made to the contract. Is it the expectation of the FSA that a 40 year old applying for a 5 year extension to the term and a 60 year old applying for an extension into retirement, both need an advised sale? Does the addition or removal of a party to the mortgage need to be an advised sale, particularly if this is as a result of a relationship breakdown? Surely in these instances legal advice is more appropriate, not product advice?

180. If a customer is moving their existing loan to a new property, again with no new monies, why is there a need for this to be an advised sale? The assessment the lender will make is with regards to the new security and LTV, the mortgage itself remains unchanged. What aspect of the transaction does the FSA see as requiring advice about the product?

181. In practical terms, the need for the lender to give advice where the amount borrowed is not increasing is illogical and impractical. We do not believe that this is the FSA's intention and we would therefore urge the FSA to bring the advised sale requirements into line with approved persons and exclude contract variations involving no new monies from the advised sale requirements.

(ii) Variations to existing contract involving new monies

182. We accept that where the customer is seeking to increase the amount borrowed that the individual involved in arranging this should be an approved person and we understand the logic of applying the advised sale requirements to these transactions.

183. However, we would argue that there needs to be an element of proportionality to the proposals, as not all new borrowing would be significant enough to require a fully advised sale.

184. This is particularly relevant in relation to further advances, where the additional amount borrowed is small and where the new borrowing may increase the loan only to the amount it was originally agreed for. Subject to the customer being able to demonstrate sufficient affordability we would question if the borrower needs to be provided with a fully advised sale in order to extend the additional borrowing.

185. Requiring lender advisors to always provide an advised sale, regardless of the amount of additional borrowing, could lead to some firms setting a minimum amount for further advances. Small further advances may prove too costly in terms of lender time and administration costs to provide the required advice. This could lead to the customer being driven to more expensive forms of credit, such as a personal loan or credit card, or to more expensive forms of secured borrowing via a second charge.

186. We would question whether this is the intention of the FSA and recommend that further analysis is undertaken to understand the full impact of the advised sale proposals on further advances.

(iii) Limited product ranges

187. There are a number of smaller lenders who offer a limited product range, some only offer one product. It is impractical for these lenders to provide advice and recommend a product, when there will only ever be one product to recommend.

188. In these situations, the lender, or intermediary is only able to determine if the customer is eligible for that product or not, which is clearly very different to giving advice.

189. Under the Mortgage Code, which was abolished with the introduction of FSA regulation in October 2004, there were three clear levels of service:

- Advice and a recommendation as to which mortgage is most suitable for you.
- Information on the different types of mortgage product we offer so that you can make an informed choice of which to take;
- Information on a single mortgage product only, if we only offer one mortgage product, or if you have already made up your mind.

190. These levels of service allowed for execution only sales specifically where the lender only offered one product, as the code recognised the impracticalities of an advised or even a non advised sale by these lenders.

191. We would strongly urge the FSA to consider how their proposals will work for such firms and allow the lender to continue to offer their product on an execution only basis whether the sale is interactive or not.

192. In addition to this, there will be some smaller building societies who will be required to offer a limited product range at various times, either as a result of limited funding tranches, or

more importantly as they have been instructed to do so by their supervisor under the guidance contained in the Building Societies Sourcebook.

193. Smaller building societies may at times be required to withdraw their fixed rates as they have reached the limit recommended in the sourcebook. We accept the FSA position that these limits have some flexibility, but there remains the potential that at some point that a building society will be required to amend its product range.

194. As a result, the choice of products available could be narrow and the ability to give advice becomes less practical, posing the same issues as those lenders who only offer one product.

195. We would therefore urge the FSA to consider how the proposals will work for lenders with a limited product range and to clarify the requirements on lenders in this situation.

(iv) Impact on lenders moving to advised sales

196. We are concerned that the cost impact on lenders has not been fully considered in terms of training existing staff to be able to provide advised sales. The impact assessment does not include any assessment of the costs involved in training existing staff, the time scales for doing so, the impact on remuneration and other HR costs.

197. The CBA has also not taken into account that some lender staff may be unable to fulfil the role of providing advised sales, as this was not the role they were recruited for. This has implications in terms of managing these individuals to another role within the firm, or as a last resort, resulting in redundancy from the lender.

198. The BSA has undertaken some work with its members to understand the likely impacts. However, we recommend the FSA conducts further, more detailed analysis prior to pressing ahead with a move to a fully advised market.

Staff training

The average cost per head of training staff who currently only offer non advised sales is **£1,532.**

Responses ranged from **zero** to **£4,000**. This is because some lenders already require certain standards, such as CeMAP to be obtained by their advisors, even where they offer only non advised sales. Age and skill sets of staff are also considered, as the amount of training required will vary by individual. In addition, there is each firm's own training and competency requirements to fulfil.

For some firms they will need to bring in external resource to complete the necessary training and this has also been factored in.

Ongoing monitoring and training costs have not been factored into this figure.

Staff remuneration

63% of respondents believed they would have to change staff remuneration as a result of moving to advised sales.

Of this 63%;

67% would increase staff salaries and **50%** would increase bonuses or other incentives. (respondents were able to select more than one option)

The average increase in salary expressed by value was **£5,600** per head, per annum. The average increase in bonuses or other incentives expressed by value was **£600** per head, per annum.

Some respondents expressed the increase by percentage. On average salaries would increase by **20%**, per head, per annum. Bonuses and other incentives would increase by **2%**, per head, per annum.

Staff levels and other HR costs
44% of respondents felt they would have to increase staffing levels as a result of moving to advised sales. However, it was difficult to quantify exactly how this would need to change until a full review had been conducted on existing staff. Some small lenders felt they may need to recruit more administrative staff to assist advisors. On average, recruitment costs for mortgage staff currently averages at £3,030 per head. **71%** of respondents believe this will increase as a result of needing to recruit more highly skilled staff. If a staff member was unable to complete the required training and competency requirements to carry out advised sales, respondents recognised that these individuals would either need to be given another role in the firm, or leave the company. On average it would cost **£1,970** to move an individual to another role and **£3,750** if an individual was to leave the company. These costs include HR and management related costs in resolving the situation with the individual staff member. **Notes:** Survey based on a cross section of BSA members ranging from those with mortgage assets over £5 billion to those with mortgage assets under £50 million, based on the BSA Yearbook 2011-12. Figures are based on new business only and exclude post completion staff, who may handle product switches and other contract changes. Costs per heads are based on full time equivalent (FTE) staff

Intermediary role in assessing affordability

Q30 Do you have any comments on our proposed approach to intermediaries' role in assessing affordability?

