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Dear Nicky,

Improving switching options for mortgage customers who are currently unable to do so

As I mentioned at the Brexit hearing, I am writing to provide an update on our work on this important issue.

We define 'mortgage prisoners' as customers on a so-called reversion interest rate who would benefit from switching but are unable to do so, despite being up to date with payments on their existing mortgage.

Our analysis suggests that of the mortgage customers who are unable to switch, there are around:

- 10,000 customers with active, authorised lenders,
- 20,000 mortgage customers with firms that are no longer lending commercially, despite being authorised to do so (inactive lenders), and
- 120,000 customers of firms that are not authorised to lend (unregulated firms), who could potentially benefit from switching and may be unable to do so.¹

We have already made progress to help customers of active lenders to switch to a better deal (see below). Beyond this, we will take immediate action to help customers of inactive lenders and unregulated firms. We outline in this letter how we plan to address regulatory barriers to switching for these customers and how industry can contribute to a solution for this group.

Our approach to customers with active lenders

To help customers of active lenders, we proposed in our recent Mortgage Market Study Interim Report that lenders should commit to allowing customers to switch to a cheaper deal where they are up to date with payments on their current mortgage and are not looking to borrow more. We were therefore pleased to welcome the subsequent agreement among UK Finance, the Building Societies' Association and the Intermediary Mortgage Lenders' Association that enables borrowers on a reversion rate to move to a better deal with their existing lender where they meet certain criteria.²

¹ We hold insufficient data on these mortgages as firms not authorised to lend do not report to us, so we are not able to fully estimate the number of customers on a reversion rate that are unable to switch.

² Examples of this criteria: being up to date with payments, having a minimum of 2 years and £10,000 left on their mortgage.

Sixty-seven authorised lenders, making up 95% of the residential mortgage market, have signed up to the agreement. We will continue to monitor the impact of this agreement.

Our approach for customers of inactive lenders and unregulated firms

The key issue for the remaining customers is that their mortgages are held by a firm that does not or cannot offer the customer a new loan so internal switches are typically unavailable. In our view, the solution for such customers is therefore a switch to an active lender, with whom they may be able to get a better deal.

Since the implementation of the Mortgage Credit Directive in 2016, mortgage lenders have been required to undertake an affordability assessment of new customers even when customers are not borrowing a larger amount. These customers can therefore only switch to a better rate if they pass an affordability assessment and meet the lending criteria of an active lender.

We have limited data on customers whose mortgages are part of a book that has been sold to an unregulated firm, because we do not currently receive regulatory reporting on these mortgage books.³ The data we do have indicate that these customers are more likely to hold interest-only mortgages and mortgages with higher loan to value ratios than other mortgage borrowers. A significant minority of these mortgages may also be credit-impaired, as we know they were when the original mortgages were taken out.

We want to remove potential barriers in our rules to these customers switching to a cheaper mortgage. To help these customers, we will consult on changes to our responsible lending rules, with the aim to deliver a more proportionate affordability assessment. We intend to move the affordability assessment from an absolute test to a relative test. Thus, the test would be whether the new mortgage costs are more affordable than the current mortgage costs. Our focus will be on those customers who are seeking to move to a cheaper mortgage and are not borrowing more to ensure that a new mortgage is more affordable for these customers.

The role of industry

There also needs to be a willingness from industry to offer re-mortgaging opportunities to these customers once the regulatory barriers are removed. Participation will be a commercial decision for individual firms and not all will have the risk appetite to participate. Not all customers are likely to benefit as some will have specific circumstances that are likely to put them outside the commercial risk appetite of lenders. Such circumstances include mortgage customers who:

- are in arrears,
- have very high loan to value mortgages,
- have other considerable debts, or
- have mortgages in negative equity.

However, there will be customers who do not fall into these categories and who we believe will be able to switch to a better deal under our proposed rule changes.

Last week, we held a roundtable with industry to discuss appetite to lend to customers with closed or inactive firms and what regulatory support might be needed. This conversation suggested that there was a willingness to consider re-mortgage options, if commercially viable, for these customers. It may be that we see a two-tier approach, with the larger lenders offering a choice to those with the simplest needs, for example those with a repayment mortgage not in arrears, and a range of more specialist lenders able to manually underwrite more complex cases.

³ In our recent consultation paper [[CP18/41: FCA and PRA changes to mortgage reporting requirements | FCA](#)], we outlined how we are looking to improve the data we collect. As part of this, we are proposing to place a reporting obligation on the authorised administrators that administer mortgages on behalf of these entities.

Over the coming months, we will work with firms and trade bodies on the practicalities of re-mortgage options and how these options will be communicated to affected customers.

Next steps

We will publish our consultation paper setting out our proposals to remove regulatory barriers to switching for these customers alongside the Final Report of the Mortgage Market Study this spring.

Yours Sincerely

A handwritten signature in black ink, appearing to read "Andrew", with a long horizontal stroke extending to the right.

Andrew Bailey
Chief Executive