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Financial Services Authority

# Mortgage Market Review:

Distribution & Disclosure

November 2010



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**Annex 1:** Cost-benefit analysis

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**Appendix 1:** Draft Instruments

The Financial Services Authority invites comments on this Consultation Paper. Comments should reach us by Friday 25 February 2011.

Comments may be sent by electronic submission using the form on the FSA's website at:

[www.fsa.gov.uk/Pages/Library/Policy/CP/2010/cp10\\_28\\_response.shtml](http://www.fsa.gov.uk/Pages/Library/Policy/CP/2010/cp10_28_response.shtml).

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**A confidential response may be requested from us under the Freedom of Information Act 2000. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by the Information Commissioner and the Information Tribunal.**

Copies of this Consultation Paper are available to download from our website – [www.fsa.gov.uk](http://www.fsa.gov.uk). Alternatively, paper copies can be obtained by calling the FSA order line: 0845 608 2372.

# List of acronyms used in this Consultation Paper

APER	Statement of Principles and Code of Practice for Approved Persons
CBA	Cost-benefit analysis
CCA	Consumer Credit Act
CCD	Consumer Credit Directive
CCJ	County Court Judgement
CFEB	Consumer Financial Education Body
CML	Council of Mortgage Lenders
COBS	Conduct of Business Sourcebook
CP	Consultation Paper
CPD	Continuing Professional Development
CPMA	Consumer Protection and Markets Authority
DP	Discussion Paper
DRO	Debt Relief Order
EU	European Union
FIS	Financial Information Statement
FOS	Financial Ombudsman Service
FPC	Financial Policy Committee
FSMA	Financial Services and Markets Act 2000
HPP	Home Purchase Plan
IDD	Initial Disclosure Document
KFI	Key Facts Illustration
LTV	Loan-to-Value (ratio)
MCOB	Mortgages and Home Finance: Conduct of Business sourcebook

MLAR	Mortgage Lending and Administration Return
MMR	Mortgage Market Review
PRA	Prudential Regulatory Authority
PS	Policy Statement
PSD	Product Sales Data
QCF	Qualification and Credit Framework
RMAR	Retail Mediation Activities Return
RDR	Retail Distribution Review
SYSC	Senior Management Arrangements, Systems and Controls
TC	Training and Competence sourcebook
TRN	Transaction Reference Numbers

# 1 Introduction

- 1.1 Just over a year ago, in October 2009, we published our Mortgage Market Review (MMR) Discussion Paper (DP09/3).<sup>1</sup> This drew on comprehensive research into the effectiveness of existing regulation, a significant body of supervisory work and findings from thematic reviews. We identified several failings in market practice and regulation. The crisis further highlighted many of these.
- 1.2 The DP set out the case for regulatory reform of the mortgage market. Our two key objectives are to create a sustainable mortgage market, and a market that is flexible and works better for consumers. Since the DP we have taken several steps to deliver these improvements. We first consulted on strengthening our arrears rules and extending the Approved Persons regime.<sup>2</sup> This was followed by a consultation on responsible lending.<sup>3</sup>

## Distribution proposals

- 1.3 The focus of our proposals for regulatory reform so far has largely been on the lender. This Consultation Paper (CP) turns to the mortgage sales process and the role of the seller (both intermediary and branch based). In Chapter 2, we set out our proposals for:
  - reforming the mortgage sales process by removing any regulatory requirement on intermediaries to assess affordability while at the same time requiring intermediaries to assess appropriateness in every sale (page 14/15);
  - requiring that all those selling mortgages hold a mortgage qualification and ensuring appropriate professional standards (page 16); and
  - strengthening the current sales standards (page 17).

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1 DP09/3: *Mortgage Market Review*, (October 2009): [www.fsa.gov.uk/pubs/discussion/dp09\\_03.pdf](http://www.fsa.gov.uk/pubs/discussion/dp09_03.pdf)

2 CP10/2: *Mortgage Market Review: Arrears and Approved Persons*, (January 2010): [www.fsa.gov.uk/pubs/cp/cp10\\_02.pdf](http://www.fsa.gov.uk/pubs/cp/cp10_02.pdf)

3 CP10/16: *Mortgage Market Review: Responsible Lending*, (July 2010): [www.fsa.gov.uk/pubs/cp/cp10\\_16.pdf](http://www.fsa.gov.uk/pubs/cp/cp10_16.pdf)

## **Disclosure proposals**

- 1.4 Disclosure has not delivered the outcomes we had hoped for and, consistent with the approach already taken in the investment and insurance markets, we propose moving to a policy position that focuses on early disclosure of key pieces of information, rather than the prescription of the form of that information. In Chapter 3, we set out our proposals for:
- replacing the requirement for an Initial Disclosure Document (IDD) with a requirement to disclose information on remuneration and scope of service early in the process (page 24);
  - replacing our existing scope of service labels with the Retail Distribution Review's (RDR) 'independent' and 'restricted' labels (page 26);
  - removing the requirement for an independent firm to provide consumers with a fee option (page 27); and
  - changing the trigger points for the Key Facts Illustration (KFI) to minimise information overload (page 29).
- 1.5 A detailed cost-benefit analysis of the above proposals on distribution and disclosure is included in Annex 1. The proposed rules are in Appendix 1.

## **Discussion about niche market segments**

- 1.6 The proposals we are consulting on in this CP are principally designed with the mainstream mortgage market in mind. However, we recognise that our proposals may impact on the equity release and Home Purchase Plan markets. In Chapter 4 we set out some preliminary thoughts about what the implications could be for these markets. We are not yet consulting on proposed changes to the regulatory regime applying to these markets, or to business loans but invite comment to help inform future proposals. Our draft rules in Appendix 1 should only be read as applying to standard regulated mortgage contracts. We will finalise our position in relation to all product types before rules concerning any of them are implemented.

## **Discussion about data requirements**

- 1.7 In the DP, we noted that changes to our regulatory approach would inevitably lead to a review of the data we collect from firms. In Chapter 5, we set out some preliminary thoughts about possible changes to the data we collect. Again, these are not firm proposals at this stage. We are simply seeking views on our current thinking to help inform future proposals.



## Scope

- 1.8 Our mortgage regime is limited to first charge lending secured on residential property. The MMR proposals have the same scope. This means nothing in this CP should be read as applying to second charge lending regulated under the Consumer Credit Act (CCA) or to unregulated buy-to-let sales or mortgage book purchases.
- 1.9 The government has previously consulted on changes to our regulatory scope to give us responsibility for some or all of these markets.<sup>4</sup> If our scope is extended in any of these areas, we will consult separately on our regulatory approach to the market(s) concerned.

## The regulatory framework

- 1.10 Since work began on the MMR the government has decided to change the UK regulatory framework for financial services.
- 1.11 Our regulatory responsibilities will rest with two new bodies: the Prudential Regulatory Authority (PRA), which will operate as a subsidiary of the Bank of England and be solely responsible for the day-to-day prudential supervision of deposit takers, insurance firms and investment banks and the Consumer Protection and Markets Authority (CPMA), which will have responsibility for the conduct of all financial services firms, both retail and wholesale.
- 1.12 These proposals were set out for consultation in July.<sup>5</sup> The government indicated that it would expect the CPMA to build on our new more interventionist and pre-emptive approach to regulation and continue with the MMR.<sup>6</sup>

## European dependency

- 1.13 In comparison with many other European markets, UK retail mortgage activities have for some time been subject to detailed regulation addressing both prudential and conduct aspects. So there is a relative abundance of regulatory data and knowledge, which the MMR analysis adds to. This means we are well placed to provide factual input into the ongoing European policy debate on mortgages. New initiatives at the European level are likely in early 2011.
- 1.14 In the meantime, we remain alive to the links between our own policy thinking and the possibility of intervention from Europe. The UK is far from alone in making regulatory change to address mortgage market detriment. For example, several countries have applied some or all of the requirements in the Consumer Credit Directive (CCD) to mortgages. France and Italy have both been looking at

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4 HM Treasury: *Mortgage regulation: a consultation*, (December 2009).  
[www.hm-treasury.gov.uk/d/consult\\_mortgage\\_regulation.pdf](http://www.hm-treasury.gov.uk/d/consult_mortgage_regulation.pdf)

5 HM Treasury: *A new approach to financial regulation: judgement, focus and stability*, (July 2010):  
[www.hm-treasury.gov.uk/d/consult\\_financial\\_regulation\\_condoc.pdf](http://www.hm-treasury.gov.uk/d/consult_financial_regulation_condoc.pdf)

6 Ibid. Para 4.24

introducing national regulation on intermediaries, while Poland has developed new disclosure requirements. European policymakers will obviously be aware of these national changes and reflect on this in framing any action they propose.

## **Next steps**

- 1.15 The consultation period on the proposals in this CP runs until 25 February 2011. During the consultation period, we will take our ideas on the road for debate and discussion with intermediaries.
- 1.16 Over the past year we have spent considerable time speaking to firms, trade associations and individuals within the industry, and have come across widespread support for our determination to address past problems. We welcome and value those discussions. Our objective is that we deliver the right outcomes for the market. We will not rush into rule changes without fully assessing their impact. Although we are pressing ahead with this consultation, the final implementation dates for the proposed changes will depend on the state of the market.

## **Who should read this CP?**

- 1.17 The proposals in this CP will be of special interest to consumers and their representatives, to firms and to trade bodies. We would also expect those with a wider interest in mortgages may want to consider the proposals.

# 2 Distribution proposals

## Background

- 2.1 In the Mortgage Market Review (MMR) Discussion Paper (DP09/3)<sup>7</sup> we explained our high-level view of the mortgage distribution landscape. The UK is notable among European markets for the highly developed nature of its distribution channels for mortgages. Consumers can use the telephone and internet to find out about deals. They can also take advantage of the services of a mortgage intermediary, whether to provide advice, do some of the searching for them or simply facilitate the purchase of the particular product they want.
- 2.2 Large numbers of consumers use mortgage intermediaries in this way. A study for the European Commission found that the UK is the only EU market in which intermediary sales typically account for more than half the total number.<sup>8</sup> Consumers clearly value the service they receive. The enduring role of the intermediary is also borne out by their continuing high share of the market in recent years, at a time when individual lenders have adjusted business models to focus on lending through their branches.
- 2.3 Intermediated lending developed in parallel with the growth in our mortgage and housing markets. In 2000, intermediaries originated 35% of total lending,<sup>9</sup> but at the peak of the market in 2007/08, 60%<sup>10</sup> of all mortgage sales were being sold through intermediaries.<sup>11</sup>

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7 DP09/3: *Mortgage Market Review*, (October 2009): [www.fsa.gov.uk/pubs/discussion/dp09\\_03.pdf](http://www.fsa.gov.uk/pubs/discussion/dp09_03.pdf)

8 European Commission (2009), *Study on Credit Intermediaries in the Internal Market*, pp 71-2, [http://ec.europa.eu/internal\\_market/finservices-retail/docs/credit/credit\\_intermediaries\\_report\\_en.pdf](http://ec.europa.eu/internal_market/finservices-retail/docs/credit/credit_intermediaries_report_en.pdf)

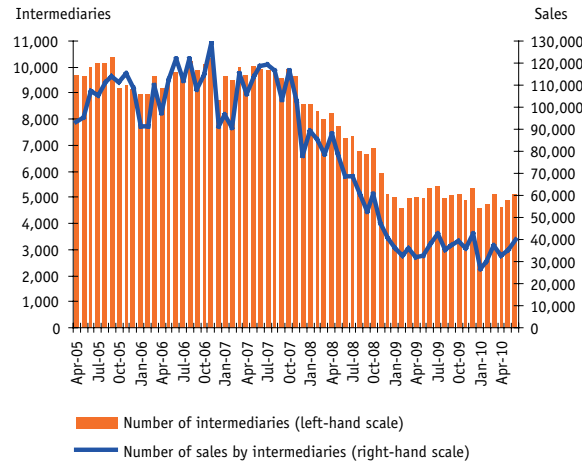
9 Mintel (2002).

10 In our DP we quoted 55%, this was based on Product Sales Data from April 2008 to March 2009.

11 FSA Product Sales Data for April 2007 to March 2008 [www.fsa.gov.uk/pubs/other/psd\\_trends\\_invest.pdf](http://www.fsa.gov.uk/pubs/other/psd_trends_invest.pdf)

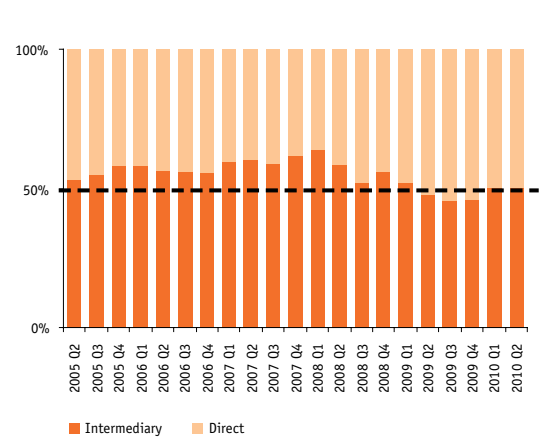
2.4 The rapid contraction in lending has resulted in the number of intermediary firms steadily declining. Unsurprisingly, the decline in intermediary firms has coincided with a decline in the number of intermediated sales (Exhibit 2.1), but their overall market share shows considerable resilience.

**Exhibit 2.1: Number of intermediary firms and regulated mortgage sales**



Source: FSA PSD<sup>12</sup>

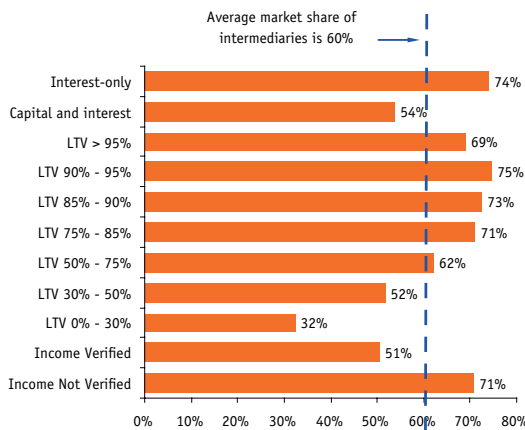
**Exhibit 2.2: Proportion of regulated mortgage sales, by channel**



Source: FSA PSD

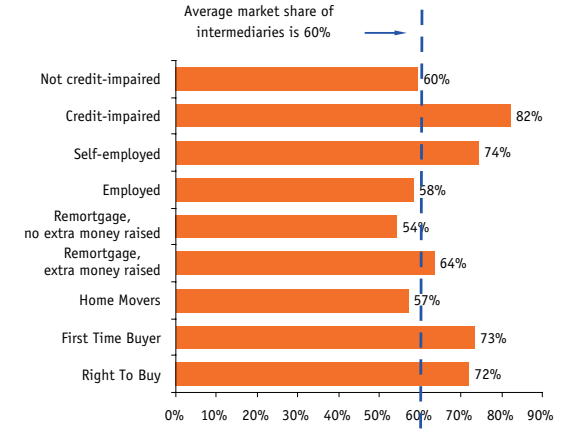
2.5 June 2009 was the first time since 2005 that more people bought their mortgages direct than through intermediaries. Since then the market seems to have stabilised, with an equal share of consumers purchasing directly as through an intermediary (Exhibit 2.2).

**Exhibit 2.3: Share of intermediaries in total sales, by product, 2007**



Source: FSA PSD

**Exhibit 2.4: Share of intermediaries in total sales, by borrower type, 2007**



Source: FSA PSD

2.6 This relatively even split in business belies considerable differences in the customer base. Many lender sales will be retention deals offered to existing borrowers. Intermediaries on the other hand will help many consumers meet more specialist borrowing needs. So, for example, a much higher population of credit-impaired sales went through intermediaries (around 80% in 2007).<sup>13</sup> More generally across

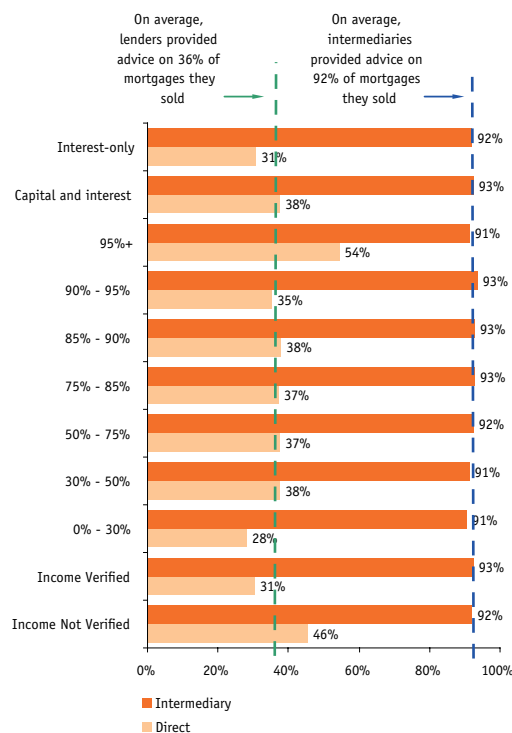
12 (1) intermediaries include directly authorised firms and appointed representatives; (2) the count of intermediaries includes firms with at least one sale in a month.

13 In 2007, 82% of credit-impaired sales were intermediated and 60% of all sales were intermediated, (FSA Product Sales Data).

all products, intermediaries facilitated a greater proportion of higher-risk business than lenders directly. This is true both for product type (Exhibit 2.3) and borrower characteristic (Exhibit 2.4). Lenders will undoubtedly continue to adjust their risk appetite, and the resulting differences in lending criteria will help maintain the role the intermediary plays in helping many consumers find an appropriate product.

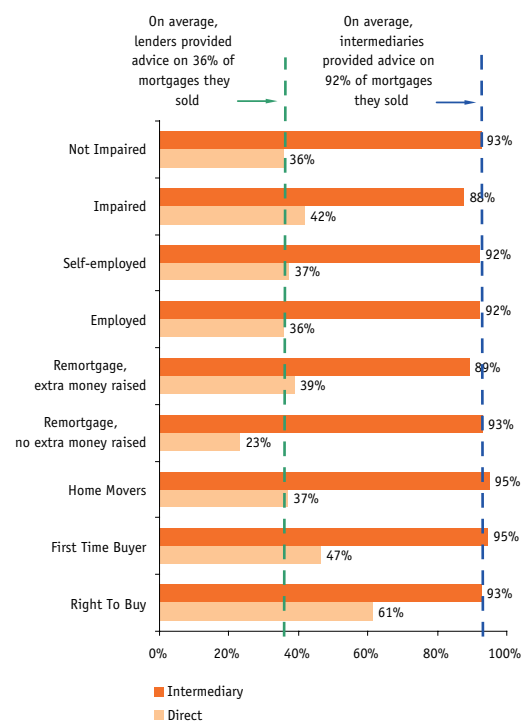
2.7 One reason a consumer may use an intermediary is that they provide advice in the vast majority of their sales, regardless of the borrower's or product's risk characteristics. On average less than half of all direct sales are advised, although this has been steadily increasing – from 34% in Q2 2006<sup>14</sup> to 47% in Q2 2010. The level of advice provided by lenders is somewhat higher for higher-risk borrowers or products with higher-risk characteristics. But even with this, there are still a considerable proportion of consumers who do not receive advice through lenders.<sup>15</sup> In these cases, there may have been no assessment of whether the mortgage sold was appropriate for the borrower and the seller would be subject to lower standards of professionalism, both of which are key MMR concerns (Exhibits 2.5 and 2.6).

**Exhibit 2.5: Proportion of mortgages sold with advice, by channel – Product type, 2007**



Source: FSA PSD

**Exhibit 2.6: Proportion of mortgages sold with advice, by channel – Borrower type, 2007**



Source: FSA PSD

2.8 Hand in hand with the increase in mortgage intermediation has been an increase in product diversity. At the height of the market, there were many thousands of different mortgage products offered,<sup>16</sup> many of which were almost exclusively available through intermediaries. The number of products has reduced significantly since the crisis, although this is now rising again (Exhibit 2.7). In relative terms the proportion of

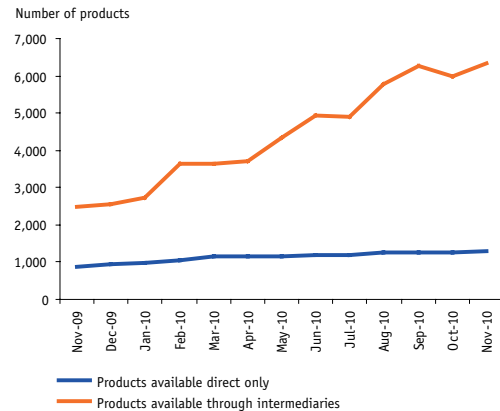
14 We started collecting data from firms in Q2 2005. However, data on the number of advised and non-advised sales was not made compulsory until Q2 2006.

15 For example, in 2007 58% of credit-impaired borrowers were not given advice by lenders.

16 According to Mortgage Brain, there were just over 35,500 mortgage products available at the peak of the market (this does not include direct-only deals, which were relatively few at the time).

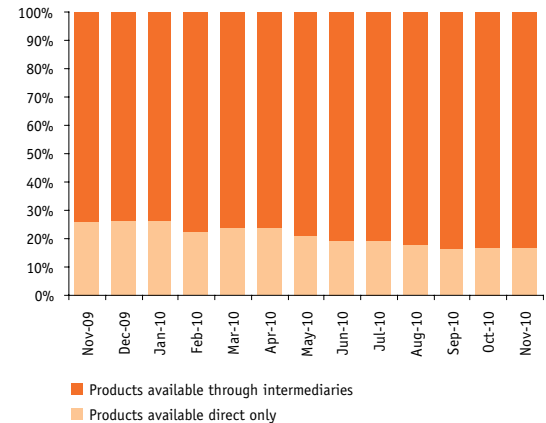
products that are only available direct from a lender has reduced quite considerably – from 26% in November 2009 to 17% in November 2010 (Exhibit 2.8). Despite this reduction, the number of products available direct means that consumers using an intermediary may, depending on that intermediary’s approach, be unaware of a number of mortgage deals that could be appropriate for them.