199. We remain unconvinced that the intermediary role should be restricted to no more than checking whether the consumer fits within the expected parameters of the lender's affordability assessment.

200. As we argued in our response to CP 10/28, assessment of affordability is one of the key aspects of the advising and selling process and therefore it should remain a requirement for the intermediary to do this.

201. We appreciate the FSA wishes to make it clear that the ultimate responsibility for assessing affordability lies with the lender and we are supportive of this approach. However, this does not mean that the requirement should be removed fully from the intermediary.

202. The removal of this requirement makes the process more product focussed, when we recommend a more holistic approach to affordability. This would assess what the customer could potentially afford now and in the future, taking account of potential life events. This would result in the advice being focussed on how much they should borrow, rather how much they could borrow from any one lender.

203. We recognise that the requirement still exists for intermediaries to assess foreseeable changes to circumstances, but removing the affordability requirement provides no footing for this assessment. We therefore fail to see how this will work in practice.

204. We would strongly urge the FSA to reconsider removing this aspect of the process.

Execution only

Q31 (i) Do you have any comments on our proposed approach which allows high net worth consumers and mortgage professionals to opt out of receiving advice and purchase on an execution only basis?

205. The proposed approach does not work for mortgage professionals and we do not believe that lenders would set up a separate process to exclude these customers from the advised sale process.

206. As we have stated previously the consumer must be able to make an informed choice about the service they will receive before the sale commences. This approach would mean that specific carve outs would not be required and would therefore ensure the process is transparent and straightforward.

207. We do not believe a specific exclusion is needed for high net worth and this explained in more detail in our response to section 10 of the CP.

(ii) Do you have any comments on our proposed definition of a 'mortgage professional'?

208. The definition of a 'mortgage professional' is broad in scope and could capture administrative staff, which we would assume is not really the intention. We would also question whether all parties need to be 'professionals' in order to proceed on an execution only basis, or if it will be sufficient for one party only to be defined as such. The rules are not clear in this respect.

209. Again, if the FSA amends the approach and allows the consumer to choose the service they will receive, we see no reason to have a specific definition and carve out for mortgage professionals.

(iii) Is there anything we can do to mitigate the risk of intermediaries using these exceptions to circumvent the rules?

210. As we have stated previously the consumer must be able to make an informed choice about the service they will receive before the sale commences. This approach would mean that specific carve outs would not be required and would therefore ensure the process is transparent and straightforward, with improved disclosure.

211. The record keeping requirements as to why the customer opted for the chosen service should ensure that the ability for the intermediary to lead the customer in choosing an execution only route should mitigate the risk of the rules being circumvented.

(iv) Are there any other customer types you think should be able to purchase on an execution only basis in an interactive sale?

212. Yes, as we have stated previously all consumers, with the exception of some 'vulnerable consumers', should be able to choose the service they will receive and not be defaulted to an advised sale automatically.

Non Interactive Sales

Q32 Do you have any comments on our proposed approach which allows consumers to opt out of advice when purchasing products online, or by post and allows them to purchase on an execution only basis.

(i) Internet Sales

213. The rules proposed in the MMR need to be fit for purpose for the future as well as the current market and therefore need to take account of how consumers will purchase a mortgage going forward.

214. Whilst the number of consumers currently purchasing a mortgage online is low, as stated in the CP, this does not mean this will remain the case in the future. The FSA needs to be mindful of this when assessing how internet sales interact with the proposed rules.

215. Internet sales do not fit comfortably into an advised sale process. As the FSA admits, the nature of internet sales can vary and include live and automated chat functions and the use of decision trees to help the consumer choose their product.

216. Internet sales in our view, fit within the definition of a non advised sale, where information can be provided to the consumer as they go through the online process.

217. As mortgages are a more complex product to buy online than many other financial products, such as insurance, the majority of consumers are unlikely to be able to proceed on a pure execution only basis. They are likely to have some questions at some point in the process. This is why many lenders offer a live or automated chat function which allows the consumer to obtain answers to their questions whilst remaining in the online process.

218. There is a difference between live chat and automated chat functions. Live chat generally involves the consumer interacting with a lender's advisor who will connect with them online. Automated chat responds to key words or phrases to give a 'best match' answer to the consumer's question.

219. The FSA has not made a distinction between the two and we would challenge whether automated chat functions are an 'interactive dialogue' and therefore would not be captured by the proposals regardless of how the FSA proceeds.

220. We believe there is a strong argument for retaining the non advised sale for at least internet sales. If the FSA believes that all face to face or spoken dialogue constitutes advice, then leaving internet sales as non advised would make that clear distinction between the two services, which the FSA believes is lacking currently.

(ii) Postal Sales

221. As we have stated previously, the Approved Persons regime explicitly excludes lender staff involved in changes to the contract which involve no new monies being advanced. This includes rate switches and product retention deals. We would argue that these transactions should be excluded from the advised sale requirements.

222. As a result, we do not agree with the assertion in the CP that where a lender writes to the consumer offering a new product, that this is considered to be an advised sale.

223. With regards to new business, we agree that where the lender will simply carry out the consumer's instructions, this will be excluded from being an advised sale.

Advising vulnerable consumers

Q33 (i) We are proposing that consumers who are vulnerable should always be advised and therefore will not be able to purchase their mortgage through a non interactive process. Do you have any comments on this approach?

224. We agree that some consumers should always have advice, as we recognise the detriment that has been evidenced via poor selling practices in the case of sale and rent back and the higher proportion of arrears for RTB customers.

225. We would question whether those borrowers consolidating debts should always need advice. Whilst the main purpose of raising additional funds may be for debt consolidation, this could be only a small aspect of the overall borrowing. We believe that further analysis is needed in relation to debt consolidation to determine if there is a suitable amount, below which advice is not mandatory. We would recommend a cut off based on the total percentage of the overall borrowing, to ensure the proposal remains appropriate for those consumers consolidating a small amount of debt.

