

29 October 2020

Dear CEO/Board of Directors

**Portfolio Strategy: Mortgage Intermediaries**

We are writing to:

- set out our view of the key risks mortgage intermediaries pose to their consumers or the markets in which they operate
- outline our expectation of mortgage intermediaries, including how firms should be mitigating these key risks
- describe our supervisory strategy and programme of work to ensure that firms are meeting our expectations, and harms and risks of harm are being remedied and/or mitigated

As part of [our approach to supervision](#), we group firms into portfolios based on their business models. Each portfolio is made up of firms with broadly similar business models. We have allocated your firm to the **Mortgage Intermediaries** portfolio.

We recognise firms allocated to other portfolios may also be involved in mortgage intermediary activity so we are publishing this letter on our website. You should consider the degree to which your business presents such risks and assess your strategies for mitigating them.

Our Mortgage Intermediaries supervision strategy covers the period to December 2021 and includes a programme of work to mitigate the harms we have identified, including second charge and lifetime mortgage advice. We will write to you after the end of this period to provide an updated view of the key risks posed by firms in this sector and our supervisory plans.

**Firm business models**

Mortgage intermediaries vary significantly in their size and type of business. They range from sole advisers to networks with a large number of Appointed Representatives (ARs). Many intermediaries focus primarily on mainstream mortgages, providing advice to first time buyers,

home movers and those looking to refinance current borrowing. Other intermediaries focus on more niche activities such as lifetime mortgage advice or second charge lending.

### **The market is working well but there are potential harms**

Our Mortgages Market Study (MMS) ([MS16/2](#)) found that the mortgage market works well in many respects; engagement is high, and consumers are getting mortgages that are suitable and affordable. However, the MMS identified 3 potential harms relating to our mortgage advice and selling standards:

- our rules and guidance may be a barrier to developing tools that help consumers choose a mortgage
- consumers looking to buy an execution-only mortgage (ie without advice) are diverted to advice; execution-only sales channels are not always easy to use
- while many consumers get a good deal, many could be overpaying for their mortgages, even when they get advice

To address these harms, we consulted on changes to our mortgage advice and selling standards, and have recently issued a Policy Statement ([PS20/01](#)) which summarises the feedback we received and sets out our final rules.

The changes we have made make it easier for firms to present options to consumers without giving regulated advice. They help firms make execution-only sales channels easier to use and, alongside recent changes to our responsible lending rules, they reduce regulatory barriers and help consumers get a mortgage that is right for them. These 2 changes complement each other to deliver the outcomes we want to see.

### **Our view of the key drivers of harm**

To assess how firms in the portfolio could cause harm, we analysed the information available to us about firms' strategies and business models. We considered a range of information and data, including firms' regulatory histories, and the number and nature of complaints.

To direct our work, we set out to identify the most apparent drivers of harm across the portfolio. We have several areas of concern which may lead to consumers and markets being harmed that you should consider and address:

- Firms advise their customers to purchase an unsuitable product which does not meet their needs. Firms should be able to clearly demonstrate why their customers have been advised to take a product. The customer should also understand the reason for the recommendation.
- Customers potentially pay excessive fees and charges for the service they are provided. There is also a risk that customers are unclear about the fees they are paying and the implications when they are added to the loan.
- The risk of fraud, both in terms of firms having inadequate systems and controls and risk management frameworks (leading to them being used to facilitate financial crime), and firms not being fully aware of the threats of cyber-attacks (leading to consumer data being compromised).

The above potential harms were identified before coronavirus (Covid-19), but awareness of these is even more important in the current environment, as each has the potential to exacerbate the difficulties customers are facing. To support customers, we recently introduced measures to help customers with short-term payment difficulties. We will be closely monitoring the impact of these, as well as the broader impacts of Covid-19, over the coming months.

### **Our area of focus for supervision work**

In prioritising our work, we will focus on second charge and lifetime mortgages.