**Exhibit 2.7: Number of products available direct and through intermediaries**



Source: Mortgage Brain

**Exhibit 2.8: Proportion in total of products available direct and through intermediaries**



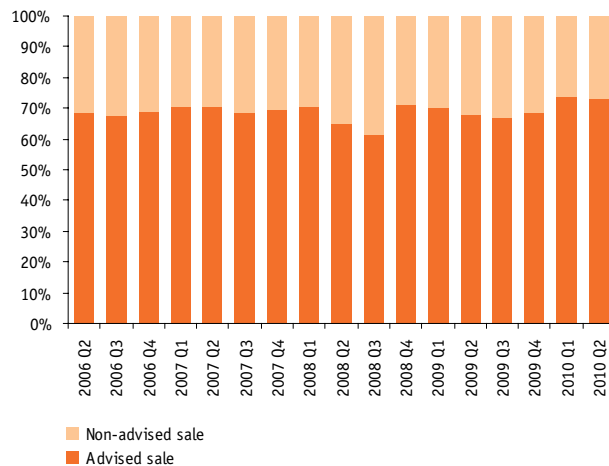
Source: Mortgage Brain

## Our detailed proposals

- 2.9 Our current regulatory regime distinguishes between two types of sales – advised and non-advised (‘information-only’) sales. An advised sale is one where the seller makes a personal recommendation on a particular product or a number of products. An information-only sale is one that simply facilitates a decision already made (because the consumer knows which product they want) or where the seller narrows down the appropriate product options available, but leaves the choice to the consumer.
- 2.10 As we noted in our DP, consumers simply do not understand or value the distinction between the two. Instead consumers:
- assume that in a regulated market no firm will identify options that are not broadly appropriate for them;
  - in any event, believe that the final purchasing decision is one for them; and
  - see intermediaries more as a means of accessing available products than as providing a standalone advice service.
- 2.11 Currently, the affordability and the ‘appropriateness’ of a mortgage is required to be assessed in advised sales but not in information-only sales, where the only high-level requirement on the seller is not to sell an obviously inappropriate product. Ensuring that a product is ‘appropriate’ for a consumer means ensuring the product meets the consumer’s needs and circumstances, for example that the consumer gets a fixed rather than variable interest rate product where they have a need for stable repayments, or a prime rather than subprime product where they have a good credit history.

2.12 Around 30% of sales in the mortgage market are information-only (Exhibit 2.9) the great majority of these being lender sales. So, in almost one third of all mortgage sales there is currently no requirement to check that the consumer's product choice is appropriate given their needs and circumstances. In addition, a large proportion of these non-advised sales are to borrowers with higher-risk characteristics. For example, in 2007, 58% of credit-impaired borrowers received no advice from branch-based sellers (lenders) (Exhibit 2.6). We believe this is not delivering adequate consumer protection.

**Exhibit: 2.9: Proportion of advised and non-advised sales in total**



Source: FSA PSD

2.13 In their responses to the DP, the vast majority of firms agreed with this view and supported our proposal to strengthen the selling standards for non-advised sales. However, there was some concern that in doing so, rather than making the distinction clearer for the consumer, we would simply blur the regulatory line between advised and non-advised sales further. Our previous research<sup>17</sup> has shown that consumers do not appreciate the distinction between an advised and an information-only sale, and tend to assume they have been given advice anyway, no matter what the sales process.

2.14 We have considered simply moving to an all-advised market (except for internet sales). But we believe it is important to allow consumers the freedom to continue to choose a product for themselves, rather than being forced down an advised route.

2.15 In our view, rather than moving to an all-advised market, the more proportionate approach is to retain the existing distinction but to apply the same basic sales standards across both advised and non-advised sales. From the consumer's perspective the important outcome is that, so far as possible, they buy a product that is affordable and appropriate for their needs and circumstances. However, firms will be able to continue to differentiate themselves by choosing whether to make a personal recommendation.

Q1: Do you agree that we should continue to allow consumers to get a mortgage without advice? If not, what other options should we consider and how would these result in better outcomes for consumers?

17 [www.fsa.gov.uk/pubs/other/mortgage\\_review.pdf](http://www.fsa.gov.uk/pubs/other/mortgage_review.pdf) and [www.fsa.gov.uk/pubs/other/MER2\\_report.pdf](http://www.fsa.gov.uk/pubs/other/MER2_report.pdf)

## Assessing affordability

- 2.16 Currently, the Mortgages and Home Finance: Conduct of Business sourcebook (MCOB) contains detailed requirements for affordability assessments where advice is given, as well as a high-level requirement for lenders in every sale to assess affordability. This has led to considerable uncertainty about the respective responsibilities of lenders and intermediaries (by 'intermediaries' throughout this chapter we mean sellers, both intermediary and branch based). Our view is that lenders should bear ultimate responsibility for assessing affordability. This responsibility cannot be passed to the intermediary.
- 2.17 If a lender is undertaking a detailed affordability assessment in every sale, this begs the question why we should require the intermediary to do the same. When we first considered this in the DP, we took the view that an intermediary could not properly assess whether a mortgage is appropriate for a consumer without first considering the borrower's ability to pay. Moreover, the intermediary will need, at point of sale, some degree of certainty about whether the lender will agree the mortgage.
- 2.18 Our view, therefore, was that intermediaries do have a role to play in assessing affordability but that it should be limited to doing no more than checking that the consumer fits within the expected parameters of lenders' affordability criteria.
- 2.19 We have considered whether requiring an intermediary to check that the borrower fits within lenders' affordability criteria needs to be covered by a specific affordability requirement, or whether it would be sufficient to include this only as part of a more general 'appropriateness' test. We have included these options in our draft rules (in Appendix 1).
- 2.20 We have concerns that imposing a specific affordability requirement on intermediaries risks muddying our very clear message that lenders should be ultimately responsible for affordability checks. Therefore, our preferred approach would be to remove the specific regulatory requirement for a firm to check whether the consumer meets the affordability aspects of the lender's eligibility criteria.
- 2.21 However, we are also concerned that there may be unintended consequences. So, if we remove the specific requirement we will still require intermediaries to consider the customer's eligibility for a particular product as part of their more general appropriateness check (discussed in the following section). We would welcome feedback on this.
- 2.22 While our regulatory requirement would be limited, we expect most lenders will continue to use intermediaries to obtain information about a consumer's income and spending, and to help gather all the supporting documentary evidence the lender needs to check affordability.

Q2: Do you agree with removing from sellers any requirement to assess affordability?

Q3: Can you see any risks from us adopting this approach?



## **Assessing appropriateness: needs and circumstances**

- 2.23 We believe it is right that the responsibility for assessing whether a product meets the needs and circumstances of a consumer lies with the seller. However, currently there is no obligation on the seller in a non-advised sale to assess whether the mortgage being sold is actually appropriate to their needs and circumstances. We believe this does not deliver adequate consumer protection.
- 2.24 In response to our DP, many firms told us they already require their sales staff to assess whether a mortgage is appropriate for a consumer even where they are not giving advice. We want to build on this existing good practice in the market, so we are proposing that the seller must always assess whether the product recommended, or the product choice presented to the consumer, meets their needs and circumstances. Sometimes in this CP we refer to this as the appropriateness test.
- 2.25 Regardless of whether the consumer receives advice or not, they will be entitled to complain to the Financial Ombudsman Service should they believe they have been mis-sold a product. In an information-only sale, the ombudsman service will consider the accuracy of the information provided and whether the product was inappropriate. In an advised sale, they will consider whether the intermediary was right to recommend the particular product they did. The merits of each complaint would be decided by the ombudsman service in the light of the particular facts and circumstances of the case. Our proposals do not change this, nor do they mean that firms will be exposed to greater liability.
- 2.26 Some respondents to the DP felt any appropriateness check should be waived in certain circumstances, such as when consumers know exactly how much they want to borrow on a particular product, or if the consumer is a sophisticated borrower and wants a 'streamlined' service. While we could allow these as 'execution-only' sales, we are concerned that this would be open to abuse by less scrupulous firms, so we do not see a case for creating an execution-only channel.
- 2.27 Our rules already allow consumers to make their own decisions and reject a personal recommendation made by a firm. If consumers wish to reject a personal recommendation and proceed on an information-only basis they will be able to do so. But where a firm is unable to identify an appropriate option, it will not be able to sell a product to the consumer.

Q4: Do you agree with our proposed approach to ensuring appropriateness is assessed in every sale? If not, in what circumstances do you believe the checks should be waived and how could we prevent this being used as a mechanism to circumvent our requirements?

## **Most suitable rule**

- 2.28 When a firm provides advice, our rules require that the firm recommends the 'most suitable' product from all those available to the firm. Given the number of products that potentially meet a consumer's needs and circumstances, this is a difficult standard

to attain and prove. The important outcome for us is that consumers get an affordable product that meets their particular needs and circumstances.

- 2.29 Therefore, to ensure the seller acts in the consumer's interests, in line with the approach taken in the retail investment market, we propose to replace the 'most suitable' rule with a requirement for a firm to act in the 'client's best interests'.<sup>18</sup> So we expect a firm to use information on the consumer's needs and circumstances to filter and present a choice of products or provide a recommendation.

Q5: Do you agree with our proposal for a 'client's best interest rule' and removing the obligation for a recommended mortgage to be the 'most suitable' product?

## Professional standards

- 2.30 Greater professionalism is central to our regulatory initiatives in the retail investment market, however, compared with the investment market, the market for mortgages is much simpler. Characteristics can be compared in advance and do not rely on the same degree of inherently uncertain judgements about the relative rates of return and risks from investing in different assets. Accordingly, our DP discussed a tailored approach to professionalism, which supported the individual registration of mortgage sellers, enhanced Continuing Professional Development (CPD) and adherence to a Code of Ethics. We received little comment on this proposed approach.
- 2.31 There are currently fewer Training and Competence (TC) obligations on non-advised firms than on those offering advice. All firms must employ personnel with the skills, knowledge and expertise necessary to discharge the responsibilities allocated to them<sup>19</sup>, but firms that provide advice are also subject to TC which includes a minimum qualification standard.
- 2.32 We are proposing to require all individuals who sell mortgages to meet the same qualification standards, as they must all consider the consumer's needs and circumstances. Under the TC requirements, individuals will have thirty months to pass all modules of a relevant qualification.<sup>20</sup> So for new sellers, this will be thirty months from when they first carry out the activity specified in TC; existing sellers will also have thirty months from implementation of our rules. We also propose to extend the standards to individuals who design structured questions e.g. for use in internet sales. Consistent with the approach taken in the RDR, we also propose to allow firms to use other assessment methodologies<sup>21</sup> to achieve the equivalent of a Qualification and Credit Framework (QCF) Level 3 standard.<sup>22</sup> As the mortgage

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18 COBS 2.1.1 (1) states that a firm must act honestly, fairly and professionally in accordance with the best interests of its client (the client's best interests rule). The duty extends across the transaction, rather than just applying only to the sales standards. This was a direct implementation from MiFID.

19 SYSC 3.1.6R and SYSC 5.1.1R – 'The competent employees rules'

20 CP10/12: *Competence and ethics*, (June 2010): [www.fsa.gov.uk/pubs/cp/cp10\\_12.pdf](http://www.fsa.gov.uk/pubs/cp/cp10_12.pdf)

21 These could include course work, provided they are independently accredited as being of an equivalent standard to the more traditional written exams.

22 CP09/31: *Delivering the Retail Distribution Review*, (December 2009): [www.fsa.gov.uk/pubs/cp/cp09\\_31.pdf](http://www.fsa.gov.uk/pubs/cp/cp09_31.pdf) (paragraphs 2.79 to 2.85)

qualification standards have not been reviewed since 2004, we are proposing (in line with the RDR) to review these and keep them under review on an ongoing basis, to ensure they remain fit for purpose.

- 2.33 In line with our approach to the Approved Persons regime (set out in PS10/9<sup>23</sup>), our qualification requirements will only apply to those individuals who sell mortgages. This will include all consumer-facing sellers i.e. individuals working for lenders or intermediary firms (sellers). It will not include those engaged in processing, underwriting or administration activities, for example we would not expect those individuals involved in arrears handling, solely dealing with forbearance measures, to be caught by our proposals.
- 2.34 Beyond this, we do not see a strong case to be more prescriptive about professionalism. As we have already noted, in contrast to the retail investment market, the mortgage market is much simpler. It is unlikely that a mortgage firm will be required to sell a product which is unfamiliar to them. We will, of course, continue to promote enhanced CPD as best practice, however we do not now think it would be proportionate to apply the enhanced approach to CPD proposed under the RDR.<sup>24</sup>
- 2.35 Given the extension of the Approved Persons regime to those selling mortgages, these individuals will be subject to the Statements of Principle and Code of Practice for Approved Persons (APER). Feedback received to CP09/18<sup>25</sup> led us to conclude that a Code of Ethics should apply to all Approved Persons and not just those within the scope of the RDR. Therefore, mortgage intermediaries and those designing structured questions will also be subject to the proposed new high-level Code of Ethics. Over and above this, we do not see any need to apply any additional requirements in relation to ethics.

Q6: Do you agree with our approach to applying common professional standards across the mortgage market?

## Enhancing our sales standards

- 2.36 We have identified three issues with the current sales standards in MCOB that we wish to address:
- **Borrowing into retirement.** Through our thematic work<sup>26</sup> we found that firms were not adequately considering changes to the consumer's needs and circumstances as they reached retirement. A seller should be aware, through fact-finding, if the mortgage will run beyond the client's nominated retirement age, and where it does, we would expect the firm to assess whether this is/or remains appropriate.

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23 PS10/9: *Mortgage Market Review: Arrears and Approved Persons – Including feedback to CP10/2*, (June 2010): [www.fsa.gov.uk/pubs/policy/ps10\\_09.pdf](http://www.fsa.gov.uk/pubs/policy/ps10_09.pdf)

24 CP10/14 proposes that full-time advisers will need to complete a minimum of 35 hours of relevant CPD each year, with at least 21 hours of this being structured learning.

25 CP09/18: *Distribution of retail investments: Delivering the RDR*, (June 2009): [www.fsa.gov.uk/pubs/cp/cp09\\_18.pdf](http://www.fsa.gov.uk/pubs/cp/cp09_18.pdf)

26 FSA – Mortgage quality of advice processes - [www.fsa.gov.uk/pages/Library/Communication/PR/2007/001.shtml](http://www.fsa.gov.uk/pages/Library/Communication/PR/2007/001.shtml)

- **Taking a further advance.** Borrowers may be able to take a further advance with their existing lender, thereby potentially avoiding unnecessary fees and charges usually associated with remortgaging. Therefore, as part of the appropriateness test, we would expect firms to explore whether consumers are able to take a further advance with their existing lender, alongside any other option.
- **Rolling-up the mortgage fees into the loan.** Where consumers do not have the money to hand, it may be cheaper to roll-up mortgage fees and charges into the loan rather than borrow unsecured funds from elsewhere. However, we will expect firms to establish whether rolling-up mortgage fees and charges into the loan is appropriate for the particular consumer, taking into account their needs, circumstances and the financial implications of rolling-up fees (for example the extra interest which could accrue over the term of the mortgage). We explain our proposals in more detail in the following section.

2.37 We are proposing that firms must consider these three additional elements as part of their assessment of a borrower's needs and circumstances.

Q7: Do you agree with our proposals to include these three elements as part of the new appropriateness test?

## **Rolling-up fees and charges into the loan**

2.38 Our DP considered prohibiting the rolling-up of intermediary and mortgage product charges altogether. We expressed concern that where borrowers do not have to pay fees or charges upfront, they are unlikely to focus on the levels of such fees and this reduces consumer price sensitivity. Indeed, this lack of consumer price sensitivity may have contributed to the increase in mortgage arrangement fees since 2002. The DP noted that in 2002, a typical arrangement fee was around £199 to £295. By 2009, arrangement fees ranged from £299 to £1,995.

2.39 There are two main options available to address the issue of rolling-up fees and charges into loans:

- a) banning of the roll-up of fees and charges into loans (which we discussed in the DP); and
- b) improving consumer awareness in this area for example through disclosure.

## **Banning the roll-up of fees and charges**

2.40 Respondents to the DP overwhelmingly agreed that it would not be appropriate to ban the roll-up of fees and charges into mortgages. Although a ban would raise consumer awareness of the level of upfront fees consumers are being charged, the feedback highlighted a number of potentially negative consequences. It would be easy for firms to circumvent our rules – consumers would simply obtain a larger mortgage and pay the fees and charges out of the additional borrowing. Alternatively consumers could simply borrow funds to cover their fees and charges using unsecured credit which could be considerably more expensive. In August 2010, the average quoted

two-year fixed interest rate for a mortgage product with a 75% LTV was 3.79%.<sup>27</sup> The average quoted rates for unsecured borrowings for August 2010 were 13.11% for personal loans of £5,000, 16.70% for credit card debts and 19.08% for overdrafts.<sup>28</sup>

- 2.41 There was also concern that banning the roll-up of fees and charges would remove the choice from those consumers who can afford the higher payments associated with rolled-up fees and who are making an informed decision to do this. For example, first-time buyers who can afford the higher payments may decide to roll-up application fees as they will already have to pay a number of significant upfront costs, such as stamp duty, deposits and legal fees.
- 2.42 Another view was that the new affordability assessments in CP10/16<sup>29</sup> will protect consumers by ensuring that even after adding fees and charges to the loan, the mortgage remains affordable. We have carefully considered the feedback and agree that an outright ban on the roll-up of fees and charges would not be in consumers' interests.

### **Improving consumer awareness through disclosure**

- 2.43 The roll-up of fees is a widespread practice amongst lenders, but there is significant variation between lenders on the number of their consumers whose fees are rolled into the loan. Estimates provided by five smaller lenders ranged from less than 10% to 98%, with an average across all five of 59%. This would suggest very different approaches to rolling-up fees into mortgage advances – for some this appears to be the default position.
- 2.44 Respondents to the DP were split on whether the existing disclosure requirements for the roll-up of fees and charges were adequate. There is an existing requirement on firms to provide relevant details in the Key Facts Illustration (KFI).<sup>30</sup> The illustration must state that mortgage payments would increase and must include details of what the mortgage advance would increase to if the fees and charges were rolled-up. The rules also provide that a consumer who wishes to roll-up fees into the mortgage can request another illustration that shows the effect of this on the payments.<sup>31</sup> This is followed at the offer stage by a further illustration<sup>32</sup> which must reflect any changes to the charges since the mortgage was applied for. Consumers who are rolling-up their fees into their mortgage should therefore be well aware of what their increased monthly repayments would be as a result.
- 2.45 As Chapter 3 describes, we know that few consumers use the KFI to compare products. Notwithstanding this, we think there could be value in letting the consumer make an immediate and direct comparison of the impact of rolling-up fees into the mortgage by requiring that they are presented with two KFIs (one illustrating the overall cost of the mortgage to the consumer with fees rolled-up

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27 The data is available in the statistical reports on the Bank of England website ([www.bankofengland.co.uk](http://www.bankofengland.co.uk)) under the data series IUMBV34.

28 The data is available in the statistical reports on the Bank of England website ([www.bankofengland.co.uk](http://www.bankofengland.co.uk)) under the data series IUMCCTL, IUMBX67 and IUMODTL.

29 CP10/16: *Mortgage Market Review: Responsible Lending*, (July 2010): [www.fsa.gov.uk/pubs/cp/cp10\\_16.pdf](http://www.fsa.gov.uk/pubs/cp/cp10_16.pdf)

30 <http://fsahandbook.info/FSA/html/handbook/MCOB/5/6>

31 MCOB 5.6.70 R (3)

32 <http://fsahandbook.info/FSA/html/handbook/MCOB/6>

into the loan and the other illustrating the overall cost of the mortgage to the consumer where the fees are not included but will be paid separately). We propose to make this a requirement where the rolling-up of fees is being considered.

Q8: Do you agree with our proposal to improve the disclosure of the impact of the roll-up of fees through the provision of a second KFI?

### **Automatic roll-up of fees**

2.46 Several respondents to the DP reported that certain lenders automatically roll-up fees and charges into mortgage loans without the consumer's consent. We propose to look into this practice further as part of the MMR charges work. Our view is that mortgage fees should never be automatically rolled-up into the mortgage without the explicit consent of the consumer. Automatic roll-up without any regard to the consumer's needs and circumstances is not treating consumers fairly.

2.47 We propose to amend the rules to require that firms obtain the consumer's informed consent about rolling-up fees into the mortgage. We will expect firms to offer the consumer a choice between the two options based on the two KFIs they have seen. The choice can be voiced orally, in writing or over the internet, but firms must keep a record which shows what the consumer has elected to do and to confirm they have met our requirements.

Q9: Do you agree with our proposal to require firms to present consumers with a choice of rolling-up the fees and charges, and to record the decision made?

2.48 We are keen to improve consumer awareness of the impact of the roll-up of fees. Measures we are considering include a downloadable consumer guide explaining what rolling-up is, which would be hosted on our website and placed on third-party sites. Another option could be printable guides that consumer bodies could give out to their stakeholders.

2.49 In addition, the Consumer Financial Education Body (CFEB) plans to update its information about mortgage fees and costs on the [Moneymadeclear<sup>TM</sup> website<sup>33</sup>](http://www.moneymadeclear.org.uk/), providing an illustrative example and encouraging consumers who are considering rolling-up fees to use the mortgage calculator<sup>34</sup> to compare the cost with and without fees included. This will help consumers to make an informed decision by showing the impact of rolling-up fees on their monthly payments and the overall cost of the loan.

Q10: Do you agree or have any other suggestions about how to improve consumer awareness of the impact of rolling-up fees and charges?

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33 [www.moneymadeclear.org.uk/](http://www.moneymadeclear.org.uk/)

34 [www.moneymadeclear.org.uk/tools/mortgage\\_calculator.html](http://www.moneymadeclear.org.uk/tools/mortgage_calculator.html)

## Record keeping requirements

- 2.50 Our detailed record keeping requirements in MCOB only apply to advised sales. We propose to extend them across all sales.<sup>35</sup>
- 2.51 We will expect the firm to retain a record of the consumer information it obtained to assess appropriateness and where applicable, the reasons why a personal recommendation was made. Where firms present a number of appropriate products to the consumer, leaving them to make their own choice, we will require them to retain a record of the products presented. Where fees are rolled-up into the loan (as outlined in paragraph 2.45) we would expect the firm to retain two KFIs, one with the fees added and one without. We also expect the firm to retain a record of a positive election made by the consumer to roll-up fees into the loan.