226. We also have concerns with the definition of debt consolidation and do not believe this is sufficiently clear. We would also question whether this includes the consolidation of an existing secured loan into the first charge mortgage.

227. It raises the issue of consumers who have carried out home improvements on the property, initially funded by other borrowing for cash flow purposes (such as credit cards) who now wish to consolidate this onto the mortgage. It is unclear whether this would be defined as debt consolidation or home improvements. The FSA needs to be clear to ensure the rule is applied as intended.

(ii) What are your views on our proposal to allow high net worth consumers and mortgage professionals to opt out of receiving advice irrespective of whether they are considered to be vulnerable?

228. As we have stated previously, we do not agree that the definition for a mortgage professional works and we would recommend that this is not implemented. If a customer falls into one of the 'vulnerable' categories, the process should remain straightforward and the consumer should be required to receive advice.

229. We explain our views on high net worth customers in more detail in our response to section 10 of the CP.

(iii) Are there any other consumer types you think should always receive advice?

230. We do not believe there are any other consumer types who should always receive advice.

Rejecting Advice

Q34 Do you agree that, except in the case of sale and rent back, we should allow consumers to reject advice and proceed on an execution only basis?

231. As we have stated previously, we strongly support the consumer having a choice as to the service they will receive and we would argue this should occur before the sale commences.

232. Where the consumer initially opts for advice (or is required to have advice if the proposals remain unchanged), we agree that the consumer should be able to reject this and make a decision for themselves.

233. However, we would question the proposal that 'advice' is rejected as this a fundamental shift from the current practice.

234. Under the current advised sale rules, the advisor provides a personal recommendation as to the product that best meets the customer's needs. If the customer does not wish to proceed with that product, they are rejecting the personal recommendation, they are not necessarily rejecting the advice and we think this is an important distinction.

235. For example, the personal recommendation could be a 5 year fixed rate. The customer disagrees that 5 years is right for them and opts for a 2 year fixed. The advice that they have a fixed rate still stands, the consumer has only rejected the length of time the mortgage should be fixed for.

236. The concept that the consumer would reject the advice in its entirety is very unlikely in practice. If the consumer believes that the advisor recommended them to take a fixed rate, the fact they didn't go with the recommended product, would not in the consumer's view mean that they did not take heed of the advice. They have instead made an informed choice. In practice consumers would still have received advice, even when they no longer rely upon it. This creates another element of confusion that the FSA already believes exists regarding advised and non advised sales.

237. This practical issue, in our view, supports the retention of the non advised sale route, which allows the consumer to receive advice, but reject the personal recommendation if they are not happy with the specific choice of product. We would strongly urge the FSA to reconsider its decision to remove non advised sales.

Monitoring execution only business

Q35 (i) We are proposing that intermediaries monitor their execution only business. Do you have any comments on our proposed approach to monitoring?

238. If the proposals are implemented unchanged, we agree that execution only business should be monitored as suggested in the CP.

(ii) Are there any other steps we should take to ensure that consumers are protected when purchasing on a non-interactive basis. Eg should we place any other limitations on the types of consumers who are able to purchase online.

239. We do not believe that further limitations are appropriate and we would reiterate our views with regard to consumer choice about the service they receive and the need for non advised sales to remain, particularly for online sales.

Amending the approach to disclosure

240. The BSA believes that simple changes to the disclosure process would negate the need to force consumers through the advised sale route and would still provide the ability for non advised (information only) sales to be offered.

241. We do not believe that the current disclosure on the KFI is sufficient to ensure the consumer is aware of the service they have received. Making the statement on the service received clearer, both on the KFI, but also orally at the start of the sale would in our view deliver better outcomes for the consumer.

242. We would therefore propose that advised, non advised and execution only sales are described in the following way:

Advised: We will assess your personal circumstances and make a recommendation as to which product would be the most suitable for you.

Non advised (or information only): We will assess your personal circumstances and provide you with a selection of products to choose from. We will not guide you or provide a recommendation as to which one you should choose, but we will provide you with information to help you make that decision.

Execution only: We will not make an assessment of your personal circumstances, it is your choice which product you choose and we will arrange it for you. If you choose this option we cannot provide you with any assistance to help you make a decision.

243. We believe this approach is much clearer and ensures the consumer is clear as to what service they are receiving.

244. We recognise that some consumers who choose the non advised route, may actually require advice and therefore we recommend the onus is on the firm to recognise this and suggest the customer switches to an advised sale, as currently required under existing regulation.

245. We should make clear that irrespective if the service that the consumer selects the onus remains on the lender to lend responsibly.

Section 5
Sales Standards

Enhancing the sales standards

246. We are concerned that the intermediary role is being diminished to an extent which may cause consumer detriment, particularly in relation to the lending into retirement and interest only proposals, in relation to advised sales.

247. The CP states that the FSA does not wish to blur the distinction in responsibilities between the lender and intermediary, but by doing so would result in the consumer not having advice on two key areas and this is a concern.

(i) Lending into retirement

248. We agree that the issue about whether a mortgage runs into retirement is more about affordability, but the advice should be focussed on whether the customer *should* do this, not whether they *could*. As such we believe there is a strong argument that the intermediary should still be required to assess whether it is appropriate for the customer to run the term into retirement and the lender will be responsible for assessing whether that is affordable.

249. We think this distinction is clear, therefore the rule should be amended to require the intermediary to make this assessment.

(ii) Interest Only

250. We agree that the responsibility should remain with the lender with regards to the assessment of the repayment strategy, but again we would question why the intermediary is not required to provide advice on the proposed strategy, as this is an integral part of recommending whether or not an interest only loan is appropriate for the consumer?

251. We believe that there is a strong argument for the intermediary to assess whether an interest only loan is appropriate for the consumer, taking account of the proposed repayment strategy. The lender will be responsible for ensuring that strategy fits within their proposed lending criteria and has a likelihood of being able to repay the capital, as proposed in section 4 of the CP.

Consumer information about an intermediary's service

Q36 Do you agree that we should be specific about the appropriate method of disclosing service fees that are not simple flat fees?

252. We do agree that the FSA should be specific about the method of disclosing service fees that are not flat fees and we agree with the proposals set out in the CP.