**Second charge mortgages:** Second charge brokers generally serve customers who may be less able to access mortgages from their existing lender or the mainstream market. Many require second charge mortgages to raise funds for debt consolidation and/or home improvements. We will review a sample of firms' advice in this area, to consider:

- the suitability of the advice
- if customers are getting a product that meets their needs
- if customers have understood the product and have been treated fairly throughout the process

We will also be considering how the fees and charges payable by the customer are described to them and whether these may be considered excessive. We will aim to carry this work out during 2021.

**Lifetime mortgages:** We recently published the [findings](#) from our work on later life lending, in which we reviewed lifetime mortgage advice provided by several firms. Our findings were mixed, identifying 3 areas of concern:

- personalisation of advice
- insufficient challenging of customer assumptions
- lack of evidence to support the suitability of advice

We will follow this up to assess if firms have made any necessary changes as a result of our published findings. Before we do this, we will allow firms time to assess what they need to do, and to introduce and embed any changes required. If we find that firms have not made the necessary changes to mitigate any previous harms we identified, we will consider further intervention and appropriate action.

Again, we will be investigating how firms describe the fees and charges payable to the customer and whether these might be considered excessive. We aim to carry this work out in the first half of 2021.

The impact of Covid-19 may exacerbate the risk of unsuitable advice, particularly if consumers seek to address any short-term financial pressures caused by the crisis without understanding any longer-term implications. We are also concerned that advisers seek to address their own income shortfalls by providing services where they may not have the relevant experience.

We will consider this within our work but, more generally, we will also prioritise the following areas across the portfolio:

### **Mortgage fraud is an inherent risk within the sector**

We have an operational objective to protect and enhance the integrity of the UK financial system. Mortgage fraud is an inherent risk within the sector, and it is essential that firms operating in this area have sufficient controls in place to prevent their firm being used to commit fraud. Firms should also remember they are responsible for reporting any wider suspicions of fraudulent activity and have a statutory duty to report this.

Firms should ensure that appropriate due diligence is carried out on any adviser, AR or introducer it uses. This should include monitoring the quality of business, taking steps to improve introducers, advisers and ARs' understanding of the firm's expectations, and being bold in addressing any issues it may encounter. We expect firms to be able to spot inaccurate or implausible information, including payslips, accountants' certificates, tax returns or bank statements.

We will continue to actively monitor the risk of fraud within the portfolio via our mortgage fraud strategy and will take the appropriate action where necessary. This will include contacting individual firms where we identify concerns.

### **Firms should be aware of cyber risks**

[Cyber risks](#) pose a threat to all financial services firms, including mortgage intermediaries. Firms should be aware of the threat and be able to defend themselves effectively, responding proportionately to cyber events.

We will continue to monitor the risk of cyber related issues that could cause harm to consumers and act where required. Firms are reminded that, under Principle 11 of the FCA's Principles for Business, they must deal with their regulators in an open and cooperative way, and must disclose to the FCA anything relating to the firm of which we would reasonably expect notice. This would include making us aware of material cyber incidents and where any customer harm occurs as a result of an attack.

Firms may find it useful to read our recent [shared policy summary](#) and [consultation papers](#) on our new requirements to strengthen operational resilience in the financial services sector. We would also refer you to our [cyber insights document](#) that highlights a number of industry insights on cyber resilience.

### **Governance and oversight**

Firms should have the appropriate oversight in place for all advisers, including any ARs. We will engage with those firms where we have identified concerns about whether the oversight in place is sufficient and there is risk of harm to consumers.

Where firms increase their number of advisers and/or ARs we would expect to see a corresponding increase in resources to ensure that adequate systems and controls are maintained. Where we see significant growth in firms we will contact them to assess if the changes made to oversight arrangements are appropriate.

Operational and financial pressures have increased due to the impact of Covid-19. This has the potential to turn into harm for consumers. For all firms, appropriate governance and effective systems and controls are key in balancing the needs of their customers and that of their businesses. We expect firms to consider the impact of Covid-19 and how this has affected customers when making any decision in relation to the advice they provide.

### **We expect appropriate oversight of trading names**

Firms can use trading names and, when used, the trading name should be added to the Financial Services Register. However, a firm must not add a separate and independent unauthorised firm as a trading name and allow it to carry out a regulated activity without being authorised or being an AR.