## Better engaged consumers

- 2.52 The mis-buying we have seen in the mortgage market provides clear evidence that some consumers are failing to engage properly with their purchasing decision. We have considered a number of ways to address this. For example, we considered requiring firms not to proceed with the sales process unless the consumer had completed a budget planner. Our aim was to encourage consumers to take time to work through their income and expenditure and think carefully about what they could actually afford away from a pressurised sales environment. But we recognise the practical difficulties in this approach. Different types of mortgage borrowers will have different degrees of useful financial information available. It should be straightforward for a remortgagor to provide a reasonably detailed budget plan. However, it might be unrealistic to expect a first-time-buyer – likely to be less well aware of the costs involved in running a home – to provide comprehensive information. In addition, stakeholders indicated that this approach could be easily gamed. So we would have little comfort that all consumers would engage in the way we intended.
- 2.53 We also considered requiring firms to provide the consumer with a ‘representative summary’ of all the products the seller presented as being appropriate, which the consumer could take time to consider. We thought this might empower consumers to question the products presented and, where applicable, why one product had been recommended over all other appropriate options.
- 2.54 Feedback from stakeholders suggested it would be difficult for firms to provide a comprehensive list to the consumer. For intermediaries, sourcing system print-outs were only ever viewed as an indicator of the products available. In many cases, specific characteristics (such as property type, credit profile or purpose of borrowing) could not be factored into the systems, but may have an impact on the products available. It would also be difficult for us to prescribe the best comparison points for each consumer.

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35 Our existing record keeping requirements (which require firms to retain a record of information in relation to the consumer’s needs and circumstances) only apply where a personal recommendation is made.

- 2.55 Given all the practical difficulties, we instead intend to work with CFEB and their financial capability programme which is aimed towards creating better informed, educated and more confident consumers. In support of their '*stay on top of your mortgage*' campaign, CFEB actively encouraged consumers to carry out regular health-checks on their finances using a range of online information and tools, including an updated budget planner and mortgage calculator.
- 2.56 CFEB continues to explore ways to reach people early in the borrowing process and ways to drive prospective borrowers to its impartial information and advice. CFEB is developing a national financial advice service and a financial health-check, building on the Money Guidance Pathfinder. This service provides guidance online, by telephone or face-to-face and is targeted at those 'vulnerable to the consequence of poor decision making'. Budgeting, credit and mortgages were amongst the subjects consumers sought information and guidance on.<sup>36</sup> Taken together, we think these work-streams will support consumers to make better informed financial decisions in the future.
- 2.57 We would welcome the views of stakeholders on other ways in which we could promote consumer engagement.

Q11: Do you have any views on other ways in which we could promote consumer engagement?

## **Equality and diversity issues**

- 2.58 We have identified the possibility that our proposals for distribution could have an adverse effect on some groups with protected characteristics (e.g. race, religion, age, disability) when they wish to take out a mortgage. We are carrying out analysis on whether this is the case, and would welcome input from respondents.

Q12: Do you think that these distribution proposals will impact any groups with protected characteristics (e.g. race, religion, age, disability)?

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36 Money Guidance Pathfinder: A report to the FSA: [www.cfebuk.org.uk/pdfs/20100709\\_pathfinder.pdf](http://www.cfebuk.org.uk/pdfs/20100709_pathfinder.pdf)



# 3 Disclosure proposals

## Background

- 3.1 When we designed the Mortgages and Home Finance: Conduct of Business sourcebook (MCOB) regime, we strongly emphasised the role that disclosure could play in bringing about positive outcomes for consumers. Consistent with the prevailing wisdom of the time, we considered that well-informed consumers would make rational choices and avoid getting inappropriate or unaffordable mortgages. Disclosure of key pieces of information about the service a consumer should expect (through the Initial Disclosure Document – IDD) and about the mortgage being offered (through the Key Facts Illustration – KFI) was therefore the cornerstone of the mortgage regime.
- 3.2 However, our consumer research suggests that these disclosure documents are not being used in the way we intended.<sup>37</sup> The IDD has not been a strong factor in consumers' choice of mortgage firm, with consumers instead relying on personal recommendations or past experience. Consumers have low recall of the document and rely more on what they have been told. The KFI, on the other hand, has been recognised as valuable by consumers, but more as a record of their purchase than as a tool to inform their decision on a product. The KFI has only been used to compare products by a small proportion of consumers, typically those who had researched the mortgage market themselves, e.g. on the internet.
- 3.3 We outlined in the Mortgage Market Review (MMR) Discussion Paper (DP09/3)<sup>38</sup> that we are no longer seeking to place such a strong reliance on disclosure to achieve our regulatory aims in the mortgage market. We are strengthening our approach through our responsible lending proposals and enhanced sales standards, to ensure that as far as possible consumers do not end up with inappropriate or unaffordable products.
- 3.4 However, disclosure has its part to play in this and other markets. We believe it is right that consumers continue to receive appropriate information about the products and services they are choosing, and that we encourage them to shop around.

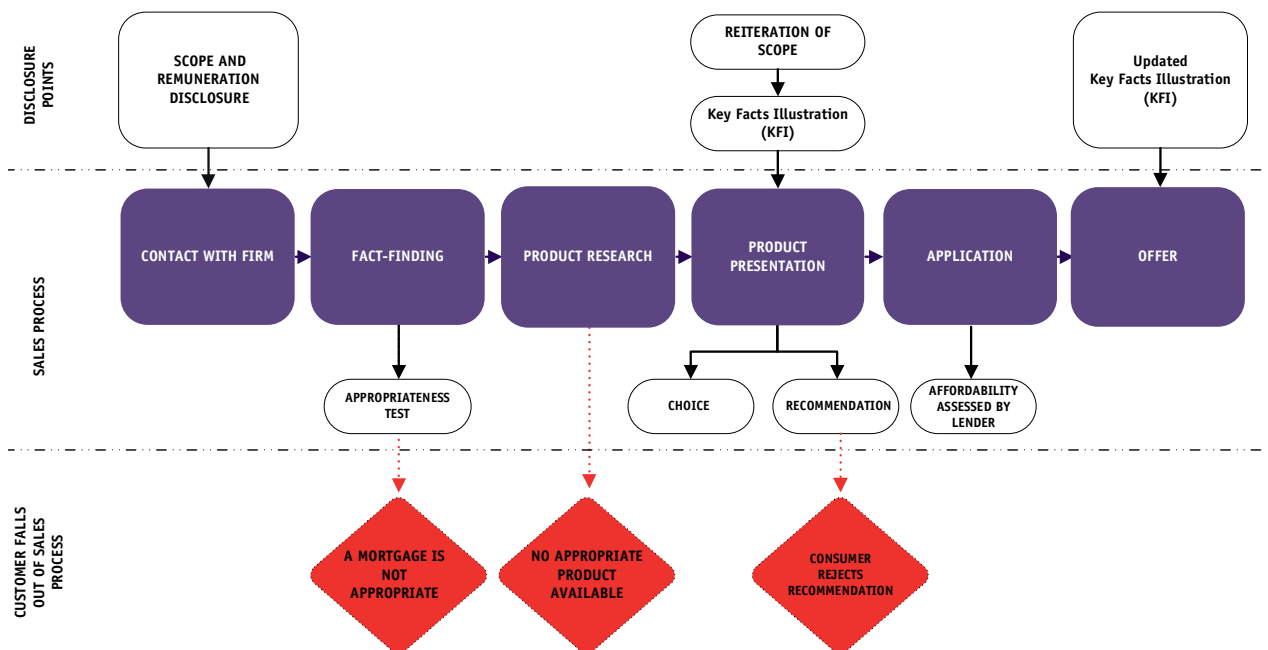
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37 [www.fsa.gov.uk/pubs/consumer-research/crpr81.pdf](http://www.fsa.gov.uk/pubs/consumer-research/crpr81.pdf)

38 DP09/3: *Mortgage Market Review*, (October 2009): [www.fsa.gov.uk/pubs/discussion/dp09\\_03.pdf](http://www.fsa.gov.uk/pubs/discussion/dp09_03.pdf)

- 3.5 Alongside this, as we noted in the previous chapter, the Consumer Financial Education Body (CFEB) retains an important role in providing information, education and advice to consumers about what to expect in their interaction with the mortgage market, and what key pieces of information they should look out for when considering products and services, to facilitate shopping around and better informed decisions.
- 3.6 We have outlined below our detailed proposals for changing the disclosure regime. Exhibit 3.1 illustrates how the new disclosure proposals fit within the proposed mortgage sales process discussed in Chapter 2.

**Exhibit 3.1: The new mortgage sales process**



## Our detailed proposals

### Service disclosure

- 3.7 In the DP, we discussed removing the compulsory requirement for firms to provide consumers with an IDD (the prescribed document that contains detailed information about a firm’s service), and replacing it with requirements for firms to disclose key messages to consumers. This would bring the service disclosure requirements for mortgages more in line with those in the investment and insurance markets. Consumer groups were supportive of us making this change, though the response from firms was mixed, with many noting that their opinion would depend on what the key messages are.
- 3.8 The outcome we want to achieve is that consumers understand the service they can expect from a firm. In particular, we believe that it is important for consumers to have a proper understanding at the outset of the key pieces of information that matter – whether the firm’s scope means that the range of products being offered is restricted and the basis on which the firm will be remunerated.

- 3.9 The scope of a firm's service (i.e. the range of mortgage providers and products that it includes when sourcing mortgage products for the consumer) is important because it helps consumers know how comprehensive a search of the market the firm will be undertaking. Where a firm's range is limited, the consumer might consider the option of checking whether a better deal exists elsewhere.
- 3.10 Information about the basis of the firm's remuneration is important for a number of reasons. We consider that a consumer should know, before the firm starts doing anything for them, how much they will have to pay the firm, what this payment is for, at what stage they must pay and whether the fee is refundable under any circumstances. They should also know whether the firm will receive any commission for the sale, which will alert them to the risk of firm or product bias.
- 3.11 In our view, this information is most beneficial to consumers early on in the process, before they or firms have invested too much time or effort in the transaction. We therefore propose that this information is given in the initial contact between firm and consumer.
- 3.12 The proposed delivery of our initial service disclosure requirements has two elements. The first is a requirement that the information on scope and remuneration be provided in a durable medium. This will protect consumers in case there is a future complaint or dispute. It is also intrinsically in a firm's interest to ensure these matters are documented. So we propose that the information is given in a durable medium in the initial contact where practicable, or five working days following the initial contact where it is not, for example, in the case of telephone sales.
- 3.13 The IDD can meet the requirement to provide the information in a durable medium if firms wish. It may minimise costs for firms, and it would also allow them to provide other relevant services to consumers (e.g. retail investment advice, insurance advice) and give a combined IDD if this suits their operations. Our Handbook will continue to contain these templates as guidance to firms.<sup>39</sup> However, using these would not be compulsory, and firms may choose to give the information in another durable format.
- 3.14 While having this information in a durable medium is useful, we do not consider it enough on its own to ensure consumers really understand, and base their decision to proceed on, a firm's scope of service and remuneration. Therefore, the second element of the delivery of the initial service disclosure is a requirement on firms to clearly and prominently emphasise these messages to the consumer.
- 3.15 The Retail Distribution Review (RDR)<sup>40</sup> has introduced an oral disclosure requirement for the investment market where firms offer a restricted service. Building on this approach, we propose using oral disclosure to make the key messages in the mortgage market clear and prominent. So where firms have spoken interaction with consumers, we propose to require that they tell them about their scope of service and the basis of their remuneration orally.

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39 MCOB will continue to contain the IDD for mortgages and COBS will continue to contain the combined IDD.

40 CP09/18: *Distribution of retail investments: Delivering the RDR*, (June 2009): [www.fsa.gov.uk/pubs/cp/cp09\\_18.pdf](http://www.fsa.gov.uk/pubs/cp/cp09_18.pdf)

- 3.16 Recognising the potential for the growth of sales channels that do not require spoken interaction, e.g. internet sales, we also propose that, where there is no spoken interaction, there will be other requirements that firms display these messages clearly and prominently at the start of the sales process. For firms communicating over the internet, pages that provide an IDD through a link will not be enough to meet our requirements. They will have to display the messages on a webpage that all consumers must access, and cannot avoid, as part of going through the initial stage of the on-line sales process. Firms communicating by post will have to set out these messages clearly and prominently in a communication separate from the IDD.

Q13: Do you agree that it is appropriate to focus our service disclosure on these key messages? Do you agree that this is the correct approach for communicating these messages to consumers?

### *Scope of service labels*

- 3.17 We are also proposing changes to the current scope of service labels to make them clearer and to align them more closely with the new labels for the retail investment market.
- 3.18 In the DP we discussed the idea of using the ‘independent’ and ‘restricted’ labels that were outlined in the RDR. Most respondents supported this simplification, although some raised concerns about applying labels designed with one market in mind to another.
- 3.19 Given the support for this approach, we propose to apply the ‘independent’ and ‘restricted’ labels to all firms in the mortgage market. Consistent with the approach in the retail investment market, firms who label themselves as ‘independent’ will have to source products from a ‘comprehensive and fair analysis of the relevant market’. In the mortgage market we consider that the ‘relevant market’ should relate to the relevant home finance transaction (i.e. the regulated mortgage contract market, the equity release market, the sale and rent back market, etc.).
- 3.20 We are conscious that in the mortgage market, there are a number of products that cannot be accessed by all firms, e.g. products that are only available to a consumer directly from a lender (which we discuss further below), or products only available through special deals between particular lenders and intermediaries. We propose to specify that a firm’s search does not need to extend to these products in order to use the label ‘independent’. In practice, as currently, a firm may use a panel of lenders in meeting the requirement for a comprehensive and fair analysis of the market, but the panel would need to be sufficiently large to ensure it is representative of the range of products available.
- 3.21 To be ‘independent’ firms will also be required to offer an unbiased and unrestricted service. This means they should not be bound by any form of agreement with a lender that restricts the service they can provide.
- 3.22 Where a firm does not meet these requirements, it must describe its service as ‘restricted’. In doing so, it will need to clarify whether it offers products from just one firm or a limited number of firms, and note any restrictions on the range available.

- 3.23 In the DP we also raised the option of changing the description of ‘non-advised’ sales to ‘information-only’ on the grounds that it might help consumers better understand what the firm is offering. However, as noted in Chapter 2, we have found that consumers do not understand or value the distinction between advised and non-advised sales. Moreover the sales standards will be the same regardless of whether consumers receive advice or not. So we no longer see a strong case for applying the additional label of ‘information-only’ in the mortgage market.

#### Deals available only to consumers directly through a lender

- 3.24 A significant proportion of products in the mortgage market are deals that are only available to the consumer directly from a lender (see Exhibit 2.8). We already expect firms that cover the whole market to inform consumers when they consider there might be a better deal on the market that they themselves cannot offer. We consider that, within the new labelling landscape, this needs to go further and an independent firm should be required to tell a consumer explicitly whether it will consider direct-only deals.
- 3.25 If consumers do not know this, they may presume an independent firm is including these deals in their product search when they are not. This could create problems for firms down the line should it become clear that other deals were available direct from lenders and the consumer was not made aware of these.

#### Fee option

- 3.26 The concept of ‘independence’ already exists within MCOB. As part of this a firm cannot hold itself out as independent unless it enables the consumer to pay a fee for its services (rather than rely upon commission). We considered whether we should retain this requirement as part of our new labelling landscape.
- 3.27 As discussed in the DP, we have not seen significant evidence of commission-bias in the mortgage market. Even if there were risks of commission bias, our enhanced sales standards will ensure that a firm only puts forward products on the basis of a consumer’s needs and circumstances. Our re-focused disclosure requirements will also require firms to highlight their remuneration (including whether they get commission). Therefore we do not believe that there is a strong case for retaining the requirement for a fee option in our new ‘independent’ label.

- Q14: (i) Do you agree with our application of the ‘independent’ and ‘restricted’ labels to the mortgage market?
- (ii) Do you agree that we should require ‘independent’ firms to disclose whether they consider direct-only deals?
- (iii) Do you agree that we do not need to retain a fee option as part of our requirements for the label of ‘independent’?

### *Reiteration of scope*

- 3.28 While information on a firm's scope of service is important early on in the process, it is equally important that the consumer bears the scope of a firm's service in mind when they consider the product(s) the firm is presenting to them. Where a firm's scope is restricted, it is important that consumers make their decision about the product in the knowledge that there might be other products on the market that are also appropriate for their needs and circumstances.
- 3.29 We therefore propose to require that, when a firm, after assessing a consumer's needs and circumstances, provides consumers with information about a product that is specific to the amount they wish to borrow, they tell the consumer again whether the product range that they can offer is restricted or not. We are not specifying how this information is disclosed (e.g. orally or written) but it must be clear, prominent and directly linked to the presentation of the product(s).

Q15: Do you agree that firms should reiterate their scope at the point that they put the product(s) forward?

### *Distance Marketing Directive*

- 3.30 The EU Distance Marketing Directive<sup>41</sup> outlines the information that must be supplied to consumers by firms that sell financial services at a distance. MCOB currently gives effect to the relevant disclosure requirements for the mortgage market. However, as we are now proposing to make changes to our service disclosure requirements and reduce the amount of information that all firms have to provide to consumers ahead of the sale, we are amending our rules relating to the Distance Marketing Directive to ensure that firms selling mortgages at a distance still meet all the EU requirements (such as disclosing the name and main business of the firm, and how to make a complaint, in good time before the contract for mediation services has been agreed).

### **Product disclosure**

- 3.31 We received strong support from consumers and firms for retaining the KFI in its current form. Respondents to our DP supported the findings of our research that consumers value it as a record of their purchase. As there is also the possibility of European action on product disclosure, the costs<sup>42</sup> of us making any changes to the format of the document would not seem proportionate. Therefore, we are not proposing any changes to the content of the KFI.
- 3.32 The DP raised the question of whether we should require elements of disclosure to be provided orally. We considered whether oral disclosure requirements relating to key comparison points in the KFI might help consumers to compare different products. However, our research tells us that many consumers have already chosen a product by the time they receive the KFI. It would also be difficult to pick out the key

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41 The Distance Marketing of Consumer Financial Services Directive (DMD) (Directive 2002/65/EC).

42 Oxera estimated that the one-off costs to the industry of changing the format of the KFI as £23m. [www.fsa.gov.uk/pages/Library/Policy/CP/2010/10\\_28.shtml](http://www.fsa.gov.uk/pages/Library/Policy/CP/2010/10_28.shtml)

comparisons between products that will be useful to most consumers, given they all have different needs and circumstances. On this basis, we do not currently see a strong case for adding oral disclosure requirements relating to product features.

- 3.33 While we are not proposing changes to the format of the KFI, we do see value in changing the trigger points for presentation of the KFI to ensure maximum impact and avoid information overload. This would also reduce compliance burdens on firms.
- 3.34 Though most consumers have not used the KFI in the past to make a decision between products, it is still important that they receive a KFI before making an application, so they can understand exactly what they are applying for. But receiving it at the right point before making the application is important.
- 3.35 Our current rules require a pre-application KFI to be given in three circumstances, where:
- a firm makes a recommendation to a consumer to take out a product;
  - a firm provides written information about a product to the consumer that is specific to the amount they want to borrow; or
  - a consumer requests information from a firm about a product that is specific to the amount they wish to borrow.
- 3.36 We consider that the first trigger point above remains appropriate. A consumer should get a KFI where a firm has considered the available products and is recommending one that the consumer should apply for.
- 3.37 However, as our research indicates most consumers have not used the KFI to compare products in the past, we do not see a lot of value in the second trigger point. Essentially, it means that a consumer has to receive a KFI for each product they may be interested in. Removing this requirement, and instead requiring the firm to provide a KFI only once the consumer has indicated a preference for a particular product, should help to minimise the amount of information overload.
- 3.38 We recognise that some firms will want to provide consumers with written information about products to help them make a choice. Our current rules say that firms can only give consumer's information about a product that is specific to the amount the consumer wants to borrow in limited circumstances, (i.e. when giving a KFI, when providing supplementary information to accompany a KFI, when providing information on a screen, or when providing the information orally).
- 3.39 We propose to remove this rule and thereby expand the circumstances in which a firm can give information to a consumer. We will instead remind firms of their obligations to present any information in a clear, fair and not-misleading manner. We will also highlight the link to the client's best interest rule that is set out in Chapter 2. To be consistent with this rule, firms will have to ensure that they are guided by their customer's interests, and not by commission for example, when choosing to present a select number of available products to a consumer.

- 3.40 Our research<sup>43</sup> established that a small proportion of consumers do use KFIs to make comparisons between products. This is something we want to encourage. Therefore, we propose to alter the third trigger point above to ensure that a firm must provide consumers with a KFI if they ask for one. We propose to add a specific requirement that firms inform consumers that they can ask for KFIs to ensure consumers are aware of this.
- 3.41 There are a significant number of ‘direct-only deals’ (Exhibit 2.7) in the mortgage market. We want to encourage firms to consider whether any of these deals might be the best offering for their consumers, even if they cannot provide the product themselves. The current rules get in the way of this, because firms must provide a KFI when proposing a product and are liable for its accuracy. So we propose that where a firm (other than the actual lender) puts forward or recommends a direct-only deal, they will not be required to provide a KFI. Instead, the firm will be required to keep a record where they recommend a direct-only deal and provide the consumer with a copy of that record in a durable medium. The record can take the form of a KFI, but it does not need to. As there will no longer be a regulatory requirement on the firm to produce a KFI, it will not have responsibility for the KFI’s accuracy. The record need only contain the fact that the firm has recommended that the consumer take out the specific product concerned. The consumer should get a complete and accurate KFI about the product from the lender.
- 3.42 Our existing rules say that a firm cannot accept fees from, or commence a mortgage application for a consumer, until that consumer has had the chance to consider a KFI. This is intended to ensure that a consumer is not committed to a mortgage in any way before they have considered the facts about it. However, in light of the changes outlined above concerning direct-only deals, we will clarify this rule to make it clear that a firm can receive a fee for its service where it does not take the consumer’s application forward itself.