253. We also welcome the clarification that these requirements do not apply to lender advisors.

Q37 Do you have any comments about our revised approach to the requirements for the messages on product range and remuneration to be given 'clearly and prominently'?

254. We agree with the proposed approach that consumers should be given this information 'clearly and prominently' ie orally as we recognise the limited use consumers make of the IDD.

255. However, in order to ensure an adequate record is retained in case of future queries or complaints, the lender is likely to continue to supply this information in writing.

Q38 Do you consider the combined IDD template remains useful with respect to mortgage service disclosure?

256. As per our response to question 37, we do agree that it remains useful and it is likely to continue to be used by lenders going forward.

257. As such we would support the proposal to keep the template up to date and available via the FSA website.

Scope of service

Q39 Do you agree that we should not apply the 'independent' and 'restricted' labels to the mortgage market, but instead require intermediaries to explain to the customer in clear and straightforward terms any limitations to their service?

258. We do agree that the FSA should not apply the 'independent' and 'restricted' labels as proposed in CP 10/28. In our response we recommended that the FSA consider the use of key phrases, therefore we welcome the revised proposals to proceed on that basis.

259. However, the draft rules do not take account of lender advisors and no guidance is given in respect of the description that lenders will be expected to use. In order to ensure consistency it would be helpful for the FSA to provide guidance for lenders as well as intermediaries.

Q40 Do you have any views about our updated proposals for product disclosure?

260. Our views remain unchanged from CP 10/28, we continue to support the proposals with regards to product disclosure and we have no issues with the proposed rules.

Draft Rules

Q41 Do you have any comments on the draft rules on distribution and disclosure as set out in the draft *Mortgage market Review (Conduct of Business) Instrument 2012*?

261. Aside from the comments made in response to some of the specific proposals, we have no further comments on the draft rules.

Section 6
Arrears Management

Q42. Do you have any comments on the proposed policy approach on the calculation of arrears charges?

262. In our response to CP 10/16 we agreed with the principle of ensuring that arrears charges are a fair reflection of the additional administration costs faced by the lender.

263. In general terms we believe that most firms already calculate fees in accordance with the rules. As such, we support the clarification provided by the revised rules on the types of fees which must not be taken into account.

264. We did have some concerns with the original proposal that would have prohibited smaller lenders from taking into account executive staff costs, where such staff are involved in the day to day management of arrears.

265. It is very welcome that the FSA has recognised this within the proposed final rules and provided an exception on this basis.

266. We were also concerned that the original proposals appeared to indicate that fees would need to be continually analysed and adjusted as appropriate. Again, it is helpful that the FSA has recognised that this is not the intention of the proposal and has been explicit in stating that firms should monitor for any significant cost variances as part of their ongoing management oversight.

Q43. Do you have any comments on the proposed policy approach on direct debit payments?

267. In our response to CP 10/16 we agreed with the proposals to limit the number of times fees for missed payments are charged. It is reasonable to allow firms to make two attempts to obtain payment by direct debit and levy a fee each time the payment fails. We also highlighted the mis-match between the stated policy and the draft rule and we are pleased the FSA has amended the rule in line with the intended policy.

268. We were supportive of the need for the proposals to allow flexibility for firms to undertake additional attempts to collect payment by Direct Debit. However, we recognise that this may incur additional charges for the borrower via their bank. Recognising that this is detrimental to the consumer who is already under pressure financially, we are supportive of the proposal to limit the number of times a direct debit is taken to two per month, regardless of whether a charge is levied by the lender.

269. With regards to the repeated failing of direct debit payments, we remain supportive of the FSA proposals in this respect. We welcome the further clarification that the lender can continue to attempt to collect payment by Direct Debit where it is not possible to make contact with the borrower and we support the clarification that this applies only to Direct Debits, rather than the wider definition of 'payment requests'.

Q44. Do you have any comments on the proposal to extend the application of MCOB 12.4 and 13.3 rules to include payment shortfalls?

270. In our response to CP 10/16 we agreed with the proposal to ensure the rules are applied to payment shortfalls and not just the technical definition of arrears and we remain supportive of this proposal.

271. However, we would reiterate the point made we made in response to CP 10/16 that we are supportive of widening the definition, subject to a common sense approach being applied by the FSA in relation to customers with very small arrears, such as a few pounds or pence. Under the proposed rules a customer 1p in arrears would be captured by the

requirements of MCOB 13, therefore the FSA need to be proportionate when discussing such cases with lenders.

Q45. Do you have any comments on the proposal to replace MCOB 12.4.1 (2) with a rule permitting firms to remove concessionary rates where there is a material breach of contract unrelated to a payment shortfall?

272. We recognise the concern that removing the concessionary rate for a borrower with payment difficulties, may have the effect of making that borrower's position worse. We also accept that although many lenders have terms and conditions which allow the concessionary rate to be removed, in practice few of them would enforce this. Our own analysis supports the FSA view.

273. Mutual lenders have a strong track record of effective arrears management and low levels of repossessions, therefore the need for them to remove the concessionary rate (for those that have that provision within their terms and conditions), is negated by the fact that few of their borrowers fall into serious arrears.

274. Of those that have sought to remove the concessionary rate, this has in the main been due to the customer not engaging with the lender once they have fallen into payment difficulties. As such we would suggest that lenders should continue to be permitted to remove the concessionary rate where the account is in serious arrears and contact with the borrower has not been possible.

Q46. Do you have any comments on the draft rules on arrears management as set out in the draft *Mortgage Market Review (Conduct of Business) Instrument 2012?*

275. We have no further comments with regards to the draft rules and, as drafted they achieve the intended outcome from the proposed policy.

Section 7
Other Conduct Matters

Data Requirements

276. We agree that the current regulatory reporting needs to be reviewed to ensure relevant data is captured from firms going forward.

277. In our view, the key objective should be to ensure the data collected is useful and relevant and delivers the information needed for the FSA to monitor the rules in place.

(i) Mandatory reporting of some optional PSD fields

278. We support the FSA intention of reviewing some of the current optional fields with a view of making them mandatory. We believe it would be sensible to capture data on the incentive rate end date, ERC end date and the initial gross interest rate on a mandatory basis.