Firms or individuals conducting business in their own right should not be registered as a trading name but should instead apply to be directly authorised or become an AR. [PERG 2.3.7G](#) provides guidance on the factors that we think are relevant to whether a person is to be treated as carrying on their own business or that of the person they are working for (the 'principal' firm). This includes the degree to which the person is integrated into the principal firm's business, and the degree of control the principal firm has over the person.

Firms or individuals who carry out regulated activities in their own right, without being authorised or being an AR, risk committing a criminal offence. In this situation, the authorised firm may also be breaching our Threshold Conditions or Principles for Businesses. Customers may also not have Financial Ombudsman Service (FOS) or Financial Services Compensation Scheme (FSCS) protection.

As we have indicated, we expect firms to have appropriate oversight of their ARs or advisers. We expect similar oversight over the use of trading names. Customers dealing with an AR or trading name must be clear who is providing the advice and who is ultimately responsible for that advice.

We have seen firms in the portfolio with a large number of trading names, and we will be contacting some of these firms to understand their business models, how their trading names are used and the oversight in place.

### **Brexit**

The UK left the EU with a Withdrawal Agreement on 31 January 2020 and entered a transition period, during which it will negotiate its future relationship with the EU. The transition period is due to operate until 31 December 2020. During this time EU law will continue to apply in the UK and passporting will continue. As matters develop during the course of this year, you will need to consider how the end of the transition period will affect you and your customers, and what action you may need to take to be ready for 1 January 2021. For information on Brexit, including what the transition period means, visit our [website](#).

## Next steps

We expect you to take notice of the areas of concern we have set out. You should look at your business, consider whether there are changes you need to make and act to reduce harm or potential harm to consumers. We will seek to identify firms across the portfolio, large and small, who appear to cause such harms.

The Senior Managers and Certification Regime (SM&CR) came into force for firms such as yours in December 2019. You must ensure your firm has implemented the SM&CR effectively. We will assess how firms have allocated individual responsibilities across their Senior Managers, and how those Senior Managers discharge their personal accountability. We expect them to create a healthy culture where the risk of misconduct is minimised. For further information, please see our [SM&CR Guide](#).

Your firm has until 31 March 2021 to ensure all staff in Certified roles are fit and proper to perform those roles. You must identify a Senior Manager as having individual responsibility for ensuring your firm carries out proper assessments of Certified staff, and those who do not meet fit and proper standards cannot be certified. Particularly where firms need to do a significant number of Certification assessments, we will challenge those firms whose assessment processes do not result in some individuals being found not to meet these standards.

Senior Managers and Certified staff should already have been trained on our Conduct Rules, and your firm also has until 31 March 2021 to train its other staff. This training must ensure that staff understand how the Conduct Rules apply to them. We will challenge the adequacy of training programmes which consist only of simple e-learning packages or presentations.

Where we find failings in implementing the SM&CR, we will hold Senior Managers with relevant responsibilities to account.

We will be proactively engaging with firms over the period through our planned programme of work. Our reactive supervisory work will be supported by wider engagement to allow us to clarify our expectations of firms, identify harms and ensure appropriate mitigation is put in place. We will act where we identify that firms have not put customers at the heart of how they do business.

We expect firms to keep up to date with regulatory development generally and with the areas covered in this letter. If you haven't already, we would recommend you sign up to our monthly [regulation round-up](#) newsletter.

If you have any questions please contact your normal supervisory contact on 0300 500 0597. This is the primary point of contact for your firm's day-to-day interactions with the FCA. Also, see our website on how to contact us: <https://www.fca.org.uk/contact>.

However, we recognise there may be occasions when your firm faces urgent issues of strategic importance. In such significant circumstance, please contact me on 0131 301 2052 or at [andrew.kay@fca.org.uk](mailto:andrew.kay@fca.org.uk). If I am not available, then please contact one of my managers, Craig Mason, on 0131 301 2060 or at [craig.mason@fca.org.uk](mailto:craig.mason@fca.org.uk).

Yours sincerely

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