- Q16: (i) Do you agree that we make these changes to the trigger points for the pre-application KFI?
- (ii) Do you agree that we should have a requirement to make firms tell consumers that they can request a KFI for any product they offer?
- (iii) Do you agree that we should require firms to provide the consumer with a record, rather than a KFI, where they recommend a direct-only deal?

- 3.43 We believe that it remains right that a firm provides a consumer with an up-to-date KFI as part of the offer document, both as a final check that the mortgage they are taking out is as they understood it, and as a record that the consumer can retain. We are therefore not proposing to make any changes to providing a KFI at the offer stage. Similarly, we do not propose to change the requirements for a KFI after completing the initial deal, for example, where the mortgage terms vary as a result of a further advance. This ensures that consumers have an up-to-date record of their arrangement and enables them to see the impact of the change. Our other existing

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43 [www.fsa.gov.uk/pubs/consumer-research/crpr81.pdf](http://www.fsa.gov.uk/pubs/consumer-research/crpr81.pdf)



requirements for events following a mortgage sale<sup>44</sup> will also remain, such as the requirement for firms to give a prominent reminder to consumers on the impacts of switching to an interest-only mortgage or having interest deferred and capitalised when in payment difficulties.

### **Suitability letters**

- 3.44 In the DP, we highlighted the arguments for and against requiring firms to provide consumers with post-sale suitability letters that summarised the consumer's needs and circumstances and explained why, given these, a particular recommendation had been made.
- 3.45 While many respondents were in favour of making suitability letters compulsory, some questioned the benefits to consumers, given the significant amount of information they already receive.
- 3.46 We have reconsidered the matter in light of the feedback received and in the context of the wider changes we are making to the sales process. We remain concerned that consumers get suitable products; however, given the limitations of disclosure as a regulatory tool, we believe our enhanced sales process outlined in Chapter 2 will be a much stronger method of ensuring this than requiring suitability letters.
- 3.47 We also recognise the limited value that these letters have in the mortgage market given that they are received after the sale when it is likely to be too late for the consumer to change to another product without incurring significant cost. This is in contrast to the value of suitability letters in the investment market, where the suitability of a product is a longer-term consideration and suitability letters have a useful and ongoing purpose in helping the consumer consider whether the product remains best for their circumstances.
- 3.48 Therefore, we do not see a strong case for making suitability letters a compulsory requirement in the mortgage market. The record-keeping required as part of the revised sales standards will instead provide a good basis for investigating any consumer complaints about the appropriateness of a product, and we will be looking to ensure firms comply with these. Firms can of course continue to provide suitability letters if they want to.

### **Equality and diversity issues**

- 3.49 We have identified the possibility that our proposals for disclosure could have an adverse effect on some groups with protected characteristics (e.g. race, religion, age, disability) when they wish to take out a mortgage. We are carrying out analysis on whether this is the case, and would welcome input from respondents.

Q17: Do you think that these disclosure proposals will impact any groups with protected characteristics (e.g. race, religion, age, disability)?

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44 See MCOB 7.6.

# 4 Discussion about niche market segments

## Background

- 4.1 The Mortgage Market Review (MMR) aims to remedy failures that have caused material mortgage market detriment. The measures we propose taking are designed principally with the mainstream mortgage market in mind. However, we recognise that there are several niche markets for which we are also responsible. In the MMR Discussion Paper (DP09/3)<sup>45</sup> we invited input on the impact of our proposals on the equity release markets.
- 4.2 The responses we have received have allowed our thinking to further develop. At this stage we are not proposing to consult on specific rule changes; instead we consider how our proposals might impact on these areas. We would welcome further views from stakeholders on the views set out here.

## Equity release

- 4.3 Our DP set out our reasons for not making specific proposals on equity release. Our existing conduct of business regulations already address the likely causes of consumer detriment in this market. We also thought that some proposals for the standard mortgage market would beneficially impact the equity release market. Responses to the DP raised concerns that our proposals could unintentionally have a negative impact on this market. We have further considered the impact of our proposals, focusing on areas where there is a clear difference between the equity release and the mainstream mortgage market.
- 4.4 As with the mainstream mortgage market, consumers have difficulty in understanding whether or not they have received advice. Most equity release products are sold on an advised basis.<sup>46</sup> In a non-advised sale, firms are required to consider whether a product broadly meets the needs and circumstances of the

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45 DP09/3: *Mortgage Market Review*, (October 2009): [www.fsa.gov.uk/pubs/discussion/dp09\\_03.pdf](http://www.fsa.gov.uk/pubs/discussion/dp09_03.pdf)

46 Data collected from firms shows that 97.46% of all lifetime mortgage sales in 2008 were advised. In 2009 this rose to 97.81%.

borrower.<sup>47</sup> Given the approach we are proposing in the mainstream mortgage market, we think there may be scope to strengthen this test. We will, of course, need to be clear on what ‘appropriate’ means for an equity release sale, as there are important differences from the mainstream market.

- 4.5 We know from the Mortgage Effectiveness Review<sup>48</sup> that lifetime mortgage consumers approach their purchasing decision differently to mainstream mortgage consumers. They are more likely to spend time over their buying decisions and will review information with friends, family and professionals. This means they are less likely to be making use of an Initial Disclosure Document (IDD). They know the product they want and are less likely to shop around for service.
- 4.6 We can therefore see a benefit in applying our disclosure proposals to equity release. This would mean that consumers may no longer get an IDD but are given key information about the scope of a firm’s service and how the firm will be remunerated (Chapter 2). As there are two distinct sectors in the equity release market (lifetime mortgages and Home Reversion plans) we would expect equity release advisers to disclose the scope of the service they offer in each market sector.
- 4.7 In principle, therefore, we see no reason why our distribution and disclosure proposals should not equally apply to equity release. We will continue to work on developing the finer detail, including the costs and benefits to this market. We are aware the proposed changes to the Mortgages and Home Finance: Conduct of Business sourcebook (MCOB) Chapters 4 and 5 may need consequential changes in relation to equity release (MCOB Chapters 8 and 9). Any necessary changes will form part of a future consultation.

Q18: Do you have any comments on the most appropriate way to read these proposals across to equity release?

## Home Purchase Plans

- 4.8 Home Purchase Plans (HPPs) are covered by our MCOB rules as they are a home finance product. We have kept a high-level, principles-based regime in this market since regulation began in 2007. The distribution and disclosure of HPPs is similar to regulated mortgage contracts, and so our proposals (and reasons behind them) appear relevant in this market. We therefore see benefits in reading across our distribution proposals. However, there are some differences in the disclosure requirements between regulated mortgage contracts and HPPs and we set out our current thinking on these below.
- 4.9 The IDD currently used in HPP sales allows for an additional section showing the name of the Islamic Scholar who has checked that the service being offered complies with Islamic law. This may be important to some consumers when choosing to go ahead with a firm, but could be lost under our initial disclosure proposals set out in Chapter 3. We will look into this issue before consulting on applying any changes.

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47 See the Mortgage and Home Finance: Conduct of Business sourcebook (MCOB) Chapter 8.6 [www.fsahandbook.info/FSA/html/handbook/MCOB/8/6](http://www.fsahandbook.info/FSA/html/handbook/MCOB/8/6)

48 Mortgage Effectiveness Review Stage 2 [www.fsa.gov.uk/pubs/other/MER2\\_report.pdf](http://www.fsa.gov.uk/pubs/other/MER2_report.pdf)

- 4.10 Pre-application disclosure is different for HPP as it includes a Financial Information Statement (FIS) rather than a Key Facts Illustration (KFI). However, we believe that consumers use the FIS in much the same way, so our proposals on product disclosure in Chapter 3 (and reasons behind them) could be read-across without complication.
- 4.11 The proposed changes to MCOB will need consequential changes in relation to HPPs. We will, therefore, be consulting on any necessary changes before our proposals take effect, in order to make the application and impact clear.<sup>49</sup>

Q19: Do you have any comments on the most appropriate way to read these proposals across to Home Purchase Plans?

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49 For example, see paragraph 2.81 of CP10/16 [www.fsa.gov.uk/pubs/cp/cp10\\_16.pdf](http://www.fsa.gov.uk/pubs/cp/cp10_16.pdf)

# 5 Discussion about data requirements

- 5.1 In the Mortgage Market Review (MMR) Discussion Paper (DP09/3)<sup>50</sup> we noted that changes to our regulatory approach would inevitably result in a need to review the current data collected through Product Sales Data (PSD), the Mortgage Lending and Administration Return (MLAR) and to a lesser extent the Retail Mediation Activities Return (RMAR).
- 5.2 We set out here our current thoughts about the changes that may be needed. It is important to stress that our thinking in this area is still developing but that we wish to engage the industry at as early a stage as possible. Before making any firm commitments about change, we want to discuss our views with firms and trade bodies and have a full understanding of the cost implications of change both for industry as well as ourselves. We also need to consider carefully the timing of any changes we make.

## Product Sales Data

- 5.3 Since 1 April 2005, product providers have provided us with transaction-level data on all sales of regulated mortgage contracts. The data we currently collect includes various mortgage and borrower characteristics and measures, most of which are compulsory for lenders to report.<sup>51</sup>
- 5.4 The changes we have been thinking about making to Product Sales Data (PSD) reporting include:
- making the reporting of some data fields that are currently optional mandatory;
  - adding new data fields to monitor compliance with the regulatory requirements;
  - adding new data fields to gather better evidence for FSA policy making and supervision (specifically, data on arrears, possessions and forbearance); and
  - clarifying the definition of credit impairment.

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50 DP09/3: *Mortgage Market Review*, (October 2009): [www.fsa.gov.uk/pubs/discussion/dp09\\_03.pdf](http://www.fsa.gov.uk/pubs/discussion/dp09_03.pdf)

51 Summary statistics from these returns are available on the FSA web-site: PSD trend reports – [www.fsa.gov.uk/Pages/Doing/Regulated>Returns/psd/publications/index.shtml](http://www.fsa.gov.uk/Pages/Doing/Regulated>Returns/psd/publications/index.shtml)

5.5 We explain the rationale for our views in the sections below.

### **Mandatory reporting of some data fields that are currently optional**

5.6 A number of data fields are currently reported in PSD on a voluntary basis, including:

- the date any incentive rate ends;
- the date an early payment charge ends; and
- the initial gross interest rate.

5.7 We think that it would help if completing these fields was mandatory rather than optional. This is because interest rate data would help us monitor compliance with our responsible lending requirements. Data on the date when incentive rates and early repayment charges end would help us understand better when borrowers are likely to remortgage and what effect changes in interest rates may have on borrowers' ability to service their debt.

### **Adding new data fields to monitor compliance with regulatory requirements**

5.8 If the proposed more prescriptive affordability checks in CP10/16 go ahead, to effectively monitor compliance with the new standards, it would help to have more data on borrowers' income and expenditure. For example, the incomes of each borrower in a mortgage application (currently, joint income is reported where there is more than one borrower); data on family size and on estimated expenditure.

5.9 To improve the quality of income data reporting in PSD, it would also help if we could introduce additional 'flags' for lenders to complete, which would allow us to identify 'special cases' where the reported borrower's income does not reflect the borrower's circumstances, such as 'staff mortgage', 'guaranteed mortgage', 'regulated buy-to-let mortgage', or 'regulated business mortgage'.<sup>52</sup>

### **Adding new data fields to gather better evidence for FSA policy making and supervision – arrears, possessions and forbearance**

5.10 Although we collect data on both individual mortgage transactions (PSD) and arrears/possessions/forbearance (MLAR), we are not currently able to link individual cases of non-performance back to the original transaction. This limits the extent that we can analyse the drivers of mortgage non-performance at an individual transaction level.

5.11 In 2009, the Council of Mortgage Lenders (CML) helped us obtain a one-off transactional arrears and possessions data report from a cross-section of banks, building societies and non-bank lenders – covering April 2005 to August 2009. The vast majority of lenders were able to report this data to a good standard within a relatively short period. This data proved invaluable for our policy analysis and helped inform many of our responsible lending proposals. We shortly plan to start

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52 We discovered serious problems with the quality of income data when we looked at individual transactions reported by lenders as part of our analysis for CP10/16.

another similar data collection exercise with the CML. In future, we would like to make this a regular part of firms' regulatory reporting requirements.

- 5.12 We raised the prospect of collecting transactional arrears and possessions data in the DP. We asked whether respondents agreed that we should collect data to enable us to track arrears and possessions cases back to the original product transaction.
- 5.13 Most respondents supported this proposal. Some felt that having such data would enable us to analyse risks taken by the lenders and to ensure that firms comply with the principles of responsible lending. A few though expressed concerns that linking arrears back to product characteristics would have limited value as payment difficulties are often caused by life events, such as unemployment or illness. Some respondents noted that the arrears and possessions data is already available to lenders and should not be difficult or costly to report. However, others expressed concerns that the additional data collection requirement may necessitate changes to IT systems and that the cost of this could be significant.

### **Clarifying the definition of credit impairment**

- 5.14 Because of recent legal developments, we may need to expand the types of credit impairment currently collected in PSD to include Debt Relief Orders (DROs). These are a new type of bankruptcy instrument that are not explicitly captured in the current definition used in PSD (although it is arguable that they might be implicitly captured). As DROs are new, they are not very prevalent at the moment, but might become more so in future (and be a substitute for bankruptcy orders). We may also introduce changes to the definition of County Court Judgements (CCJs).

### **Mortgage Lending and Administration Return**

- 5.15 Since the beginning of 2007, regulated mortgage lenders and administrators have had to submit a Mortgage Lending and Administration Return (MLAR) each quarter, providing aggregate data on their mortgage lending and administration activities.
- 5.16 We have undertaken a thematic review of forbearance practices with a view to improving the disclosure and recognition of these on reported arrears and impairment provisions. This review may conclude that additional reporting to the FSA would be useful to enable us to understand a firm's complete impairment profile. We will report on the outcome of this review in due course.

### **Retail Mediation Activities Return (RMAR)**

- 5.17 Since July 2005 retail intermediaries have had to provide us with aggregate data on their business in the Retail Mediation Activities Return (RMAR).
- 5.18 Minor changes to RMAR will be needed if the proposals discussed in Chapter 3 on changing the scope of service labels goes ahead.

## **Fees and charges**

- 5.19 Our DP announced our desire to collect fees and charges data. We are still considering what would be the most cost-effective way to collect this information. For lenders, we think it may not be feasible to require this data for every individual borrower at a transactional level. However, we would like to collect regular information on lenders' charges and procurement fees. Intermediaries currently report fee income from regulated mortgages in their RMAR. It is however difficult to determine with any degree of accuracy what the fees are on a case-by-case basis. So we are considering how we can refine this data requirement.
- 5.20 As noted earlier, our thinking about changes to data reporting is still developing and before we make any firm proposals about change, we would value input from firms and trade bodies to help inform our views.



# Cost-benefit analysis

## Introduction

1. The Financial Services and Markets Act 2000 (FSMA) requires us to publish a cost-benefit analysis (CBA) of our proposed rules and guidance, defined as ‘an estimate of the costs together with an analysis of the benefits’ that will arise if the proposed rules are made.
2. This CBA assesses, in quantitative terms where possible, and in qualitative terms where not, the cost and benefits of the proposed requirements set out in Chapters 2 and 3 of this Consultation Paper (CP). To do this it compares the situation that will arise once our proposed requirements are in place with that where they had not been introduced, i.e. the baseline.
3. We commissioned Oxera, an independent firm of economic consultants, to assess the compliance costs and the indirect costs of the policy proposals. We have published Oxera’s report separately.<sup>1</sup> In line with our approach to the CBA, Oxera has estimated the incremental costs of complying with our proposals, taking what firms currently do as the baseline.
4. The Oxera report was commissioned before some of the policy proposals were finalised. Where proposals have changed, we have supplemented Oxera’s analysis with additional requests for information from several firms and have also used information available to us from previous compliance and indirect costs studies.

## Scope of the CBA

5. This CBA covers the sales standards, professionalism and disclosure proposals. It does not cover Mortgage Market Review (MMR) proposals related to responsible lending<sup>2</sup> or present an analysis of the overall impact of the MMR.

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1 The Oxera report is available on our website at: [www.fsa.gov.uk/pages/Library/Policy/CP/2010/10\\_28.shtml](http://www.fsa.gov.uk/pages/Library/Policy/CP/2010/10_28.shtml)

2 For more on these see CP10/16, available at: [www.fsa.gov.uk/pubs/cp/cp10\\_16.pdf](http://www.fsa.gov.uk/pubs/cp/cp10_16.pdf)

6. The proposals consulted on in this CP are limited to regulated mortgage contracts that are not business loans. It also does not cover lifetime mortgages, Home Reversion Plans or Home Purchase Plans. Similarly, the CBA presented here only covers the impacts related to the covered regulated mortgage contracts.

## **Market failures**

7. The proposals set out to address several market failures in the mortgage market.<sup>3</sup>
8. First, consumers typically have less information about the products than the mortgage seller. Also, they often have limited ability to differentiate between good and poor quality sales staff, often believing that they are dealing with an expert in the field who knows the characteristics of the various different products and how they interact with their needs and circumstances. In addition, confusion about the service a seller provides can lead to consumers' expectations on the service they are receiving being inaccurate. Mortgage sellers can use these information asymmetries to their advantage and put forward products that are not appropriate for the consumer.
9. Second, assumptions by consumers that mortgage sellers are experts may reduce incentives for sellers to meet satisfactory levels of competency on the appropriateness of mortgage products for different consumers. This can lead to mortgages being offered to consumers that are not appropriate to their needs and circumstances.
10. Third, some consumers are liable to make choices about mortgages without fully understanding the consequences. This may be due to the effects of these choices materialising only a long time after a choice has been made, thus leading consumers to give insufficient consideration to these effects. The resulting incomplete weighing up of consequences by consumers increases the risk that they choose an inappropriate mortgage product.
11. Overall, the policy proposals on sales standards, professionalism and disclosure aim, by addressing these market failures, to increase the likelihood that consumers end up with a mortgage that meets their needs and circumstances.

## **Cost-benefit analysis**

12. This section sets out detailed costs and benefits of the proposals. It begins with the direct costs to us, i.e. those we will incur in implementing the proposals. It then presents estimates of the compliance costs of the proposals, i.e. those costs firms will incur in implementing the proposals. These draw largely on the Oxera report. It finishes with a discussion of the indirect impacts, i.e. the costs and benefits that will be incurred from the microeconomic impacts of the proposals.

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3 See Annex 2, DP09/3 for a more general discussion of the market failures motivating the MMR proposals.

## **Direct costs to the FSA**

13. The direct costs of regulation to the FSA are those we incur as a result of introducing and implementing our proposals. Our proposals will impact supervision and enforcement, and we anticipate that additional resourcing needs will mainly arise from supervising implementation and then supervising and enforcing compliance.
14. Our estimated costs are based on the working hypothesis that the following actions may be undertaken:
  - a) At the pre-implementation phase, communications and discussions with firms to ensure they are aware of the regime changes.
  - b) A review of adequacy of the implementation project.
  - c) Reviewing implementation with management; assessing adequacy of systems and controls; reviewing management information; reviewing the internal audit output; identifying shortcomings and feedback through the risk mitigation plan and close and continuous processes as appropriate.
  - d) Thematic work to test compliance, including supervisors dealing with potential instances of non-compliance with the new requirements.
  - e) Once implementation is complete, supervisors would move to a business-as-usual phase. Review of continued compliance would be included in firms' ARROW risk assessments.
15. As a result, we expect the incremental costs to the FSA to be in the region of £175,000 for one-off costs. Also, given the impact of the remaining MMR proposals on supervision, these estimates may need to be revised as we consult on these proposals.

## **Compliance costs**

16. In this section we provide the estimates of compliance costs for policy proposals for which we are publishing draft rules in this CP.
17. Oxera were commissioned to estimate compliance costs to firms. Their identification and analysis of the compliance costs and indirect costs were informed by interviews with the industry and through a survey of lenders which was already described in the CBA of CP10/16. Oxera's study was commissioned in March and therefore, in some cases, policy proposals have been modified following feedback from stakeholders or our own further consideration. When this has been the case, and the changes were likely to have a significant impact on our cost estimates, we have supplemented Oxera's analysis with additional requests for information to the industry and information that was available to us from previous CBAs or other sources.

18. Total compliance costs for the proposals for which draft rules are contained in this CP are estimated to be up to somewhere between £39m and £50m for one-off costs and up to £2m per annum for ongoing costs.

**Table 1 – Total industry compliance costs**

<b>Proposal</b>	<b>One-off cost (£m)</b>	<b>Annual cost (£m)</b>
Sales standards	0.8	1.0
Professionalism	17 - 28	–
Labelling	17	–
Ban automatic roll-up of fees	2	–
Replacing Initial Disclosure Document (IDD) and changing Key Facts Illustration (KFI) requirements	1.7	0.7
Changes to record-keeping requirements	–	0.3
<b>Total<sup>4</sup></b>	<b>39 - 50</b>	<b>2</b>

19. Oxera’s report does not cover the proposal to remove the requirement for intermediaries to assess affordability, or the alternative proposal that intermediaries only be required (instead of the current requirement) to determine whether the borrower meets the lender’s eligibility criteria. For the first, as it is a removal of regulation, incorporating it would reduce the cost estimates, as it would reduce compliance costs for intermediaries. The second, alternative proposal would imply a minimal change from current requirements. As such, we expect this is unlikely to lead to material compliance costs.
20. We discuss in more detail below the compliance costs associated with the other proposals.

## **Sales standards**

21. Oxera estimate that a significant majority of firms selling through a non-advised route already conduct an appropriateness assessment which is similar to that which we are consulting on. This implies that a large proportion of non-advised sales already meet the proposed requirements.
22. For firms that reported having to incur a one-off cost to enable them to comply with the requirement to make the assessment in all cases, the average cost was quite small. The reported one-off costs relate to having to train or recruit additional staff and from having to change systems.
23. Ongoing costs are also estimated to be relatively small, essentially because most firms already conduct similar tests or plan to introduce such tests in the future even in the absence of regulatory intervention. Ongoing reported costs were largely related to expected increases in time for collecting and assessing information for each sale and also include related costs, such as IT and other overheads.

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<sup>4</sup> Total figures are rounded to the nearest million.