(ii) Adding new fields

279. We recognise the desire to capture more information relating to income and expenditure. However, the FSA needs to consider carefully how this information will be captured, particularly where the affordability has been factored into the income multiple, as per our response to chapter 3, as it may not be possible to provide the breakdown suggested in the CP.

Section 8
Impact of Basel III

Q47: Do you agree that the new prudential requirements are unsuited to meeting the objectives of the MMR, specifically deterring high risk lending?

280. The prudential reforms under Basel III (and consequently, CRD 4) are significant and likely to change parts of deposit takers' business models. Basel III has different objectives to the MMR therefore the two should not be compared in this way. We do agree that Basel III is likely to deter higher risk lending as a consequence of its objectives.

281. The European manifestation of Basel III, CRD 4, is not yet final and changes could still be made. The FSA asserts nonetheless that these policy changes will not have a particular effect on mortgages relative to other loan classes. Generally, mortgages attract low risk weights (35%) in comparison with other lending such as unsecured household and corporate lending. But not all mortgages. Some are deemed higher risk and thus attract higher risk weights. This could have the effect of driving lenders to originate lower risk loans. This in turn could lead to some borrowers being unable to remortgage and lenders being unable to price risk accordingly.

282. Building societies are already subject to tighter controls than other institutions under the Building Societies Sourcebook.

283. Every society has adopted one of three lending approaches: traditional, limited and mitigated. Each of these models has a range of limits attached to them covering a wide variety of lending measures. Working with their supervisors, societies have been guided towards one of these lending approaches. We recognise that societies are able to move categories, if they are able to demonstrate they have the requisite expertise, information systems and accounting systems and controls in place, but we understand few have. This suggests that building societies' lending models may remain static. However, the FSA has recognised that societies do not always fit neatly into one approach and has permitted "pick and mix" between the three categories where appropriate.

284. Moving to a prescriptive sourcebook has imposed a tougher and more prescriptive regime on societies than banks or other lenders are subject to. We agree with robust lending criteria but believe all lenders should follow the same requirements. Some societies consider that the sourcebook has been a limiting factor in the number of loans they can offer at a higher LTV, for example. Higher LTV lending can be done carefully and in our view, there is no greater risk in building societies lending on higher LTVs than other lenders.

285. Our members consider that the sourcebook has not helped their businesses over the past few years; indeed some consider it has placed them at a competitive disadvantage. Banks and non-deposit taking lenders have not been subject to equivalent provisions and have been able to operate, unaffected by the various restrictions that apply to building societies.

286. When the sourcebook was first published, we called for a full post-implementation review within 12-18 months of it coming into force. We said such a review could address any harmonisation needed between the sourcebook and the final policy that emerged at the end of the MMR. We strongly suggest that this review is carried out once the MMR rules have been finalised.

Section 9
Non deposit taking lenders

Q48: Do you have any comments on the proposed risk-based capital requirement?

287. Overall we support the proposal for non-deposit taking lenders (non-banks) to be subject to a formal prudential regime on a solo basis. The regime will be applied only to those non-banks actively involved in first-charge regulated mortgage lending. This should reduce the lending risk in future transactions.

288. We acknowledge that the regime must be proportionate ie tailored to their business model. Anything that acts to "level the playing field" is encouraged. The consequences of the current financial crisis show that one of the reasons non-banks were able to lend irresponsibly and thus overheat the housing market in the UK was the complete lack of a prudential brake. A prudential framework should also act to slow down the entry and exit of such lenders to the market without reducing competition.

289. The FSA has proposed a minimum risk-based capital requirement comprising 8% of risk weighted assets (RWA) based on the standardised credit risk and securitisation chapters of BIPRU, with a 1% requirement applied to other relevant assets. We agree in general with that proposal but add that it should be reviewed 12-18 months after implementation - and thereafter every two years – to check that the regime is still fit for purpose. While the new regime will raise the capital required for new lending, particularly above 80% LTV, we think it may help promote responsible lending in the future.

290. To help the transition the FSA is proposing that the standardised credit risk and securitisation requirements are limited to those on-balance sheet assets that relate to lending activities or exposures to collective investment schemes entered into before the new rules are implemented. Any other tangible assets (including loans and securitisations entered into before the new rules are implemented) will be subject to the 1% other relevant asset charge. We consider these transitional arrangements to be appropriate.

291. We agree that non-deposit taking lenders should in future be subject to some form of capital buffers in view of the potential pro-cyclical impact of non-bank lending on asset bubbles and market volatility.

292. And finally, we are pleased to read that the FSA has decided against applying an operational risk change, as it would not have been appropriate given non-banks' business structure.

Q49: Do you have any comments on the proposed restriction on the eligible capital calculation?

293. We note the proposal to require non-banks entering into new lending to have at least 20% of eligible capital to be in the form of share capital and reserves less intangible assets ie the current MIPRU rule for some mortgage firms. While we agree with the FSA that non-banks pose a lower risk as they have no depositors, they still have the potential to destabilise market confidence – even if there were no customer detriment - particularly if more than one defaults at the same time. In view of this, we consider that the 20% figure could be raised to 25 or 30%.

Q50: Do you have any comments on this proposed liquidity regime?

294. Given the nature of non-bank business models, where there are no depositors and future funding requirements are generally known and covered, we agree that a quantitative regime would not be proportionate to any benefits – to the non-bank or to the regulator. We also agree that only those engaged in new lending should be subject to some form of liquidity regime. While the high level qualitative requirement proposed is an improvement, it may still be disproportionate for smaller non-banks. These are likely to be unduly affected by such a

potentially burdensome requirement. We therefore suggest that in its supervision, the FSA undertakes to apply this high-level requirement in an appropriate way.

Q51: Do you have any comments on the proposed scope and application of the regime?

295. In general, we agree with the scope and application. We consider that the new regime should apply only to those non-banks entering into new lending and not to those in run-off, which will remain on the current capital requirements set out in MIPRU (1% of tangible assets). Finally, we have no comments on the proposal to apply the new regime at solo level.

Q52: Do you have any comments on the draft rules set out in the draft *Prudential Sourcebook for Mortgage and Home Finance Firms, and Insurance Intermediaries (Non-Bank Lenders) Instrument 2012* at Appendix 1? Do you think the rules reflect the stated policy intention?