**Table 2 – Sales standards compliance costs**

	<b>One-off cost (£ '000)</b>	<b>Annual cost (£ '000)</b>
Small firms	300	20
Large firms	96	97
Very large firms	420	880
<b>Industry total</b>	<b>0.8m</b>	<b>1.0m</b>

24. Our policy thinking has continued to evolve since we commissioned Oxera’s study. Therefore their estimates are based upon proposals that are slightly different from those we are consulting upon. For instance, although Oxera provided estimates for enhanced sales standards, we are proposing to introduce a requirement to include in the assessment of needs and circumstances whether the consumer should take a further advance with his existing lender, and whether it is appropriate to borrow into retirement. At the same time, we are proposing to remove the ‘most suitable’ rule.<sup>5</sup> Therefore, some changes increase the stringency of the proposals, while others weaken it. Overall, therefore, we expect that the costs incurred by firms in complying with the modified requirements are unlikely to differ materially from those estimated by Oxera.

### **Professionalism requirements**

25. It is proposed that all sellers (including those who do not give advice) be required to hold a Level 3 qualification (CeMap equivalent). We have directly estimated the compliance costs related to this proposal.
26. Following discussions with industry representatives and analysis of internal data we estimate the number of non-advised sellers active in the industry to be in the region of 3,000 to 5,000. Unfortunately, we are not in a position to know how many of them already hold a relevant qualification. However, discussions with the industry show that most lenders either require or encourage their sellers to hold such a qualification.
27. To estimate the cost of obtaining a qualification, we refer to an estimate obtained for a similar proposal, i.e. the professionalism strand of the Retail Distribution Review (RDR)<sup>6</sup>, where we estimated that the cost per non-advised seller to get a qualification to be in the region of £5,600 (including the opportunity cost of time).<sup>7</sup> This implies one-off compliance costs of between £17m and £28m. These figures are conservative estimates since they assume no non-advised sellers currently active in the industry already hold a qualification. Actual costs are expected to be well below this range, given our evidence that most lenders require or encourage their non-advised sellers to have a qualification.

5 The ‘most suitable’ rule is in MCOB 4.7. See Chapter 2 for more details on the proposal to remove it and to replace with a requirement to act in the client’s best interests

6 See PS10/6: *Distribution of retail investments: Delivering the RDR - feedback to CP09/18 and final rules* (March 2010): [www.fsa.gov.uk/pubs/policy/ps10\\_06.pdf](http://www.fsa.gov.uk/pubs/policy/ps10_06.pdf)

7 This figure will overestimate the true cost as the RDR requires retail investment advisers to be qualified at Level 4 and not to Level 3 as in the present case.

28. Also relevant here is that currently staff who do not give advice are subject to the ‘competent employee rule’. This provides that a firm must employ personnel with the skills, knowledge and expertise necessary to discharge the responsibilities allocated to them. The Training and Competence Sourcebook (TC), to which non-advised sellers will be subject to if we go ahead with the proposal we are consulting on, supplements the competent employee rule. However, there is already existing guidance for firms currently not subject to TC (e.g. non-advised sellers) which says that they may wish to take the TC into account in complying with their training and competence requirements. We would, therefore, expect that a scheme similar to TC would be in place for non-advised sellers in any case and thus believe that the ongoing costs associated with this proposal would be minimal.

## Labelling

29. Compliance costs associated with simplifying the labels currently in place so they broadly align with those used in the retail investment sector have been estimated by Oxera. They estimate that most firms will retain their ‘current’ status with ‘whole of market’ firms becoming ‘independent’ and ‘limited and single’ firms becoming ‘restricted’.
30. Sellers were asked to provide estimates of the one-off costs they would incur and estimates ranged from £0 to approximately £50,000 per firm. These one-off costs result from changing letter heads, disclosure documents and marketing materials. This resulted in an overall one-off cost for the industry of £17m.

**Table 3 – Labelling compliance costs**

	<b>One-off cost (£m)</b>
Small firms	14
Large firms	1.4
Very large firms	1.6
<b>Industry total</b>	<b>17</b>

31. There are no ongoing costs associated with this proposal as sellers will only be required to change labels once.
32. We are also placing an additional requirement on independent sellers to inform consumers whether they plan on sourcing direct-only deals. However, since complying with this would only require a minimal addition to the labelling changes outlined above, and are likely to be incorporated as part of the disclosure proposals outlined below, we do not expect the requirement to imply material costs beyond those already set out for both.

## **Banning of automatic roll-up of fees**

33. Oxera have estimated the compliance costs associated with a complete ban of rolling-up fees into the loan. Our policy has since evolved and we are now proposing to ban only the automatic roll-up of such fees. The lender will be required to obtain the borrower's consent to roll-up such fees in the loan.
34. Oxera report that over half of respondents, which included the largest providers of mortgages, indicated that the change would have no cost. Where a cost was indicated, this was in the range of £2,000 - £50,000 per firm. However, this includes two firms where the amount required to change their systems is so high relative to the volume of mortgages sold that a manual intervention on a transaction-by-transaction basis would be much more economic. Because of the limited number of responses, it is difficult to extrapolate a precise total cost to the industry of this proposal. However, of those lenders responding where it would make sense to automate the process, the average cost across all those responding is in the region of £6,000. Using this estimate, the total cost for the industry is around £2m. This amount clearly represents an upper bound of the overall one-off costs as only those lenders who automatically roll-up fees will be required to introduce changes.
35. We are also proposing that, when borrowers are considering rolling-up fees into the loan, sellers will be required to hand out two Key Facts Illustrations (KFIs), one which presents the costs with and one without the fees rolled-up. Also, sellers will be required to keep a record where the consumer elects to roll-up the fees. The compliance costs of this proposal are minimal as it will only apply to a subset of sales and would only require printing an additional KFI and where a consumer chooses to roll-up fees a minimal addition to their record-keeping.

## **Changes in record-keeping requirements**

36. We are consulting on extending our record-keeping requirements to include non-advised sales.
37. In order to estimate the costs associated with these changes we relied on a report that Real Assurance Risk Management produced for us in 2006.<sup>8</sup> The report estimates that keeping records of customer recommendations cost £639,000 for the entire industry in 2006. However, the requirement will be new only for non-advised sales which account for approximately a third of all sales. By updating the above figure to take this and inflation into account we obtain an incremental ongoing cost for the industry of £327,000.
38. Since non-advised sellers will generally have some existing systems in place to keep a record of their sales transactions, and these systems are likely with only minimal changes to be adequate for the record-keeping requirement proposed here, we would expect minimal one-off costs from the proposal.<sup>9</sup>

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<sup>8</sup> Real Assurance Risk Management, Estimation of FSA Administrative Burdens, June 2006.

<sup>9</sup> Minimal one-off costs are also consistent with Oxera's survey results on the discontinued suitability letter proposal (which included record-keeping requirements) and with estimates in the Real Assurance Report 2006 Estimation of FSA Administrative Burdens.

## **Disclosure – replacing the IDD with disclosure of key messages and changing the requirements for the KFI**

39. As a result of the process of evolving and refining our policy proposals, the Handbook changes relating to disclosure are slightly different from those Oxera used when conducting their compliance cost survey. The main differences are:
- reiterating scope (i.e. whether the seller is independent or restricted) when presenting products to the consumer;
  - removing trigger points to produce different KFIs when the consumer is considering various products;
  - requiring internet providers to ensure the consumer has viewed the message clearly on screen before moving to the next stage in the sales process;
  - requiring postal sale firms to draw the key messages out in a format other than an Initial Disclosure Document (IDD);
  - requiring firms to inform consumers that they can ask for a KFI if they wish (and to provide it where they do request it); and
  - removing the obligation to produce a KFI when the seller is putting forward a direct-only product (which is replaced with a requirement to give consumers a written record where they have recommended one of these products).

A more in-depth discussion of the proposals is contained in Chapter 3.

40. Taken together, the changes between the proposals contained here and those analysed by Oxera are unlikely to materially affect the compliance cost estimates. Some changes introduce only slightly more stringent requirements on sellers while others are likely to reduce the burden on sellers by removing obligations, for example, removing the trigger points for producing different KFIs. Given this, it is our view that the estimates produced by Oxera remain a reasonable estimate for the costs associated with the proposals. We now turn to reporting Oxera's estimates.

### *Oxera's analysis*

41. Since firms may still retain the IDD if they wish to do so Oxera envisage that the proposal to replace the IDD with the disclosure of key messages in a durable medium will not imply any compliance cost for firms.
42. Oxera report that about 80% of firms are 'likely' or 'very likely' to retain the IDD as a means of satisfying the general requirement to disclose key service information early in the sales process, with only 10% of firms indicating that they are likely to replace the IDD, and a further 10% not yet sure of whether the IDD would be retained. Overall, therefore, around 10% of firms will be likely to change how they present this information to consumers.
43. Oxera estimate that those sellers that would not retain the IDD would incur a cost of approximately £1,700 for small firms, and £1,500 for large and very large firms to satisfy this requirement. One-off costs would be incurred from developing



alternative disclosure documents or using existing documents to replace the IDD. The overall cost to the industry is estimated to be around £1.7m. However, given that firms could avoid this cost by continuing with the IDD, they are only likely to incur costs if they gain some additional benefits that outweigh the costs.

44. The ongoing costs of producing an alternative disclosure document would amount to around £0.40 per copy, resulting in an estimated cost per sale of £0.60 given that there are approximately 1.5 recommendations per sale.<sup>10</sup> This results in an industry cost of £19,000 per year. However, Oxera also report that since the IDD will not be produced in these cases, there is likely to be a saving from the reduction in ongoing costs.
45. Oxera also estimated the cost associated with providing oral disclosure of the IDD. Given that we are only requiring the disclosure of some key messages, Oxera's figures may overestimate the true cost. However, we have not reduced the estimates to take into account the new requirements to reiterate the scope of service. Oxera report that, for those sales where the respondent firm already speaks to the consumer (in person or over the phone), firms indicated that oral disclosure would require an industry average of eight minutes. Oxera then estimate that the industry cost per sale would be approximately £11 and a total industry cost of £0.7m.

## **Costs and benefits from microeconomic impacts of the proposals**

46. This section presents the costs and benefits that we expect to follow from the microeconomic impacts of the proposals consulted on in this CP.

### **Costs**

47. The indirect impacts associated with the sales standards and disclosure proposals have been assessed by Oxera in conjunction with their analysis of the responsible lending proposals discussed in CP10/16. In this section, we present a summary of their analysis and conclusions, supplemented with our analysis of the professionalism requirements which were not covered by Oxera.

### **Indirect costs of the sales standards and disclosure proposals**

48. Overall, Oxera expect that the impacts on the quantity of sales, on the variety of products, on the functioning of competition and on market structure associated with sales standards and disclosure proposals to be limited, and unlikely to have material implications.
49. We briefly summarise some of the effects, due to distribution and disclosure proposals, identified by Oxera below. In terms of impacts on the quantity of sales, a few firms believed that some consumers may be deterred by the additional administrative burden, i.e. the more lengthy sales process and the additional time

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<sup>10</sup> This is also an overestimate since only one IDD (or alternative document) would be provided for a customer even where several recommendations were made, unless the nature of the service changed.

required to process each sale. However, Oxera's view is that the increase in the administrative burden will be small relative to the size of the transaction and, therefore, it is unlikely that it would result in a significant reduction in sales.

50. The only potential impact identified on the variety of products and processes in relation to the increased similarity between advised and non-advised sales channels. This may especially impact those consumers who know what product they want, who would prefer to minimise the sales procedure and would thus prefer a sales process that is as close as possible to an execution-only service. Oxera noted, however, that this kind of consumer would still be able to reject the advice they receive and instead choose their preferred product with only a minimal increase in sales time. Given this, we expect the overall effect from this to be small.
51. No detrimental effects on competition were found as the overall changes to the process are small. However, Oxera noted that the labelling requirement for some sellers to disclose that they do not deal in direct-only products, may incentivise consumers to move from intermediaries to direct-only sales. This might have competition impacts through increased shopping around by consumers and increased price competition. Oxera also reported that market structure should not be impacted by the sales standards and disclosure proposals.

### **Indirect costs from professionalism requirements**

52. As set out in the compliance cost section, we expect the professionalism requirements to impose direct costs on some non-advised sellers from the requirement to increase, if necessary, their level of qualification. In theory, the additional one-off costs could act to increase barriers to entry for non-advised sellers and have market impacts as a result. However, our evidence from discussions with industry is that most lenders already require their non-advised sellers to hold a relevant qualification. Given this, we believe that a relatively small number of non-advised sellers would be impacted by the proposal. However, these non-advised sellers, according to existing guidance, should satisfy a competency level set out in the TC sourcebook. Also, since it imposes a minimum standard for all sellers, the requirements should not favour one group of sellers over others. In summary, the proposals are unlikely to have material impacts on competition.

### **Benefits**

53. A removal of the requirement for intermediaries to assess affordability would benefit intermediaries by reducing the regulatory burden on them.
54. The benefits from the other proposals will materialise from a mitigation of the market failures set out above, which together should increase the suitability of mortgages offered and accepted by consumers. This will benefit consumers from their avoiding detriment they would otherwise have suffered from having mortgages that were less well suited to their needs and circumstances.
55. In particular, the sales standards, professionalism and disclosure proposals should address market failures and bring about benefits in the following ways:

- a) The proposals on sales standards, by requiring that an appropriateness test is performed for all sales, aim to mitigate the risks that consumers end up with products that are not appropriate for them, i.e. they aim to ensure consumers are only presented with products that match their needs in terms of length of the mortgage, stability of payments, exposure to interest rate risk, etc.
- b) The proposals on professionalism address consumers' beliefs on the quality, role and expertise of mortgage sellers and are also tailored to changes we are proposing in sales standards. They should ensure that, even if they do not provide advice, non-advised sellers have the requisite understanding of the various characteristics of the products they discuss with consumers, so they are in a position to understand whether or not a specific mortgage product meets their client's requirements.
- c) To address the information asymmetries and how consumers make their mortgage decisions, it is important to give consumers the information they may need when choosing a firm, product (or whether to accept an adviser's recommendation). Focusing disclosure requirements on the service the seller is providing and giving information on the effects of consumers' choices, (e.g. the choice of rolling up mortgage fees into the loan) should – to the extent that the disclosure is effective – help improve consumers' understanding of the products and services they are receiving.
- d) Allowing consumers a choice in whether their mortgage fees are rolled-up into the loan should help to minimise detrimental outcomes for consumers. We can provide an estimate for the expected benefit per impacted mortgage. By using £920 as the average mortgage fee, 4.5% as the average rate on a mortgage<sup>11</sup>, 3.5% as the discount rate and assuming that the mortgage lasts for 25 years, the benefit of banning automatic roll-up of fees per impacted mortgage is estimated to be approximately £100.<sup>12</sup> To calculate an overall figure for the benefits from this, we would need to know how many consumers are currently obliged to roll-up fees and would choose not to. Internal research showed that the percentage of loans where fees are rolled up varies considerably between lenders and that a few of them do automatically roll-up such fees. In addition, it is likely that most consumers who choose to roll-up fees do so for good reasons (e.g. because the cost of other types of credit is higher) and would still do so even if our new rules will be implemented. These issues make the number of consumers who would benefit difficult to estimate.
- e) The record-keeping changes should strengthen the internal and external monitoring of sales processes, which should in turn strengthen the incentives of non-advised sellers to provide appropriate mortgage products and thus, further improve sales processes.

Q20: Do you have any comments on the  
cost-benefit analysis?

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11 These figures are taken from Moneyfacts Treasury Reports, Mortgage Trends, October 2010.

12 However, this figure may underestimate the true benefit since we would expect the people who do roll-up fees to be a higher risk profile than average borrowers and thus more likely to pay a higher interest rate and a higher fee than the average mortgagee.



# Compatibility statement

## Introduction

1. In this section we set out our view on how the proposals and draft rules in this Consultation Paper (CP) are compatible with our general duties under Section 2 of FSMA and our regulatory objectives set out in Sections 3 to 6 of the Financial Services and Markets Act (FSMA). This section also outlines how our proposals are consistent with the principles of good regulation (also in Section 2 of FSMA) to which we must have regard.

## Compatibility with our statutory objectives

2. The policy proposals and draft rules in this CP contribute to three of our statutory objectives, more materially to some rather than others.

## Market confidence

3. We believe that our policy proposals will improve the standards of those that work in the home finance business. In addition, our focused disclosure regime will ensure that consumers take away key messages from the mortgage sale, such as the scope of products the firm is able to source and the costs for the service they are receiving. We would expect this to increase a consumer's understanding of, and so improve confidence in, the service of the firm.

## Consumer protection

4. There is a risk that in a non-advised sales process a consumer could be presented with a product which does not meet his/her needs and circumstances. Our draft rules address this by imposing a consistent standard of 'appropriateness' across all sales which will ensure that consumers are not presented with inappropriate products.

## **Reducing financial crime**

5. Because of the lower regulatory standards that have applied, there has been a greater risk of mortgage fraud or other financial crime being committed through a non-advised sale. By creating a standard assessment of appropriateness for all mortgage sales we are increasing the professional standards and regulatory accountability of firms and individuals in mortgage transactions, thereby reducing the opportunity for them to commit a financial crime.

## **Compatibility with the Principles of Good Regulation**

6. Section 2(3) of FSMA requires that, in carrying out our general functions, we consider the principles of good regulation. The proposals we set out in Chapters 2 and 3 fulfil all seven of our principles of good regulation:

### **a) The need to use our resources in the most efficient and economic way**

7. As outlined in the cost-benefit analysis (CBA) at Annex 1, we anticipate devoting additional resource to supervision and enforcement to ensure the delivery of our new requirements. In line with our approach elsewhere, we will use thematic tools to ensure efficient use of our resource.

### **b) The responsibility of those who manage the affairs of authorised persons**

8. Our proposals clarify and strengthen the principle that the firm must not present products to consumers which do not meet their needs and circumstances. Removing our detailed requirements for sellers to carry out an affordability assessment will make clear that ultimate responsibility for affordability lies with the lender.

### **c) The principle that a burden or restriction which is imposed should be proportionate to the benefits**

9. The proportionality of our approach is addressed in the CBA at Annex 1. The proposed rules are expected to lead to ongoing benefits from improved appropriateness of mortgage products for consumers. We would expect this to offset the one-off costs and the relatively low ongoing costs.

### **d) The desirability of facilitating innovation**

10. We do not believe our proposals on distribution and disclosure will impact on firms' ability to innovate. For example, firms will continue to be able to create on-line business models within the parameters of our draft rules, using structured questioning and filtering the consumer's product choice based on their needs and circumstances.

### **e) The international character of financial services and markets and the desirability of maintaining the competitive position of the United Kingdom**

11. In developing our proposals we have had particular regard to international parallels, and especially the possibility of European intervention on distribution and disclosure. This remains a key dependency, as we are mindful of the need to minimise the number of changes for firms. Our assessment is that the changes we need to make now to address specific UK market issues will not have a materially damaging effect on the competitive position of the UK.

### **f) The need to minimise the adverse effects on competition**

12. As explained in the CBA in Annex 1 we believe our proposals will have minimal adverse effects on competition.

### **g) The desirability of facilitating competition**

13. As explained in the CBA in Annex 1, we do not believe our proposals will have a material effect on the facilitation of competition.

### **h) Promoting public awareness**

14. As well as enhancing our obligations on firms, the proposed changes to the sales process will have the effect of highlighting to borrowers the importance of fully considering whether a product meets their needs and circumstances. Alongside this, we will be working with the Consumer Financial Education Body (CFEB) to continue to promote a number of initiatives aimed at facilitating greater understanding, knowledge and engagement among mortgage borrowers.

## **Why our proposals are most appropriate for the purpose of meeting our statutory objectives**

15. Our proposals draw on a comprehensive evidence base, and follow from extensive engagement with those interested in the mortgage market. We have previously reported on the feedback to the Mortgage Market Review (MMR) Discussion Paper (DP09/3).<sup>1</sup> We have taken account of these views in our further policy development. We have also had many helpful discussions with a wide range of stakeholders in the lead up to this CP, adding to our knowledge of the market issues and the complexities to be addressed.
16. We believe the proposals described in this CP represent the most appropriate and proportionate approach to ensuring that distribution delivers positive outcomes to consumers and that disclosure requirements are focused on key messages we want consumers to take away. The proposals will benefit both firms and consumers by ensuring that meeting their needs is at the heart of every mortgage sale.

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1 DP09/3: *Mortgage Market Review*, (October 2009): [www.fsa.gov.uk/pubs/discussion/dp09\\_03.pdf](http://www.fsa.gov.uk/pubs/discussion/dp09_03.pdf)

Q21: Do you have any comments on the compatibility statement?

Q22: Do you have any comments on the draft rules?



# Consultation questions

- Q1: Do you agree that we should continue to allow consumers to get a mortgage without advice? If not, what other options should we consider and how would these result in better outcomes for consumers?
- Q2: Do you agree with removing from sellers any requirement to assess affordability?
- Q3: Can you see any risks from us adopting this approach?
- Q4: Do you agree with our proposed approach to ensuring appropriateness is assessed in every sale? If not, in what circumstances do you believe the checks should be waived and how could we prevent this being used as a mechanism to circumvent our requirements?
- Q5: Do you agree with our proposal for a 'client's best interest rule' and removing the obligation for a recommended mortgage to be the 'most suitable' product?
- Q6: Do you agree with our approach to applying common professional standards across the mortgage market?
- Q7: Do you agree with our proposals to include these three elements as part of the new appropriateness test?
- Q8: Do you agree with our proposal to improve the disclosure of the impact of the roll-up of fees through the provision of a second KFI?
- Q9: Do you agree with our proposal to require firms to present consumers with a choice of rolling-up the fees and charges, and to record the decision made?
- Q10: Do you agree or have any other suggestions about how to improve consumer awareness of the impact of rolling-up fees and charges?

- Q11: Do you have any views on other ways in which we could promote consumer engagement?
- Q12: Do you think that these distribution proposals will impact any groups with protected characteristics (e.g. race, religion, age, disability)?
- Q13: Do you agree that it is appropriate to focus our service disclosure on these key messages? Do you agree that this is the correct approach for communicating these messages to consumers?
- Q14: (i) Do you agree with our application of the 'independent' and 'restricted' labels to the mortgage market?
- (ii) Do you agree that we should require 'independent' firms to disclose whether they consider direct-only deals?
- (iii) Do you agree that we do not need to retain a fee option as part of our requirements for the label of 'independent'?
- Q15: Do you agree that firms should reiterate their scope at the point that they put the product(s) forward?
- Q16: (i) Do you agree that we make these changes to the trigger points for the pre-application KFI?
- (ii) Do you agree that we should have a requirement to make firms tell consumers that they can request a KFI for any product they offer?
- (iii) Do you agree that we should require firms to provide the consumer with a record, rather than a KFI, where they recommend a direct-only deal?
- Q17: Do you think that these disclosure proposals will impact any groups with protected characteristics (e.g. race, religion, age, disability)?
- Q18: Do you have any comments on the most appropriate way to read these proposals across to equity release?
- Q19: Do you have any comments on the most appropriate way to read these proposals across to Home Purchase Plans?
- Q20: Do you have any comments on the cost-benefit analysis?
- Q21: Do you have any comments on the compatibility statement?
- Q22: Do you have any comments on the draft rules?

# Draft instruments

## MORTGAGES (SALES STANDARDS AND DISCLOSURE) INSTRUMENT 2011

### Powers exercised

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making power);
  - (2) section 156 (General supplementary powers); and
  - (3) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purposes of section 153(2) (Rule-making instruments) of the Act.

### Commencement

- C. This instrument comes into force on [*date*].

### Amendments to the Handbook

- D. The modules of the FSA’s Handbook of rules and guidance listed in column (1) below are amended in accordance with the Annexes to this instrument listed in column (2) below.

(1)	(2)
Glossary of definitions	Annex A
Conduct of Business sourcebook (COBS)	Annex B
Mortgages and Home Finance: Conduct of Business sourcebook (MCOB)	Annex C
Training and Competence sourcebook (TC)	Annex D

### Amendments to material outside the Handbook

- E. The Perimeter Guidance Manual (PERG) is amended in accordance with Annex E to this instrument. The general guidance in PERG does not form part of the Handbook.

### Citation

- F. This instrument may be cited as the Mortgages (Sales Standards and Disclosure) Instrument 2011.

By order of the Board  
[*date*]

## Annex A

### Amendments to the Glossary of definitions

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

Insert the following new definitions in the appropriate alphabetical position. The text is not underlined.

<i>independent service</i>	<p>a service in which a <i>firm</i> provides a <i>customer</i> with a <i>personal recommendation</i> or personalised information in relation to a <i>home finance transaction</i> which is:</p> <ul style="list-style-type: none"><li>(i) unbiased and unrestricted; and</li><li>(ii) based on a comprehensive and fair analysis of the market for that type of <i>home finance transaction</i>;</li></ul> <p>but which need not include <i>home finance transactions</i> that can only be obtained direct from one or more <i>home finance providers</i> which do not include the <i>firm</i>.</p>
<i>restricted service</i>	<p>A service in which a <i>firm</i> provides a <i>customer</i> with a <i>personal recommendation</i> or personalised information in relation to a <i>home finance transaction</i> which is not an <i>independent service</i>.</p>

Amend the following definitions as shown.

<i>combined initial disclosure document</i>	<p>information about the <i>scope of advice</i>, <del>or scope of</del> <u>basic advice or scope of services</u> and the nature of the services offered by a <i>firm</i> in relation to two or more of the following:</p> <ul style="list-style-type: none"><li>(a) <i>packaged products</i> or, for <i>basic advice</i>, <i>stakeholder products</i>;</li><li>(b) <i>non-investment insurance contracts</i>;</li><li>(c) <i>regulated mortgage contracts</i> other than <i>lifetime mortgages</i>;</li><li>(d) <i>home purchase plans</i>;</li><li>(e) <i>equity release transactions</i>;</li></ul>
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which contains the keyfacts logo, headings and text in the order shown in, and in accordance with the notes in, *COBS* 6 Annex 2.

*initial disclosure document*

information about the *scope of advice*, scope of services and the nature of the services offered by a *firm* in relation to:

(a) a *regulated mortgage contract* other than a lifetime mortgage ~~as required by~~ in accordance with *MCOB* 4.4.1R (1) 4.4.4CG (1) and set out in *MCOB* 4 Annex 1R; ~~1RG~~;

(b) an *equity release transaction* as required by *MCOB* 4.4.1R(1) and set out in *MCOB* 8 Annex 1R;

(c) a *home purchase plan* as required by *MCOB* 4.10.2R and set out in *MCOB* 4 Annex 1R; or

(d) a *non-investment insurance contract* in accordance with *ICOBS* 4.5.1G and set out in *ICOBS* 4 Annex 1G.

## Annex B

### Amendments to the Conduct of Business sourcebook (COBS)

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### 6 Annex 2 Combined initial disclosure document described in COBS 6.3, ICOBS 4.5, MCOB 4.4.1R(1) 4.4.4CG(1) and MCOB 4.10.2R(1)

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...

#### Home Finance Products [Note 13]

...

[1] [Lifetime] [Mortgages] [Equity Release Products] [and home reversion schemes] [Note 13]

Independent - We offer [lifetime] [mortgages] [home reversion plans] [equity release products] based on a comprehensive and fair analysis of the market from the whole market.

We will [not] include in our search mortgages that can only be obtained directly from [a/another] [lender] [Note 13A] [Note 13B]

Restricted - We [can] [~~Note 7~~] only offer [lifetime] [mortgages] [home reversion plans] [equity release products] from one or a limited number of [lenders / companies]. [**Note 13C**]

Ask us for a list of the [lenders / companies] we offer [lifetime] [mortgages] [home reversion plans] [equity release products] from and any restrictions on the range available. [**Note 13D14**]

We [~~can~~] [~~Note 7~~] only offer [~~a limited range of the~~] [~~a~~] [lifetime] [mortgage] [s] [~~home reversion plan~~] [s] [equity release products] from [~~a single lender / company~~] [~~name of single lender / company~~]. [~~Note 11(1) and (3)~~][**Note 16**]

{or}

We only offer our own [lifetime] [mortgages] [home reversions plan] [equity release products]. [**Note 11(2)**]

We do not offer [lifetime mortgages] [home reversion plans]. [**Note 12**]

...

**Note 7** – insert “can” if the *firm’s* range of products is determined by any contractual obligation. This does not apply where a *product provider, insurer, or lender, home purchase provider or home reversion provider* is selling its own products.

...

## **Note 11**

...

- (1) Insert the name of the provider, namely the *product provider* for *packaged products*, the *insurance undertaking(s)* for *non-investment insurance contracts*, ~~the lender for regulated mortgage contracts and regulated lifetime mortgage contracts~~ and the *home reversion provider* for *home reversion plans*. For example: “We can only offer products from [name of *product provider*]”. For *non-investment insurance contracts* the type of insurance offered should also be included. For example: “We only offer ABC’s household insurance and ABC’s motor insurance.” If the provider has only one product, the *firm* should amend the text to the singular – for example: “We can only offer a mortgage from [name of lender]”. If the *firm* does not offer all of the *home finance transactions* generally available from that provider, it should insert the words “a limited range of” as shown in the specimen.

...

- ~~(3) If the *firm* offers *home reversion plans* from only one *reversion provider*, and *lifetime mortgages* from only one *lender*, which is different from the *reversion provider*, then the *firm* should identify the *lender* and the *reversion provider* and specify the type of *equity release transaction* to which they relate. For example, “We can only offer lifetime mortgages from ABC Mortgages Ltd and home reversion plans from ABC Reversions Ltd.”~~

...

**Note 13A** - This sentence is required only where a firm selects this service option and its service includes *regulated mortgage contracts*.

**Note 13B** - Insert "not" if the firm does not consider in its search *regulated mortgage contracts* that the consumer can not obtain through the *firm* and only by going directly to a lender. If the *firm* is not a lender itself, use “a” and if the firm is a lender, use “another”.

**Note 13C** - if the *firm* selects this box, it will be offering:

(a) products from a limited number of lenders/companies; or

(b) products of a single lender/company; or

(c) its own products (e.g. where the *firm* is a *lender/company* offering only its own products, or is part of a *lender/company* offering only the products sold under that part’s trading name).

The *firm* should replace the preceding text with the relevant text as set out below. If the *firm* does not select this box, then no amendments should be made to the preceding text.



(a)	We [can] <b>[note a]</b> only offer [lifetime][mortgages][home reversion plans][equity release products] from a limited number of [lenders/companies]
(b)	We [can] <b>[note a]</b> only offer [lifetime][mortgages][home reversion plans][equity release products] from [name of lenders/companies] <b>[note b]</b>
(c)	We [can] <b>[note a]</b> only offer [a limited range of the] [a] [lifetime][mortgage[s]][home reversion plan[s]][equity release product[s]] from a single lender/company [name of lender/company] <b>[note c] [note d]</b>
(d)	We only offer our own [lifetime][mortgages][home reversion plans][equity release products].

[Note a] - insert “can” if the *firm’s* range of *regulated mortgage* contracts, or *equity release transactions* is determined by any contractual obligation

[Note b] – The *firm* can use this option instead of (a) if it prefers to list all of the lenders or companies it offers *regulated mortgage* contracts or *equity release transactions* from, so long as the *firm* offers all of the *regulated mortgage* contracts or *equity release transactions* generally available from each lender or company.

[Note c] - if the *firm* selects this text, it must insert the name of the lender or company. If the *firm* does not offer all of the *regulated mortgage* contracts, or *equity release transactions* generally available from that lender or company, it must insert the words "a limited range of the", as shown. If the lender or company only has one relevant product, the *firm* should amend the text to "We can only offer a [lifetime][mortgage][home reversion plan][equity release product] from [name of single lender/company]."

[Note d] – if the *firm* offers *home reversion plans* from only one *reversion provider*, and *lifetime mortgages* from only one *lender*, which is different from the *reversion provider*, then the *firm* should identify the *lender* and the *reversion provider* and specify the type of *equity release transaction* to which they relate. For example, “We can only offer lifetime mortgages from ABC Mortgages Ltd and home reversion plans from ABC Reversions Ltd.”

**Note 13D** - this sentence is required only where a firm selects this service option and describes its scope using the text option (a) in Note 13C.

**Note 14** – for services provided in relation to *home purchase plans finance transactions*, this sentence is required only where a *firm* selects this service option. It may also be omitted if a *firm* chooses to list all of the *lenders*, *home purchase providers* and *home reversion providers* it offers *home purchase plans finance transactions* from in the previous line, so long as the *firm* offers all of the products generally available from each.

...

## Annex C

### Amendments to the Mortgages and Home Finance: Conduct of Business sourcebook (MCOB)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

#### 3.8 Form and content of real time qualifying credit promotions

...

- 3.8.6 G *Firms* should note the additional disclosure requirements in MCOB 4.4.7 ~~R~~ 4.4.4AR (Additional disclosure ~~Disclosure~~ where initial contact is by telephone) and MCOB 4.5 (Additional disclosure for distance mortgage mediation contracts and distance home purchase mediation contracts with retail customers) in relation to telephone calls that may fall within the definition of a *financial promotion*.

...

#### 4 Advising and selling standards

##### 4.1 Application

...

- 4.1.2 R This table belongs to MCOB 4.1.1R

(1) Category of firm	(2) Applicable section
...	
<i>mortgage arranger</i>	whole chapter except <del>MCOB 4.7</del> and MCOB 4.10

...

##### 4.2 Purpose

- 4.2.1 G (1) This chapter amplifies *Principle 6* (Customers' interests), *Principle 7* (Communications with clients) and *Principle 9* (Customers: relationships of trust).
- (2) The purpose of this chapter is to ensure that:
- (a) *customers* are adequately informed about the scope, nature and cost of the service which they may receive from a *firm* in relation to

*home finance transactions*<sup>1</sup>. In particular *firms* need to make clear to *customers* the scope of *home finance transactions* available from them; and

- (b) where ~~*advice*~~ a personal recommendation or personalised information is given, it is ~~suitable for~~ meets the needs and circumstances of the customer and the customer meets the lender's eligibility criteria for the product<sup>2</sup>. The steps *firms* need to take to ensure that the *customer* receives ~~suitable~~ *advice* a personal recommendation or personalised information which meets these requirements will vary depending on the ~~demands and needs of the individual~~ customer and the type of *home finance transaction*.

...

### 4.3 Scope of service provided

#### ~~Providing services within and beyond scope~~

4.3.1 R (1) ~~Subject to (2), a firm must take reasonable steps to ensure that the scope of the service given to a customer, and the home finance transactions offered, is based on a selection from one of the following:-~~

~~(a) the whole market; or~~

~~(b) a limited number of home finance providers; or~~

~~(c) a single home finance provider. [deleted]~~

(2) ~~A firm may change the scope of the service it gives to a particular customer by widening the scope, for example, from that in (1)(c) to that in (b) or (a) but it must take reasonable steps to ensure that~~

---

<sup>1</sup> As explained in paragraph 1.6 of this consultation paper, we are consulting now on changes to our Handbook for regulated mortgage contracts (other than lifetime mortgages and business loans) only. We will consult at a later date on changes to the Handbook for other home finance transactions; for that reason, we have not prepared draft Handbook text showing the provisions for other product types as remaining unaltered. Where existing rules or guidance have a wider ambit, we have changed them in line with our proposals for regulated mortgage contracts other than lifetime mortgages and business loans. This is for convenience only and to avoid unnecessary drafting. Accordingly, any proposed change in this Annex which appears to have wider effect should be read with that in mind.

<sup>2</sup> As explained in paragraphs 2.21 to 2.25 of this consultation paper, we are putting forward two options for the conditions which must be met before a firm can make a personal recommendation or give personalised information in relation to a regulated mortgage contract. Our starting point is that (while we would always expect sellers to consider, as part of ascertaining whether a regulated mortgage contract is appropriate to the needs and circumstances of the customer, whether the customer's requirements appear to be within the mortgage lender's expected eligibility criteria: see MCOB 4.7.8R (1)) sellers should not be obliged to assess compliance with the lender's eligibility criteria in relation to affordability i.e. that the obligation should be that in MCOB 4.7.2 R (1) (b); however, we have also drafted an obligation to check whether the customer meets these criteria - at MCOB 4.7.2 R (1) (a) - to show the effect on our Handbook should this option be adopted following consultation. Accordingly, all references in this Annex to the lender's eligibility criteria should be read with this in mind.

~~before doing so:-~~

- ~~(a) the *customer* is made aware of the proposed change by a communication in a *durable medium*; and~~
- ~~(b) the *customer's* attention is drawn to any change in the *fees* that the *customer* must pay to the *firm* for the *firm's* services. [deleted]~~

4.3.2 R ~~A *firm* must take reasonable steps to ensure that the extent of the scope of the service which it holds itself out as offering to a *customer* reflects the extent of that scope in practice. [deleted]-~~

4.3.3 G ~~*SYSC 3.2.6R* and *SYSC 6.1.1R* (Compliance) requires a *firm* (including a *common platform firm*) to 'establish, implement and maintain effective systems and controls for compliance with applicable requirements and standards under the *regulatory system*'. In meeting this requirement in relation to *MCOB 4.3.2 R*, a *firm* which states that it provides a service based on a limited number of *mortgage lenders* (see *MCOB 4.3.1R(1)(b)*) should have adequate systems and controls in place to monitor whether business is actually placed with those *mortgage lenders*. [deleted]~~

~~Whole of market~~

- 4.3.4 R (1) ~~A *firm* which holds itself out as giving information or *advice* to *customers* on *regulated mortgage contracts* from the whole market must not give any such information or *advice* unless:-~~
- ~~(a) it has considered a sufficiently large number of *regulated mortgage contracts* which are generally available from the market; and~~
  - ~~(b) the consideration in (a) is based on criteria which reflect adequate knowledge of the *regulated mortgage contracts* generally available from the market as a whole. [deleted]~~
- (2) ~~A *firm* in (1) must satisfy the obligation in *MCOB 4.7.2 R* by taking reasonable steps to ensure that a *personal recommendation* given to a *customer* is:-~~
- ~~(a) in accordance with the consideration in (1); and~~
  - ~~(b) the *regulated mortgage contract* which on the basis of that consideration is the most suitable to meet the *customer's* needs. [deleted]~~

Services to be provided on independent or restricted basis

4.3.4- R A *firm* must provide a *customer* with either an *independent service* or a

A restricted service.

4.3.4A R In applying this chapter, there is:

- (1) one market for *regulated mortgage contracts* that are not *lifetime mortgages*; and
- (2) another market for *home purchase plans*.

Guidance on providing an independent service

4.3.5 G If a *firm* holds itself out as ~~giving information or advice~~ providing an independent service to customers on regulated mortgage contracts generally available from the whole market, the *firm* may choose to offer its *customers* only a selection of ~~those~~ the regulated mortgage contracts available from the relevant market. The *firm's* selection of *regulated mortgage contracts* for this purpose will need to be sufficiently large to enable the *firm* to satisfy the suitability comprehensive and fair analysis requirement in ~~MCOB 4.3.4R (Whole of market)~~ the definition of an independent service.

4.3.6 G (1) When offering only a selection of *regulated mortgage contracts* as described in *MCOB* 4.3.5G, a *firm* should ensure that its analysis of the market and of the available *regulated mortgage contracts* is kept adequately up to date. For example, a *firm* would need to update its selection of *regulated mortgage contracts* if it became aware that a *regulated mortgage contract* had become generally available offering an improved product feature, or a better interest rate, when compared with the *regulated mortgage contracts* currently in the *firm's* selection.

(2) ~~One way in which a firm may wish to satisfy MCOB 4.3.4R is by using a panel of mortgage lenders, which includes representative firms from the whole market. However, if a firm wishes to offer a whole of market service through the use of a panel, it must still assess the individual regulated mortgage contracts that are being offered by mortgage lenders in making its selection. [deleted]~~

(3) A firm may provide an independent service by using 'panels'. A firm would need to ensure that any panel is sufficiently broad in its composition to enable the firm to make personal recommendations or give personalised information based on a comprehensive and fair analysis, is reviewed regularly, and that the use of the panel does not materially disadvantage any customer.

4.3.6A G A firm that provides both an independent service and a restricted service should not hold itself out as acting independently for its business as a whole.

Independence

4.3.7 R (1) ~~When providing information or giving advice to a customer on home finance transactions, a firm must not hold itself out as acting~~

independently unless it intends to:-

- (a) ~~provide that service wholly or predominantly based on the whole market in the relevant type of *home finance transaction*; and~~
- (b) ~~enable the *customer* to pay a *fee* for the provision of that service.~~ [deleted]

(2) ~~A *firm* which in accordance with (1) holds itself out as independent must ensure that the information or advice subsequently given to the *customer* concerned is information or *advice on home finance transactions* from the whole market in the relevant type of *home finance transaction*.~~ [deleted]

4.3.8 G (1) ~~*MCOB 4.3.7 R* stipulates what a *firm* must do if it is to hold itself out to any particular *customer* as acting independently. A *firm* which wishes to hold itself out generally as acting independently should ensure that doing so (for example through a trading name or advertising) is consistent with the kind of service which *customers* receive in relation to the relevant *home finance transactions*.~~ [deleted]

(2) ~~A *firm* that sells both *investments* and home finance products can offer from the whole market (or the whole market for a type of *home finance transaction*) and therefore be 'independent' for one but offer only a limited range for the other. If this is the case, the *firm* should explain the different nature of the services in a way that meets the requirement for clear, fair and not misleading communications in *MCOB 2.2.6* (Clear, fair and not misleading communications).~~ [deleted]

4.3.9 G ~~*MCOB 4.3.7R*(1)(b) means that a *firm* wishing to hold itself out as independent will need to give a *customer* a purely *fee* based option for paying its *fees*. However, the *firm* may in addition provide the *customer* with other payment options, such as a combination of *fees* and commission.~~ [deleted]

4.3.9A G (1) In order to satisfy the definition of an *independent service* a *firm* should ensure that it is not bound by any form of agreement with a *mortgage lender* that restricts the *personal recommendation* or personalised information the *firm* can provide or imposes any obligation that may limit the *firm's* ability to provide a *personal recommendation* or personalised information which is unbiased and unrestricted.

(2) A *firm* may be owned by, or own in whole or part, or be financed by or provide finance to, a *mortgage lender* without falling outside the 'unbiased and unrestricted' requirement in the definition of an *independent service* provided the *firm* ensures that ownership or finance does not prevent the *firm* from providing a *personal recommendation* or personalised information which is unbiased and

unrestricted.

Appointed representatives

- 4.3.10 R A *firm* may restrict the *home finance transactions* it authorises a particular *appointed representative* to sell. If it does so, the *firm* must ensure the *appointed representative* ~~must~~ reflects this restricted scope in any *initial disclosure document* or *combined initial disclosure document* provided disclosure given to the customer under MCOB 4.4.

#### 4.4 Initial disclosure requirements

Disclosure ~~where initial contact is not made by telephone~~ in all cases

- 4.4.1 R (1) A *firm* must ~~ensure that~~, on making contact with a *customer* when it ~~anticipates giving~~ expects to give a *personal recommendation* or personalised information or *advice* on a *regulated mortgage contract*, it provide the *customer* with the following information:
- (a) ~~establishes with the *customer* whether it will provide *advice* or information~~ an *independent service* or a *restricted service*. A *firm* must include the term "*independent service*" or "*restricted service*" or both, as relevant, in the disclosure;
  - (b) ~~establishes with the *customer* how much he will pay or, alternatively, the basis on which the *firm* will be remunerated, where appropriate; and~~
  - (c) ~~provides the *customer* with either:~~ whether the *firm* will provide a *personal recommendation* or personalised information.
    - (i) ~~an *initial disclosure document*; or~~
    - (ii) ~~if the *firm* has reasonable grounds to be satisfied that the services which it is likely to provide to the *customer* will relate to a combination of different types of *home finance transaction*, or will relate to *home finance transactions* and one or more of *non-investment insurance contracts* or *packaged products*, a *combined initial disclosure document* ;in a *durable medium*.~~
- (1A) If a *firm* expects to provide the *customer* with a *restricted service*, the initial disclosure information in (1) must also include:
- (a) an explanation about whether the service is limited to *regulated mortgage contracts* from a single *mortgage lender* or a limited number of *mortgage lenders*; and

- (b) (i) where the service is limited to a single *mortgage lender*, an explanation about whether it is limited to certain *regulated mortgage contracts* from that *mortgage lender*; or
- (ii) where the service is limited to a number of *mortgage lenders*, an explanation that the *customer* can request a copy of the list of *mortgage lenders* whose *regulated mortgage contracts* it offers and confirmation of whether the *firm* provides services in relation to all of the *regulated mortgage contracts* generally available from each *mortgage lender*.