296. We have no comments on the draft rules and believe they reflect the stated policy intention.

Section 10
Tailoring for niche markets

Equity Release

Q53 Do you have any comments on our views, summarised in the table at the end of this chapter, about the MMR proposals which are either not applicable or where a straight read across to the equity release market is appropriate?

297. We have no specific comments and agree with the proposed read across for equity release.

Q54 What are your views on our proposal to treat the equity release market as a single market for regulatory purposes?

298. We have no strong views. For consistency we agree that it should be viewed as a single market.

Q55 Do you have any comments on the tailoring we propose in relation to execution-only sales following rejected advice and scope of service?

299. We agree with the tailored approach suggested to allow equity release borrowers to reject advice and opt for an execution only sale. However, we would also refer to our comments in response to the advised sale proposals, with regards to the concept of moving to a fully advised market.

Q56 Is any other tailoring required for the equity release market? If yes, please explain.

300. We do not believe any other tailoring is needed.

Q57 Overall, do you have any other comments on our proposed read-across of the MMR to the equity release market?

301. We have no further comments.

Home Purchase Plans

Q58 Do you have any comments on our views, summarized in the table at the end of this chapter, about those mainstream MMR proposals which are either not applicable or where a straight read-across to the Home Purchase Plan market is appropriate?

302. We do not believe it is appropriate to read across the advised sale requirements, which we explain in our response to question 59.

Q59 Do you have any comments on the tailoring we propose in relation to execution-only Home Purchase Plan sales following rejected advice and enhancing sales standards?

303. We do not believe it is possible to give advice on Home Purchase Plans and would refer to our response to section 5, with regards to lenders with a limited product range. For Home Purchase Plan providers, they are likely to offer one product only (as recognised in the CP), which the customer is either eligible for or is not. We therefore do not see what advice they would need to be given. As such we believe that Home Purchase Plan sales should be on an execution only basis.

Q60 Is any other tailoring required for the Home Purchase Plan market? If yes, please explain.

304. We do not believe that any other tailoring is required for Home Purchase Plans.

Q61 Overall, do you have any other comments on our proposed read-across of the MMR to the Home Purchase Plan market?

305. We have no further comments.

Sale & Rent Back

Q62 Do you have any comments on our views, summarised in the table at the end of this chapter, about those mainstream MMR proposals which are either not applicable or where a straight read-across to the Sale and Rent Back market is appropriate?

306. We agree that it is not appropriate to read across the majority of the MMR proposals. We do agree that these customers should always seek advice, but we would suggest that the advice should be from specialist money advisors, rather than mortgage advice. Under the Government's mortgage rescue scheme, which is effectively a sale and rent back option, all customers are required to seek free independent debt advice prior to proceeding with the scheme. We believe this should be encouraged for all sale and rent back borrowers as the nature of this advice is more suited to their circumstances.

Q63 Do you have any comments on the tailoring we propose in relation to not allowing Sale and Rent Back consumers to reject advice?

307. We have no further comments.

Q64 Is any other tailoring required for the Sale and Rent Back market? If yes, please explain.

308. We do not believe that any other tailoring is required for sale and rent back.

Q65 Overall, do you have any other comments on our proposed read-across of the MMR to the Sale and Rent Back market?

309. We have no further comments.

Bridging Finance

Q66 Do you have any comments on our proposal to define a bridging loan as a regulated mortgage contract with a term of 12 months or less?

310. We agree with the proposed definition for bridging finance.

Q67 Do you have any comments on how the affordability proposals should be applied to consumers taking our bridging finance?

311. We agree that in the main the affordability rules should only apply where the borrower is required to make regular monthly payments. However, we believe that firms should also give consideration to the customer's wider affordability should the exit strategy not be viable at the end of the term. This will ensure that lender's have considered whether the customer has sufficient income to enter an arrangement to repay the loan, should the exit strategy not be viable at the end of the term.

Q68 Do you have any comments on our proposed read-across of our interest-only proposals to bridging finance?

312. We agree with the proposed read across of the interest only proposals to bridging finance. The exit strategy is a key aspect to bridging finance, therefore it should always be adequately assessed by the lender.

Q69 Do you have any comments on our proposal that lenders consider the repayment or exit strategy of the borrower, and have a clear lending policy that reflects this?

313. We have no further comments.

Q70 Do you have any comments on our proposals about extending bridging finance loans?

314. We agree with the proposals with regards to extending bridging loans and have no further comments.

Q71 Are there any other factors that firms should consider in order to determine that a bridging loan is appropriate?

315. We agree with the proposals with regards to sales standards and have no further comments.

Q72 Do you have any comments on our proposal which requires that intermediaries who only offer bridging loans should describe the restriction on their service to the consumer?

316. We agree with the proposal that intermediaries should describe the restriction on their service to the consumer, if they only offer bridging loans.

Q73 Do you have any comments on the proposed prudential regime for bridging lenders?

317. We agree with the proposed prudential regime for bridging lenders.

Q74 Do you agree with our views, summarised in the table at the end of this chapter, about the MMR proposals which are either not applicable or where a straight read-across to the bridging finance market is appropriate?

318. We agree with the proposals with regards to the read across of the MMR to bridging loans and have no further comments.

Q75 In addition to the proposed tailoring set out above, is any other tailoring required for the bridging finance market? If yes, please explain.

319. We do not believe that any other tailoring is required for bridging finance.

Q76 Overall, do you have any other comments on our proposed read-across of the MMR to the bridging finance market?

320. We have no further comments.

High net worth lending

Q77: What are your views on our approach to high net worth consumers? Should we adopt a more freemarket approach, recognising that for some consumers, regulation is not needed to protect them from the decisions they make?

&

Q78: Would an elective approach similar to that adopted in the investment market be appropriate?

&

Q79: Would it be appropriate for all mortgage rules to be forgone?

321. In our view, the rules for high net worth customers are over complicated. We would recommend that where a high net worth customer is seeking a traditional regulated mortgage contract, they should be subject to the same requirements as any other borrower.

322. BSA members who lend to high net worth individuals, do not offer bespoke finance and will offer these borrowers the same range of products as they would any other borrower. As such, they are unlikely to take advantage of the tailoring and opt outs proposed in the CP and would apply the MMR rules in full.

323. For those high net worth borrowers who are seeking finance based on a structure which is not a traditional regulated mortgage contract, then a more tailored approach would be appropriate, with the ability to opt in or out of regulatory protection, similar to the approach used in the investment market. We recognise that this type of finance is more likely to be offered by larger and private banks, therefore applying the MMR, even in part, is unlikely to provide any additional consumer protection. As such a separate regime for these firms would be more appropriate.

324. With regards to advice, as per our response to section 5, we strongly believe that customers should be able to choose whether or not to receive advice, without always having to receive it and then opt out. On this basis, there would be no need for an opt out process for high net worth customers as they could choose to receive advice or not as per any other borrower.

Q80: Would it be appropriate for all regulatory protections for high net worth to be forgone or should some, such as redress, for example, be retained?

325. Where the contract is structured as a traditional regulated mortgage contract, the customer should be covered by all regulatory protection. Where the nature of the finance is not a traditional regulated mortgage contract, the regulatory protection will be determined by whether or not they opt in.

Q81: What are your views on defining high net worth consumers – what do you consider the appropriate figures for income and assets?

326. We believe the income figure used to define a high net worth borrower is too high. A more reasonable income figure would be £300,000, with assets of £3 million.

Q82: Do you agree that it is appropriate to extend the definition to include high net worth consumers acting as guarantors?

327. In the context of our response to question 77, where the contract is a traditional regulated mortgage contract, the same provisions should apply to guarantors.

Q83: Do you have any comments on how the affordability proposals should be applied to high net worth consumers?

328. As per our response to question 77, the affordability rules should be applied in the same way as it would be to any other borrower taking out a traditional regulated mortgage contract.

Q84: Do you have any comments on our proposal to extend the tailored disclosure rules to high net worth consumers?

329. As per our response to question 77, the disclosure should be applied in the same way as they would be to any other borrower taking a traditional regulated mortgage contract.

Q85: Do you think that to achieve this, an elective approach similar to that adopted in the investment market would be appropriate?

330. Where the finance is structured on a basis which is not a traditional mortgage contract, we agree an elective approach would be more appropriate.

Q86: Do you agree with our views summarised in the table at the end of this chapter about the MMR proposals which are either not applicable or where a straight read-across to high net worth lending is appropriate?

331. As per our response to question 77, we do not believe a tailored approach is necessary where the finance is structured as a traditional regulated mortgage contract.

Q87: In addition to the proposed tailoring set out above, is any other tailoring required for high net worth lending? If yes, please explain.

332. We do not believe any further tailoring is required for high net worth borrowers.

Q88: Overall, do you have any other comments on our proposed read-across of the MMR to high net worth lending?

333. We have no further comments

Business Lending

Q89: What are your views on our approach to business lending? Should we adopt a similar approach to that proposed for high net worth consumers, recognising that for some consumers, regulation is not needed to protect them from the decisions they make?

&

Q90: How would we draw a line between those business borrowers able to take the risk and those who are not?

334. We recommend that where the loan is solely for business purposes, it should be carved out of MCOB. Loans which have an element of capital raising for business purposes should be treated as a regulated mortgage contract and be subject to the same rules as any other borrower.

335. In our view this provides a clear distinction and will still provide an element of protection for those borrowers who may be taking the loan as a last resort to keep their business afloat. The affordability assessment and assessment of income by the lender is likely to show that the business may be struggling therefore a risk decision will be taken under the protection of MCOB as to whether or not to lend.

Q91: How would we prevent this proposal from being exploited as a means of circumventing our affordability proposals? Q92: Would it be appropriate for all mortgage rules to be forgone or should some, for example the arrears rules, be retained?

336. If the proposal is taken forward as per our suggestion in question 89, we do not see how this could be easily circumvented. As recognised in the CP some lenders may already be offering business lending via a further advance or remortgage and they may not be aware they are doing so, therefore retaining the protection of MCOB in these circumstances is sensible.

Q93: Do you have any comments on how the affordability proposals should be applied to business borrowers?

337. As per our response to question 89, if the loan has an element of capital raising for business purposes, the full affordability rules should be applied.

Q94: Do you have any comments on the proposed approach to professional standards in business lending?

338. We would support the requirement for business sales staff to be included in the training and competency regime, regardless of whether our suggestion as per question 89 is taken forward.

Q95: Do you agree with our views summarised in the table at the end of this chapter about the MMR proposals which are either not applicable or where a straight read-across to business lending is appropriate?

339. As we have stated previously, we believe that if the loan has an element of capital raising for business purposes, the full regime should apply. If the loan is solely for business purposes, it should be excluded from MCOB.

Q96: In addition to the proposed tailoring set out above, is any other tailoring required for business lending? If yes, please explain.

340. We do not believe any further tailoring is required for business lending.

Q97: Overall, do you have any other comments on our proposed read-across of the MMR to business lending?

341. We have no further comments.

Q98: Do you have any comments on the draft rules specific to niche mortgage markets in the draft Mortgage Market Review (Conduct of Business) Instrument 2012? Do you think the rules reflect the stated policy intention?

342. We have no further comments.

Annex 1
Cost Benefit Analysis

343. We welcome the recognition that ‘facts of life’ or life events (such as unemployment and divorce) are a key driver of impairment. [Page A1:5, para 19]

344. As stated in paragraph 15 of Appendix A1, there is considerable subjectivity in the cost-benefit analysis:

> “the decision on whether to proceed with the proposed rules has to be based on social and political judgements, but the trade-offs involved are best informed by the results of our well-being analysis”.

345. We appreciate that a good deal of uncertainty is inherent to any modelling of the mortgage market, where there are a large number of variables and limitations to the available data. We appreciate that the FSA’s cost benefit analysis has attempted to use the available data in a systematic way as far as possible, but we believe that the explanation for how the well-being weights have been arrived at could be more fully explained.

346. These well-being estimates result in the ultimate threshold for the reforms being set at a ratio of the loans that would have become impaired to all loans prevented or reduced by the MMR of 20-22%. This threshold reflects the distress caused to borrowers being impaired being greater than the distress caused to consumers who are in some way excluded from the market.