(1B) If a *firm* expects to provide the *customer* with an *independent service*, the initial disclosure information in (1) must also include whether the *firm* will, as part of its services, consider *regulated mortgage contracts* that can only be obtained direct from a *mortgage lender* which is not the *firm*.

(1C) The information required by (1), (1A) and (1B) must be communicated clearly and prominently (whether or not combined with other information) during the course of the initial contact with the *customer* when the *firm* expects to give a *personal recommendation* or personalised information on a *regulated mortgage contract*; and in doing so:

- (a) if the initial contact includes spoken interaction, the information must be communicated orally;
- (b) if the initial contact is made by electronic means, the *firm* must ensure that the *customer* cannot progress onto the next stage of the sales process unless the information has been communicated to the *customer*; and
- (c) if the initial contact is in writing, the information must be communicated by a means that is not an *initial disclosure document* or *combined initial disclosure document*, nor a document in substantially similar form to an *initial disclosure document* or *combined initial disclosure document*.

If the initial contact falls within more than one of the situations in (a) to (c), a *firm* must observe each of the relevant provisions of (a) to (c).

(1D) The information required by (1), (1A) and (1B) must be provided in a *durable medium* (additionally to the disclosure required by (1C), where necessary). This must be done during the course of the initial contact with the *customer* when the *firm* expects to give a *personal recommendation* or personalised information on a *regulated mortgage contract*, unless it is not practicable to do so (for example, because that contact is by telephone). In that case, a *firm* must



provide the information in a *durable medium* within five *business days* of the initial contact, unless the *firm* has concluded that the *customer* is not eligible for any *regulated mortgage contracts* in relation to which it is able to offer a recommendation or information, or the *customer* has not provided his contact details.

- (2) The requirements in (1) ~~to (1D)~~ ~~(e)~~ do not apply where:
- (a) ~~an initial disclosure document~~ the initial disclosure information required by those paragraphs has already been provided by the *firm* and that ~~document information~~ is still likely to be accurate and appropriate for the *customer*; or
  - (b) ~~an initial disclosure document~~ the initial disclosure information required by those paragraphs has already been provided by the *firm* which first made contact with the *customer* in respect of the particular *regulated mortgage contract*, and the *firm* subsequently making contact with the *customer*: does not expect to alter or replace the type of service or basis of remuneration described in that information.
    - (i) ~~does not anticipate altering or replacing the service described in that document;~~ or
    - (ii) ~~is not making contact with a view to concluding a distance mortgage mediation contract;~~ or
  - (c) ~~initial contact is made by telephone.~~
- (3) ~~A *firm* may choose not to include the initial disclosure information required by sections 6, 7 and 8 of the *initial disclosure document*, and sections 5, 7 and 8 of the *combined initial disclosure document*, if it provides the *customer* with the information required by those sections in some other *durable medium* at the same time as the *initial disclosure document* or *combined initial disclosure document* (as the case may be) is provided before the *customer* makes an application for a *regulated mortgage contract*. [deleted]~~
- (4) A *firm* must not use a ~~combined initial disclosure document~~ the same document to give disclosures pursuant to MCOB 4.4 in relation to a combination of:
- (a) *regulated mortgage contracts* (other than *lifetime mortgages*) or *home purchase plans*; and
  - (b) *equity release transactions*.

4.4.1A R The information as to the basis of remuneration required by MCOB 4.4.1R(1)(b) must include all relevant information, including the following details:

- (1) any fees which the *firm* will charge to the *customer*;
  - (2) when any such fees will be payable and reimbursable; and
  - (3) whether the *firm* will receive commission from a third party.
- 4.4.2 G *MCOB* 4.4.1R(2)(b) means, for example, that a *mortgage lender* will provide the initial disclosure ~~document~~ information in a direct sale but not where the sale involves a *mortgage intermediary*. If a number of different *firms* are involved in relation to the transaction, having regard to *MCOB* 2.5.4R (2), those *firms* should take reasonable steps to establish that the *customer* has been provided with ~~an~~ the initial disclosure document information as required by *MCOB* 4.4.1R .
- 4.4.3 G (1) In many cases, *MCOB* 4.4.1 R(1) means that the initial disclosure ~~document~~ information will be ~~provided~~ given at the time of the first contact between the *firm* and the *customer*. However, there may be circumstances, for example in relation to a loan for a business purpose, where the possibility of the *customer* entering into, or varying the terms of, a *regulated mortgage contract* is only identified after preliminary discussions. Disclosure, in the context of *MCOB* 4, is only required once this possibility is identified.
- (2) In the *FSA's* opinion, the requirements at *MCOB* 4.4.1R ~~and~~ *MCOB* 4.4.7R would not apply when a *customer* contacts a *firm* simply to arrange to receive personalised information or *advice* on a *regulated mortgage contract* at a later time, such as when a *customer* books an appointment. In such cases, initial disclosure should be made when the *firm* first makes contact with the *customer* with a view to actually giving the information or *advice*. However, *firms* should note the additional disclosure requirements in *MCOB* 4.5 (Additional disclosure for distance mortgage mediation contracts with retail customers), and, the need to ensure that the required information (to be provided with the initial disclosure ~~document~~) is provided in good time (see *MCOB* 4.5.3G(1)).
- (3) *Firms* which state that they provide a service based on a limited number of mortgage lenders (see *MCOB* 4.4.1R (1A) (b) (i)) are reminded that, in the light of the rules and guidance in SYSC, they should have adequate systems and controls in place to monitor whether business is actually placed with those mortgage lenders.
- 4.4.4 GR If a *firm* has ~~provided~~ given a *customer* ~~with an~~ appropriate initial disclosure ~~document~~ but subsequently discovers that the *customer* wants different services, or services which will be remunerated on a different basis, from those originally ~~anticipated~~ expected and described in ~~the document that disclosure,~~ the *firm* must inform the *customer* of the changes to the information given will need to establish the details of the new service to be provided to the *customer* and provide the *customer* with a new initial disclosure document in accordance with *MCOB* 4.4.1R ~~or~~ *MCOB* 4.4.7R, both clearly and prominently and (additionally where necessary) in a durable medium.

Additional disclosure where initial contact is by telephone

- 4.4.4A R If the initial contact of a kind in MCOB 4.4.1R(1) is by telephone, then the firm must also, before proceeding further, give the name of the firm and (if the call is initiated by or on behalf of the firm) the commercial purpose of the call.

Additional disclosure requirements where the services are to be provided to a consumer under a distance contract

- 4.4.4B R Where the services in MCOB 4.4.1R(1) are to be provided by way of a distance contract, the firm must provide a consumer with the following information in a durable medium in good time before the distance contract has been agreed:

- (1) the name and the main business of the firm, the geographical address at which it is established and any other geographical address relevant for the consumer's relations with the firm;
- (2) an appropriate statutory status disclosure statement (GEN 4), a statement that the firm is on the FSA Register and its FSA registration number;
- (3) the total price to be paid by the consumer to the firm for the financial service, including all related fees, charges and expenses, and all taxes paid through the firm or, when an exact price cannot be indicated, the basis for the calculation of the price enabling the consumer to verify it;
- (4) the arrangements for payment and for performance;
- (5) how to complain to the firm, whether complaints may subsequently be referred to the Financial Ombudsman Service and, if so, the methods for having access to it, together with equivalent information about any other applicable named complaints scheme;
- (6) whether compensation may be available from the compensation scheme, or any other named compensation scheme, if the firm is unable to meet its liabilities, and information about any other applicable named compensation scheme; and
- (7) any other contractual terms and conditions of the distance contract.

- 4.4.4C G (1) If used in accordance with its notes and provided to the customer at the correct time, using an initial disclosure document (see MCOB 4 Annex 1G) or combined initial disclosure document in a durable medium satisfies the initial disclosure requirements of MCOB 4.4.1R(1D) and may satisfy the further requirements for disclosure for distance contracts with a consumer in MCOB 4.4.4BR, though firms should consider whether the initial disclosure document or combined initial disclosure document contains all the contractual terms and conditions of the distance contract.
- (2) The FSA does not regard the use of an initial disclosure document or

combined initial disclosure document (or any document in substantially similar form) alone as satisfying the requirement in MCOB 4.4.1R (1C) or MCOB 4.4.4R for a clear and prominent disclosure.

- (3) Where a firm chooses not to use an initial disclosure document or combined initial disclosure document and there is no spoken interaction during the initial contact, it may be able to make a single disclosure in a durable medium at that stage which will satisfy the requirements of both MCOB 4.4.1 R(1C) and (1D).
- (4) MCOB 4.4.4BR contains the additional disclosure requirements for firms providing mortgage mediation activities by way of a distance contract in the circumstances contemplated by MCOB 4.4.1R. MCOB 4.5 and MCOB 4.6 contain further rules and guidance applicable where firms enter into a distance contract in respect of their home finance mediation activities independent of any contractual arrangement with a consumer relating to a particular home finance transaction or transactions.

#### Uncertainty whether a mortgage is regulated

- 4.4.5 R (1) If at the point that initial disclosure must be made in accordance with MCOB 4.4.1R or ~~MCOB 4.4.7R~~ MCOB 4.4.4AR a firm is uncertain whether the contract will be a *regulated mortgage contract*, the firm must:
- (a) ~~provide~~ make the initial disclosure ~~document~~; or
  - (b) seek to obtain from the *customer* information that will enable the firm to ascertain whether the contract will be a *regulated mortgage contract*.
- (2) Where (1)(b) applies, the initial disclosure ~~document~~ must be ~~provided~~ made unless, on the basis of the information provided by the *customer*, the firm has reasonable evidence that the contract is not a *regulated mortgage contract*.

#### Information to be provided to customers on request

- 4.4.6 R (1) If a *firm's* scope of service is based on ~~MCOB 4.3.1R(1)(b)~~ firm provides a restricted service it must maintain, and keep up to date, in a *durable medium* and in a form which is appropriate for distribution to the *customer*, a list of the *mortgage lenders* whose *regulated mortgage contracts* it offers. This list must also confirm whether or not the firm provides services in relation to all of the *regulated mortgage contracts* generally available from each *mortgage lender*.
- (2) The *customer* must be provided with a copy of the information described in (1) ~~on~~ in a durable medium as soon as possible following the customer's request and in any event no later than five business days thereafter.

...

#### Disclosure where initial contact is by telephone

- 4.4.7 R (1) If the initial contact of a kind in *MCOB 4.4.1R(1)* is by telephone, then unless *MCOB 4.4.1R(2)(a)* applies, the following information must be given before proceeding further:-
- (a) the name of the *firm* and (if the call is initiated by or on behalf of the *firm*) the commercial purpose of the call;
  - (b) the scope of the service provided by the *firm* (within the meaning of *MCOB 4.3.1R*);
  - (c) if the scope of the service is based on *MCOB 4.3.1R(1)(b)*, that the *customer* can request a copy of the list of *mortgage lenders* whose *regulated mortgage contracts* it offers and confirmation of whether the *firm* provides services in relation to all of the *regulated mortgage contracts* generally available from each *mortgage lender*;
  - (d) whether or not the *firm* will provide the *customer* with advice on those *regulated mortgage contracts* within its scope; and
  - (e) that the information given under (a) to (d) will be confirmed in writing. [deleted]
- (2) Provided that the telephone call in (1) has not led the *firm* to conclude that the *customer* is ineligible for any of its *regulated mortgage contracts*, and that the *customer* has provided his contact details, the *firm* must send the *customer* a copy of an *initial disclosure document* or *combined initial disclosure document* and any other information required to be provided, in a *durable medium* within five *business days* of the telephone call (see also *MCOB 4.5.2 R(2)(b)* for the equivalent requirement in relation to *distance mortgage mediation contracts*). [deleted]
- (3) If the *customer* accepts the offer in (1) (c) of a list of the *mortgage lenders* whose *regulated mortgage contracts* the *firm* offers, that list must also be sent with the information required in (2). [deleted]

...

#### Record keeping

- 4.4.9 G *Firms* are reminded of the general record-keeping requirements in SYSC 9. A *firm* should keep appropriate records of the disclosures required by this section.

The existing section 4.7 is deleted in its entirety and replaced with the following. The existing text is not struck through and the new text is not underlined.

#### **4.7 Sales standards**

Giving a personal recommendation or personalised information

- 4.7.1 R When giving a *personal recommendation* or personalised information in relation to a *regulated mortgage contract*, a *firm* must act honestly, fairly and professionally in accordance with the best interests of its *customer*.
- 4.7.2 R (1) Except as provided in (3), a *firm* must take reasonable steps to ensure that it does not give a *personal recommendation* or personalised information to a *customer* about, a *regulated mortgage contract* or the variation of an existing *regulated mortgage contract*, unless:
- (a) the *customer* meets the lender's eligibility criteria in relation to affordability for the *regulated mortgage contract*; and
  - (b) the *regulated mortgage contract* is appropriate to the needs and circumstances of the *customer*;
- or these conditions will be satisfied after the variation.
- (2) Where the *firm* identifies that there is no *regulated mortgage contract* to which it has access which meets the requirements of (1), it must not make any *personal recommendation* or give any personalised information.
- (3) A *firm* may provide a quick quote for a *regulated mortgage contract* in the course of the activities in (1) provided that, if the *customer* wishes to proceed beyond that initial quote, the *firm* carries out the assessment in (1) before proceeding beyond that stage.
- 4.7.3 G *MCOB 4.7.2R(2)* has the effect that a *firm* cannot recommend the 'least worst' *regulated mortgage contract* where the *firm* does not have access to products appropriate to the *customer's* needs and circumstances. For example, a *firm* dealing solely in the sub-prime market should not recommend or arrange one of these *regulated mortgage contracts* if approached by a *customer* with an unblemished credit record.
- 4.7.4 R In *MCOB 4.7*, recommending or giving personalised information on a *regulated mortgage contract* includes recommending or giving personalised information on the variation of an existing *regulated mortgage contract*.
- 4.7.5 G For the purposes of *MCOB 4.7.2R*, a *firm* may be either *advising on regulated mortgage contracts* or *arranging (bringing about) regulated*

*mortgage contracts. Firms may wish to refer to the guidance at PERG 4.6 for assistance in ascertaining which of these activities they are carrying on.*

#### Affordability criteria

- 4.7.6 R For the purposes of complying with *MCOB 4.7.2R(1)(a)*, a *firm* must give due regard to the following:
- (1) the *customer's* income, personal expenditure, credit commitments and any other resources that the *customer* has available;
  - (2) any known or reasonably foreseeable future change to the *customer's* income, personal expenditure, credit commitments and other resources;
  - (3) the costs that the *customer* will be required to meet once any discount period in relation to the *regulated mortgage contract* comes to an end; and
  - (4) any reasonably foreseeable interest rate changes.
- 4.7.7 R In relation to *MCOB 4.7.2R(1)(a)*, a *firm* must explain to the *customer* that the assessment of whether he meets the lender's eligibility criteria for the *regulated mortgage contract* is based on the *customer's* current circumstances, and that these might change in the future.

#### The customer's needs and circumstances

- 4.7.8 R For the purposes of complying with *MCOB 4.7.2R(1)(b)*, a *firm* must give due regard to the following non-exhaustive list of factors:
- (1) whether the *customer's* requirements appear to be within the *mortgage lender's* expected eligibility criteria for the *regulated mortgage contract*;
  - (2) whether the *customer* should have an *interest-only mortgage*, a *repayment mortgage*, or a combination of the two;
  - (3) whether the *customer* has a preference for a particular term;
  - (4) whether the *customer* has a preference or need for stability in the amount of required payments, especially having regard to the potential impact on the *customer* of significant interest rate changes in the future;
  - (5) whether the *customer* has a preference or need for payments to be reduced at the outset (for example, a loan with an initial discount rate period);
  - (6) whether the *customer* intends to make early repayments;

- (7) whether the *customer* has a preference or need for any other features of a *regulated mortgage contract*;
  - (8) where the term of the *regulated mortgage contract* will extend into the *customer's* retirement, whether the *regulated mortgage contract* remains appropriate;
  - (9) where the *customer* is looking to increase the borrowing secured on the property which is the subject of an existing *regulated mortgage contract*, whether it may be more appropriate for the *customer* to take a further advance with the existing lender rather than entering into a *regulated mortgage contract* with another lender; and
  - (10) whether it is more appropriate for the *customer* to pay any fees or charges in relation to the *regulated mortgage contract* up front, rather than rolling them into the loan (see also *MCOB 5.5.19R*).
- 4.7.9 G (1) Examples of criteria in *MCOB 4.7.8 R (1)* are: the amount that the *mortgage lender* permits a *customer* to borrow; and whether the *mortgage lender* will lend in respect of properties of a non-standard construction.
- (2) An example of another feature in *MCOB 4.7.8R (7)* is a payment holiday.
- 4.7.10 R Where a *firm* makes a *personal recommendation*, or provides personalised information, in relation to a *regulated mortgage contract* for a *customer* where a main purpose is to consolidate existing debts it must also take account of the following, where relevant, in assessing whether the *regulated mortgage contract* meets the conditions set out in *MCOB 4.7.2R(1)*:
- (1) the costs associated with increasing the period over which a debt is to be repaid;
  - (2) whether it is appropriate for the *customer* to secure a previously unsecured loan; and
  - (3) where the *customer* is known to have payment difficulties, whether it would be more appropriate for the *customer* to negotiate an arrangement with his creditors than to take out or vary a *regulated mortgage contract*.
- 4.7.11 G (1) A *firm* should obtain sufficient information from a *customer* to enable it to comply with *MCOB 4.7.2R*.
- (2) A *firm* may generally rely on any information provided by the *customer* for the purposes of *MCOB 4.7.2R* unless, taking a common-sense view of this information, it has reason to doubt it.
- 4.7.12 G In complying with *MCOB 4.7.2R* a *firm* is not required to consider



whether it would be preferable for the *customer* to:

- (1) purchase a property by using his own resources, rather than by borrowing under a *regulated mortgage contract*; or
- (2) rent a property, rather than purchase one; or
- (3) delay entering into a *regulated mortgage contract* until a later date (on the grounds that property prices would have fallen in the intervening period, or that the interest rate in relation to the *regulated mortgage contract* would be lower, or both).

- 4.7.13 G *MCOB 4.7.8 R(2)* does not require a *firm* to provide *advice on investments*. Whether such *advice* should be given will depend upon the individual needs and circumstances of the *customer*. Where considered relevant, *MCOB 4* does not restrict the ability of an adviser to refer the *customer* to another source of *investment advice* (for example, where the adviser is not qualified to provide *advice on investments*).

Customers in arrears or with a payment shortfall

- 4.7.14 R If a *firm* is dealing with an existing *customer* in arrears or with a payment shortfall and has concluded that there is no *regulated mortgage contract* which satisfies the requirements of *MCOB 4.7.2R*, the *firm* must nonetheless have regard to *MCOB 13.3.2AR(1)*, *MCOB 13.3.2AR(5)* and *MCOB 13.3.2AR(6)* (see also *MCOB 13.3.4AR(1)(a)* and *MCOB 13.3.4AR(1)(b)*).
- 4.7.15 G *MCOB 4.7.14 R* explains that different considerations apply when dealing with a *customer* in arrears. For example, the circumstances of the *customer* may mean that, viewed as a new transaction, a *firm* could not give the *customer* a *personal recommendation* of, or personalised information in relation to, a *regulated mortgage contract* in compliance with *MCOB 4.7.2R*. In such cases, a *firm* may still be able to make a *personal recommendation* of, or give personalised information in relation to, a *regulated mortgage contract* for that *customer*, subject to the rules in *MCOB 13* and *Principle 6*.

Giving advice

- 4.7.16 G (1) *MCOB 4.7* imposes standards for all sales of *regulated mortgage contracts*, whether advised or non-advised. *Firms* which are *advising on regulated mortgage contracts* should also have due regard to their legal obligations under the general law and the terms of their contract with the *customer*.
- (2) *Principle 9* requires a *firm* to take reasonable care to ensure the suitability of its advice. In accordance with that *Principle*, where a *firm* is *advising on regulated mortgage contracts*, it should take reasonable steps to obtain from a *customer* all further information likely to be relevant for the purposes of its advice.

## Rejected recommendations

- 4.7.17 R If a *customer* has:
- (1) rejected all of the *personal recommendations* made by a *firm* to the *customer* of *regulated mortgage contracts* which the *firm* considers meet the requirements of *MCOB 4.7.2R(1)* and requested personalised information instead on one or more *regulated mortgage contracts*; and
  - (2) been given new initial disclosure in accordance with *MCOB 4.4.1R* and, if applicable, *MCOB 4.4.4BR*;
- a *firm* may provide personalised information on those *regulated mortgage contracts* provided that they meet the requirements of *MCOB 4.7.2R(1)*.

## Record keeping

- 4.7.18 R (1) A *firm* must make and retain a record of :
- (a) the *customer* information, including that relating to the *customer's* needs and circumstances and the *customer's* satisfaction of the lender's eligibility criteria in relation to affordability, that it has obtained for the purposes of *MCOB 4.7*;
  - (b) each *regulated mortgage contract* in relation to which the *firm* has made a *personal recommendation* or given personalised information to the *customer*, that explains why the *firm* has concluded that each of them satisfies *MCOB 4.7.2R(1)*; and
  - (c) any cases where the *firm* has given personalised information to the *customer* under *MCOB 4.7.17R* including the reasons why the *regulated mortgage contracts* which were the subject of the initial *personal recommendation* were rejected by the *customer* and, where applicable, details of the *regulated mortgage contract* the *customer* has proceeded with.
- (2) The records in (1) must be retained for a minimum of three years from the date on which the *personal recommendation* or personalised information was given.

The existing section 4.8 is deleted in its entirety. The existing text is not shown struck through.