347. These well-being estimates are drawn from analysis of the British Household Panel Survey from 1991-2008. Given the fundamental changes since the 1990s in the mortgage and other consumer credit markets, it might be reasonable to place more weight on more recent well-being findings. Experiences from the 1990s might not be representative of today’s financial markets.

348. Also, obtaining mortgage finance to purchase a property is not just about well-being (or conversely, reducing distress). We appreciate that is extremely difficult to assess the benefits of avoiding payment problems relative to the benefits to a consumer being able to buy the property he or she desires. But as there is such considerable importance being put on these well-being scores we believe it is important that they are more fully explained.

349. Furthermore, Q104 asks for views on the judgement of the Executive and Board of the FSA that the benefits enjoyed by the c.30% of borrowers who would otherwise get into payment difficulties outweigh the costs suffered by the c.70% affected who would not have got into payment difficulties. Given this is central to the analysis, we would like the Executive’s and Board’s reasoning behind this judgement to be more fully explained.

Annexe 2
Equality Impact Assessment

Q105 Do you have any comments on the age-related issues discussed above?
&
Q106 Are there any other age-related impacts from our proposals not highlighted above? If yes, please provide details.

350. Under the impending law, contained within the Equalities Act 2010, regarding age discrimination in services, firms are able to set age related parameters in lending policy where it can be justified as managing risk. Therefore firms may apply tighter controls to older borrowers to ensure that they have adequately assessed affordability. We therefore agree that older borrowers may be impacted by the proposals under the MMR, but that this is not a discrimination issue.

351. However, we are concerned with the proposal for the lender to take the state retirement age as the default age for retirement. We recognise the FSA's desire to have some form of benchmark for lenders however; we are not convinced that the use of the state pension age is the right option. This is not necessarily an indicator of when an individual will retire, only when their state pension becomes payable. As such it may not be most suited to the customer's circumstances and it could conflict with the age discrimination laws under the Act.

Q107 Do you have any comments on the disability-related issues discussed above?
&
Q108 Are there any other disability-related impacts from our proposals not highlighted above? If yes, please provide details.

352. We do not believe the rules will result in any disability related discrimination issues. Although we would urge the FSA to consider how Government schemes such as Homeownership for People with Long Term Disabilities (HOLD) will work within the interest only proposals. We would urge the FSA to consider an exemption where interest only is used in relation to a Government affordable housing scheme, specifically for people with disabilities.

353. This will ensure that lenders will be able to continue to support the scheme, without creating unintended loop holes to the rules.

Q109 Do you have any comments on the gender-related issue discussed above?
&
Q110 Are there any other gender-related impacts from our proposals not highlighted above? If yes, please provide details.

354. We do not believe the rules will result in any gender related discrimination issues, although we do have some concerns with regards to pregnancy and maternity leave, which we explain in response to question 111.

Q111 Do you have any comments on the pregnancy and maternity-related issue discussed above?
&
Q112 Are there any other pregnancy and maternity-related impacts from our proposals not highlighted above? If yes, please provide details

355. As per our response to question 11, we remain concerned as to how the requirement to assess foreseeable changes to circumstances interacts with existing discrimination laws

356. The requirement for lenders to 'make reasonable enquiries' to ascertain information about changes to income and expenditure could result in the lender indirectly discriminating on the grounds of gender.

357. Where a borrower discloses that she is pregnant or on maternity leave, the underwriting decision taken by the lender as to whether or not to lend is one of risk and we accept that the lender therefore has a duty to ensure that the mortgage will remain affordable.

358. However, the issue arises with regards to how far the borrower should be pressed on regards to their intentions to return to work and future income and also whether the same questions are directed at male borrowers. The impending changes to the sharing of maternity leave means that questions with regards to affordability and plans to return to work should always be directed to both borrowers.

359. We believe the FSA has a duty to ensure that lenders are acting in accordance with equalities legislation, therefore in order to ensure this is the case, we believe that it should be explicit within MCOB that when assessing foreseeable changes to circumstances, firms should take account of the protected characteristics under the Equalities Act 2010.

360. We also believe the FSA should provide guidance in respect of the definition of 'reasonable enquiries' and the way in which a customer should be questioned, to ensure that the lender does not indirectly discriminate by asking inappropriate questions in order to comply with the proposed affordability rules.

361. We would therefore suggest that the guidance states that lenders should ask the question as follows:

'Are you aware of any future changes to your circumstances that are likely to impact your ability to meet your monthly mortgage repayments?'

362. The lender will then act upon the response to the question in accordance with their lending policy. If the borrower answers 'no', the lender will not be expected to undertake any further questioning and will have been deemed to have satisfied the regulatory requirement.

Q113 Are there any race-related impacts from our proposals that we should consider? If yes, please provide details.

363. We do not believe the rules will result in any race related discrimination issues.

Q114 Do you have any comments on the religion-related issues discussed above?

&

Q115 Are there any other religion-related impacts from our proposals not highlighted above? If yes, please provide details.

364. We do not believe the rules will result in any religion related discrimination issues.

Q116 Are there any sexual orientation-related impacts from our proposals that we should consider? If yes, please provide details.

365. We do not believe the rules will result in any sexual orientation related discrimination issues.

Q117 Are there any transgender-related impacts from our proposals that we should consider? If yes, please provide details.

366. We do not believe the rules will result in any transgender related discrimination issues.

Q118 Do you have access to, or know of, any statistics regarding the mortgage needs and habits of groups with protected characteristics that could help us with our analysis? If yes, please provide details.

367. The BSA does not collect data on this basis from its members.

Guidance for firms on the Equalities Act 2010.

368. Overall, we do not believe that the MMR proposals will result in a direct conflict with the equalities legislation. However, it would be helpful if the FSA and the Government's Equalities Office (GEO) worked together to produce some coherent guidance for firms in relation to the interaction of affordability requirements under the MMR and the Equalities Act 2010. This will ensure that lenders are not inadvertently being required to breach the Act in order to comply with MCOB, or vice versa.

369. The BSA, along with the CML has met with the GEO who are very willing to engage on this issue. A joined up approach between the industry, the FSA and GEO would be welcomed.

Contact

370. This response has been prepared by the BSA in consultation with its members. Queries should be directed to Paul Broadhead (paul.broadhead@bsa.org.uk)