## 4.8 Non-advised sales [deleted]

# Annex 1RG: Initial disclosure document

This Annex belongs to *MCOB 4.4.4CG(1) 4R(4)* and *MCOB 4.10.2R*.

...

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**1.** Whose [mortgages/Islamic home purchase plans] do we offer? [Note 6] [Note 7]

---

Independent - We offer [mortgages/Islamic home purchase plans] ~~from the whole market~~ based on a comprehensive and fair analysis of the market.

We will [not] include in our search mortgages that can only be obtained directly from [a/another] lender. [Note 8] [Note 9]

Restricted - We [can] [Note 8] only offer [mortgages/Islamic home purchase plans] from one or a limited number of [lenders/providers]. [Note 10]

Ask us for a list of [lenders/providers] we offer [mortgage/Islamic home purchase plans] from and any restrictions on the range available. [Note 911]

We [can] [Note 8] only offer [a limited range of the] [a] [mortgage[s]/Islamic home purchase plan[s]] from [a single lender/provider] [name of single lender/provider]. [Note 10]

[or]  
We only offer our own [mortgages/Islamic home purchase plans]. [Note 11]

...

**Note 8** - This sentence is required only where a firm selects this service option and its service includes *regulated mortgage contracts*

**Note 9** - Insert "not" if the firm does not consider in its search *regulated mortgage contracts* that the consumer can not obtain through the *firm* and only by going directly to a lender. If the *firm* is not a lender itself, use "a" and if the firm is a lender, use "another".

**Note 10** - if the *firm* selects this box, it will be offering:

- (a) products from a limited number of lenders/providers; or
- (b) products of a single lender/provider; or
- (c) its own products (e.g. where the *firm* is a *lender* offering only its own products, or is part of a *lender* offering only the products sold under that part's trading name).

The *firm* should replace the preceding text with the relevant text as set out below. If the *firm* does not select this box, then no amendments should be made to the preceding text.

(a)	We [can] [note a] only offer [mortgage[s]/Islamic home purchase plan[s]] from a limited number of [lenders/providers]
(b)	We [can] [note a] only offer [mortgage[s]/Islamic home purchase plan[s]] from [name of lender/provider] [note b]
(c)	We [can] [note a] only offer [a limited range of the] [a] [mortgage[s]/Islamic home purchase plan[s]] from a single

	lender/provider [name of lender/provider] <b>[note c]</b>
(d)	We only offer our own [mortgages/Islamic home purchase plans].

[Note a] - insert "can" if the *firm's* range of *regulated mortgage contracts or home purchase plans* is determined by any contractual obligation

[Note b] – The *firm* can use this option instead of (a) if it prefers to list all of the lenders or providers it offers *mortgages or home purchase plans* from, so long as the *firm* offers all of the *mortgages or home purchase plans* generally available from each lender or provider.

[Note c] - if the *firm* selects this text, it must insert the name of the lender or provider. If the *firm* does not offer all of the *mortgages or home purchase plans* generally available from that lender or provider, it must insert the words "a limited range of the", as shown. If the lender or provider only has one relevant product, the *firm* should amend the text to "We can only offer a [mortgage/home purchase plan] from [name of single lender/provider]."

**Note 11** - this sentence is required only where a firm selects this service option and describes its scope using the text option (a) in Note 10.

**Note 8**— insert "can" if the *firm's* range of *regulated mortgage contracts or home purchase plans* is determined by any contractual obligation.

**Note 9**— this sentence is required only where a firm selects this service option. It may also be omitted if a *firm* chooses to list all of the lenders or providers it offers *home finance transactions* from instead of the text "a limited number of [lenders/providers]", in the previous line, so long as the *firm* offers all of the *mortgages or home purchase plans* generally available from each lender or provider.

**Note 10**— if the *firm* selects this box, it must insert the name of the lender or provider. If the *firm* does not select this box, it must insert the words "a single lender/provider" instead. If the *firm* does not offer all of the *mortgages or home purchase plans* generally available from that lender or provider, it must insert the words "a limited range of", as shown. If the lender or provider only has one relevant product, the *firm* should amend the text to "We can only offer a [mortgage/home purchase plan] from [name of single lender/provider]."

**Note 11**— if the *firm* is a provider or lender offering only its own *home finance transactions*, or is part of a provider or lender offering only the *home finance transactions* sold under that part's trading name, it may use this alternative text.

...

## 5.4 **Mortgage illustrations: Information on regulated mortgage contracts: general**

...

### ~~Restriction on provision~~ Provision of information

5.4.13 R ~~A firm must not provide a customer with information that is specific to the amount that the customer wants to borrow on a particular regulated mortgage contract except in the following circumstances:~~

- ~~(1) when it is in the form of an illustration;~~
- ~~(2) when it is provided on screen, for example a computer screen;~~
- ~~(3) when supplementary information which is not contained within an illustration is provided after or at the same time as an illustration; or~~
- ~~(4) when it is provided orally, for example by telephone. [deleted]~~

5.4.13A G When providing information on regulated mortgage contracts, firms should bear in mind that:

- (1) the information must be clear, fair and not misleading in accordance with Principle 6 and MCOB 2.2.6R; and
- (2) where a selection of products is presented to the customer, this must be done in accordance with MCOB 4.7.1 R. For example, only presenting a small proportion of all products available on the basis that these products pay the highest commission, rather than on the basis that they best meet the customer's needs and circumstances, would not be consistent with that rule.

5.4.14 R ~~Where MCOB 5.4.13R(2) applies:-~~

- ~~(1) if the customer initiates the accessing of quotation information on screen (for example, by using the internet or interactive television), the following warning must be displayed prominently on each page on screen: 'This information does not contain all of the details you need to choose a mortgage. Make sure that you read the separate key facts illustration before you make a decision.'; and~~
- ~~(2) a firm must not provide a customised print function where the information on the screen would not be in the form of an illustration if the information were printed in hard copy. [deleted]~~

5.4.15 R ~~Where MCOB 5.4.13R(3) applies, supplementary information must only be provided when it does not significantly duplicate information provided in the illustration. [deleted]~~

5.4.16 G ~~MCOB 5.4.13 R 5~~ places no restrictions on the provision of information that is not specific to the amount the customer wants to borrow, for example, marketing

literature including generic mortgage repayment tables or graphs illustrating the benefits of making a regular overpayment on a flexible mortgage. Such literature may, however, constitute a *financial promotion* and be subject to the provisions of *MCOB 3* (Financial promotion).

- 5.4.17 G ~~Where *MCOB 5.4.13R(2)* and *MCOB 5.4.13R(4)* apply, *firms* should encourage the *customer* to obtain a copy of an *illustration* in a *durable medium*. This could be done, for example, if the information was contained on the *firm's* website, by a prompt which asked the *customer* whether he wished to print off an *illustration*. [deleted]~~
- 5.4.18 R (1) ~~Unless (2) applies, where *MCOB 5.4.13 R(2)* or *MCOB 5.4.13 R(4)* apply, a *firm* must provide the means for the *customer* to obtain an *illustration* as soon as practicable, through a delivery channel acceptable to the *customer*. [deleted]~~
- (2) ~~A *firm* does not need to provide an *illustration* if the *customer* refuses to disclose key information (for example, in a telephone conversation, his name or a communication address) or where the provision of an *illustration* is not appropriate, for example, because on the basis of discussions undertaken the *customer* is ineligible given the *mortgage lender's* lending criteria, or is not interested in pursuing the enquiry. [deleted]~~

Messages to be given when providing information on regulated mortgage contracts

- 5.4.18A R Whenever a *firm* provides a *customer* with information specific to the amount that the *customer* wants to borrow on a particular *regulated mortgage contract* following an assessment of the *customer's* needs and circumstances in order to comply with *MCOB 4.7.2 R (1) (b)*, it must give, clearly and prominently, the following information, unless the *firm* has previously given that information in compliance with this *rule* within the last ten *business days*:
- (1) the same information as is required by *MCOB 4.4.1R(1)(a)*, (1A) and (1B); and
- (2) that the *customer* has the right to request an *illustration* for any *regulated mortgage contract* in relation to which the *firm* is able to give a *personal recommendation* or personalised information to the *customer* in compliance with *MCOB 4.7.2R(1)*.
- 5.4.18B G In the *FSA's* view, the reference in the template *illustration* at *MCOB 5 Annex 1R* to the possibility of obtaining other *illustrations* is not sufficient to comply with the obligation in *MCOB 5.4.18AR(2)*. A *firm* might, however, satisfy *MCOB 5.5.18AR(2)* in a number of ways; for example, by drawing the *customer's* attention to the right to request an *illustration* orally in a face-to-face meeting, or by referring to it in a letter or electronic communication or other written information.

...

## 5.5 Provision of illustrations

### Timing

- 5.5.1 R (1) A *firm* must provide the *customer* with an *illustration* for a *regulated mortgage contract* before the *customer* submits an application for that particular *regulated mortgage contract* to a *mortgage lender*, unless an *illustration* for that particular *regulated mortgage contract* has already been provided.
- (2) Except in the circumstances in MCOB 5.5.1AR, a *firm* must provide the *customer* with an *illustration* for a *regulated mortgage contract* when any of the following occurs, unless an *illustration* for that *regulated mortgage contract* has already been provided:
- (a) the *firm* makes a *personal recommendation* to the *customer* to enter into one or more *regulated mortgage contracts*, in which case an *illustration* must be provided at the point the recommendation is made (and *illustrations* for all recommended *regulated mortgage contracts* must be provided), unless the *personal recommendation* is made by telephone, in which case the *firm* must provide an *illustration* within 5 *business days*;
  - (b) ~~the *firm* provides written information that is specific to the amount that the *customer* wants to borrow on a particular *regulated mortgage contract*; or [deleted]~~
  - (c) ~~the *customer* requests written information from the *firm* that is specific to the amount that the *customer* wants to borrow on a particular *regulated mortgage contract*, unless the *firm* does not wish to do business with the *customer*. [deleted]~~
  - (d) the *customer* requests an *illustration* in relation to any *regulated mortgage contract* in relation to which the *firm* is able to give a *personal recommendation* or personalised information to the *customer* in compliance with MCOB 4.7.2R(1); or
  - (e) the *customer* has indicated an intention to proceed with a particular *regulated mortgage contract*.
- (3) Subject to MCOB 5.5.4R, the *firm* may comply with (1) and (2) by providing an *offer document* containing an *illustration*, if this can be done as quickly as providing an *illustration*.

### 5.5.1A R A *firm* need not provide an *illustration*:

- (1) in relation to a *regulated mortgage contract* that can only be obtained direct from a *mortgage lender* which is not the *firm*; or
- (2) if the *customer* refuses to disclose key information (for example, in a telephone conversation, his name or a communication address) or where the

customer is not interested in pursuing the enquiry.

- 5.5.1B R If the firm chooses not to give an illustration in the circumstances set out in MCOB 5.5.1A R(1), where it has given a personal recommendation of a regulated mortgage contract that can only be obtained direct from a mortgage lender which is not the firm, the firm must give the customer a written record of its having done so.
- 5.5.1C G In the circumstances in MCOB 5.5.1AR(2), the rule in MCOB 5.5.1R(1) will mean that the customer may not make an application for a regulated mortgage contract as an illustration has not been provided.
- 5.5.1.D R (1) Where a firm has raised, or is otherwise considering, with a customer, the possibility that a fee or charge of any kind (receivable either by the firm or another party) is to be added to the sum advanced under the regulated mortgage contract rather than paid or discharged (and not borrowed by the customer), the firm must, whenever it is obliged under MCOB 5.5 to provide the customer with an illustration, provide the customer instead with two illustrations: one showing the effect of the fee or charge being so added, and one showing the effect of that not being done.
- (2) In the circumstances set out in (1), any reference in MCOB to an illustration includes two illustrations as set out in (1).
- 5.5.2 G The effect of the requirements at MCOB 5.3.1R and MCOB 5.5.1R(1) is that if a customer's application to enter into a regulated mortgage contract with a mortgage lender, made via a mortgage intermediary, is subsequently passed by that mortgage intermediary to another mortgage lender, then the mortgage intermediary must ensure that the application is amended and the customer is provided with an illustration for the other mortgage lender's regulated mortgage contract before the application is passed to the other mortgage lender.
- 5.5.3 G If a firm chooses to issue an offer document in place of an illustration in accordance with MCOB 5.5.1R(3), it will need to comply with MCOB 6.4 (Content of the offer document), and in particular with MCOB 6.6 (Offer documents in place of illustrations).
- 5.5.4 R A firm must not ~~accept fees, commission or a valuation, or~~ undertake any action that commits the customer to an application (including accepting fees in relation to the regulated mortgage contract concerned) until the customer has had the opportunity to consider an illustration.
- ...
- 5.5.6 G ~~Subject to MCOB 5.5.1R and MCOB 5.5.15R when an illustration is requested without delay, a firm may perform an internal credit score and obtain information on the customer's credit record from a credit reference agency (subject to the consent of the customer), in order to provide a customer with an approval in principle for a regulated mortgage contract, without having to provide an illustration. [deleted]~~



...

Providing an illustration without delay in response to a customer request

5.5.14 G Where the *customer* requests ~~written information from the *firm* that is specific to the amount that the *customer* wants to borrow on~~ an illustration for a particular regulated mortgage contract ~~under~~ (see MCOB 5.5.1R(2)(~~e~~)(d)), the purpose of MCOB 5.5.15R , MCOB 5.5.16R and MCOB 5.5.17G is to ensure that the *customer* receives an *illustration* without unnecessary delay. These requirements do not restrict the information that the *firm* may obtain from the *customer* after it has provided the *customer* with an *illustration*.

5.5.15 R In meeting a request for an illustration ~~under~~ in accordance with MCOB 5.5.1R(2)(~~e~~)(d), the *firm* must not delay the provision of the *illustration* by requesting information other than:

...

Positive choice to roll up fees or charges into loan

5.5.19 R (1) A mortgage lender must not enter into a regulated mortgage contract, or agree to do so, with a customer on the basis that a fee or charge of any kind (receivable either by the firm or another party) is to be added to the sum advanced under the regulated mortgage contract unless the customer has made a positive choice to do so. Such choice may not be made before the customer has received the two illustrations required by MCOB 5.5.1DR(1).

(2) A mortgage lender must retain a record of the customer's choice in (1) for a period of three years following the making of the choice.

...

**Schedule 1 Record keeping requirements**

Sch 1.3G

Handbook reference	Subject of record	Contents of record	When record must be made	Retention period
...				
MCOB 4.7.17R(1)(a)	Suitability	Details of the customer information obtained, including the customer's needs and circumstances, for the purpose of assessing the suitability of a regulated mortgage	When the personal recommendation is made	Three years

		<i>contract</i>		
<i>MCOB</i> 4.7.17R(1)(b)	Suitability	An explanation of why the <i>firm</i> believes the <i>personal recommendation</i> complies with the suitability requirements in <i>MCOB</i> 4.7.17R(1)	When the <i>personal recommendation</i> is made	Three years
<i>MCOB</i> 4.7.17R(1)(e)	Suitability	An explanation of the reason why a <i>personal recommendation</i> has been made on a basis other than that described in <i>MCOB</i> 4.7.13E(1)	When the <i>personal recommendation</i> is made	Three years
<i>MCOB</i> 4.7.18R(1)(a)	<u>Customer information</u>	<u>Information obtained for the purposes of <i>MCOB</i> 4.7</u>	<u>When the information is obtained</u>	<u>Three years from when the <i>personal recommendation</i> or personalised information was given</u>
<i>MCOB</i> 4.7.18R(1)(b)	<u><i>Personal recommendations</i> or personalised information</u>	A record in relation to each <u><i>regulated mortgage contract</i></u> for which a <u><i>personal recommendation</i></u> or <u>personalised information</u> has been given explaining why it satisfies <i>MCOB</i> 4.7.2R(1)	When the <u><i>personal recommendation</i></u> or <u>personalised information</u> is given	<u>Three years from when the <i>personal recommendation</i> or personalised information was given</u>
<i>MCOB</i> 4.7.18R(1)(c)	<u>Personalised information given under <i>MCOB</i> 4.7.17R</u>	A record of each case including the reasons why the <u>initial <i>personal recommendation</i> was rejected</u>	When the <u>personalised information</u> is given	<u>Three years from when the <i>personal recommendation</i> or personalised information was given</u>
...				
<i>MCOB</i> 4.8.7R	Scripted questions	A record of the scripted questions used in non-advised sales	The date on which the scripted questions are first used	One year from the date on which the scripted questions are superseded by a more up-to-date record
...				

<u>MCOB 5.5.19 R (2)</u>	<u>Rolling-up of fees or charges into the loan under a <i>regulated mortgage contract</i></u>	<u>The <i>customer's</i> choice to do so</u>	<u>When the choice is made</u>	<u>Three years from the making of the choice</u>
...				

## Annex D

### Amendments to the Training and Competence sourcebook (TC)

In this Annex, underlining indicates new text.

#### TC Appendix 1

#### App 1.1 Activities and Products/Sectors to which TC applies subject to TC Appendices 2 and 3

##### App R 1.1.1

Activity	Products/Sectors	Is there an appropriate examination requirement?
...		
<i>Regulated mortgage activity and reversion activity carried on for a customer</i>		
Advising; <u>arranging (bringing about); or designing structured questions for non-advised sales</u>	20	<i>Regulated mortgage contracts for a non-business purpose</i>
		Yes

...

	TC Appendix 4R
...	
Table 18	Advising a customer on, <u>arranging (bringing about) or designing structured questions for non-advised sales of,</u> a regulated mortgage contract for a non-business purpose

<b>TP 8</b>	<b>Transitional provisions relating to time limits for attaining qualifications</b>
...	

8.3	R	An <i>employee</i> who is carrying on the activities specified in <u>TC Appendix 1</u> of:
		(1) <u>arranging (bringing about) regulated mortgage contracts for a non-business purpose; or</u>
		(2) <u>designing structured questions for non-advised sales of regulated mortgage contracts for a non-business purpose</u>
		as at [ <i>insert date final rules come into force</i> ] will, for the purposes of <u>TC 2.2A .1R</u> , be regarded as carrying on such activities only with effect from that date.

## Annex E

### Amendments to the Perimeter Guidance manual (PERG)

In this Annex, underlining indicates new text and striking through indicates deleted text.

...

Advice must relate to a particular regulated mortgage product

...

- 4.6.9 G In the *FSA's* view, guiding a *person* through ~~scripted questions~~ or a decision tree should not, of itself, involve advice within the meaning of article 53A (it should be generic advice)...this is considered in more detail, in the context of ~~scripted~~ structured questioning, in *PERG* 4.6.22G (~~Scripted~~ Structured questioning (including decision trees)).

...

- 4.6.15 G Information relating to entering into *regulated mortgage contracts* may often involve one or more of the following:

...

- (3) the production of ~~scripted~~ structured questions for the borrower to use in order to exclude options that would fail to meet his requirements; such questions may often go on to identify a range of *regulated mortgage contracts* with characteristics that appear to meet the borrower's requirements and to which he might wish to give detailed consideration (~~scripted~~ structured questioning is considered in more detail in *PERG* 4.6.21G to *PERG* 4.6.25G (~~Scripted~~ Structured questioning (including decision trees)));

...

...

~~Scripted~~ Structured questioning (including decision trees)

- 4.6.21 G ~~Scripted~~ Structured questioning involves using any form of sequenced questions in order to extract information from a *person* with a view to facilitating the selection by that *person* of a mortgage or other product that meets his needs. A decision tree is an example of ~~scripted~~ structured questioning. The process of going through the questions will usually narrow down the range of options that are available. ~~Scripted~~ Structured questions must be prepared in advance of their actual use.

- 4.6.22 G Undertaking the process of ~~scripted~~ structured questioning gives rise to

particular issues concerning advice. These mainly involve two aspects of this *regulated activity*. These are that advice must relate to a particular *regulated mortgage contract* (see *PERG 4.6.5 G*) and the distinction between information and advice (see *PERG 4.6.13 G*). Whether or not ~~scripted~~ structured questioning in any particular case is *advising on regulated mortgage contracts* will depend on all the circumstances. If the process involves identifying one or more particular *regulated mortgage contracts* then, in the *FSA's* view, to avoid *advising on regulated mortgage contracts*, the critical factor is likely to be whether the process is limited to, and likely to be perceived by the borrower as, assisting the borrower to make his own choice of product which has particular features which the borrower regards as important. The questioner will need to avoid making any judgement on the suitability of one or more products for the borrower. See also *PERG 4.6.4 G* for other matters that may be relevant.

- 4.6.23 G The potential for variation in the form, content and manner of ~~scripted~~ structured questioning is considerable, but there are two broad types.... There are various possible scenarios, including the following:
- (1) the questioner may go on to identify several *regulated mortgage contracts* which match features identified by the ~~scripted~~ structured questioning...
  - ...
  - (3) the questioner may, before or during the course of the ~~scripted~~ structured questioning, give a recommendation or opinion which influences the choice of mortgage contract and, following the ~~scripted~~ structured questioning, identify one or more particular *regulated mortgage contracts*; the key issue then is whether the advice can be said to relate to a particular *regulated mortgage contract* (see further *PERG 4.6.22G*).
- 4.6.24 G ...
- (1) the ~~scripted~~ structured questioning may not lead to the identification of any particular *regulated mortgage contract*...
  - (2) the ~~scripted~~ structured questioning may lead to the identification of one or more particular *regulated mortgage contracts*...
- 4.6.25 G In the scenarios identified in *PERG 4.6.23 G* (3) and *PERG 4.6.24 G* (2), the *FSA* considers that it is necessary to look at the process and outcome of ~~scripted~~ structured questioning as a whole... Factors that may be relevant in deciding whether the process involves *advising on regulated mortgage contracts* may include:
- ...
- (4) the role played by any questioner who guides a *person* through the ~~scripted~~ structured questions;

...

- (6) whether the ~~scripted~~ structured questions and answers have been provided by, and are clearly the responsibility of, an unconnected third party (for example, the *FSA*)...

...

- 4.6.28 G Taking electronic commerce as an example, the use of electronic decision trees does not present any novel problems. The same principles apply as with a paper version (see *PERG* 4.6.21 G to *PERG* 4.6.25 G (~~Scripted~~ Structured questioning (including decision trees))).





**PUB REF: 002406**

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