
FINAL NOTICE

To: **Yorkshire Building Society,**

Of: **Yorkshire House, Yorkshire Drive, Bradford, West Yorkshire BD5
8LJ**

Reference
Number: **106085**

Date: **28 October 2014**

1. ACTION

- 1.1. For the reasons given in this notice, the Authority hereby imposes on YBS a financial penalty of £4,135,600.
- 1.2. YBS agreed to settle at an early stage of the Authority's investigation. YBS therefore qualified for a 30% (stage 1) discount under the Authority's executive settlement procedures. Were it not for this discount, the Authority would have imposed a financial penalty of £5,908,100 on YBS.

2. SUMMARY OF REASONS

- 2.1. Between 1 October 2011 and 31 July 2012, YBS breached Principles 6 and 3 of the Authority's Principles for Businesses and certain of its mortgage and dispute resolution rules¹ in relation to its handling of mortgage customers in payment difficulties or arrears. These require firms to treat their customers fairly and to have in place adequate risk management systems.
- 2.2. During the Relevant Period, call handlers at YBS frequently failed to probe into the particular circumstances of individual customers who were in payment difficulties. They failed to identify the root cause of customers' difficulties, failed to assess their income and expenditure sufficiently and failed to establish their future financial prospects. As a consequence, in many cases, there were significant delays in determining appropriate payment solutions and this meant that arrears built up and increased fees and associated interest were incurred by YBS customers.
- 2.3. Rather than seek to identify and to agree payment solutions quickly, call handlers instead often sought ad hoc payments without sufficiently considering how these may have affected a customer's debt burden. Call handlers also failed to consider all payment options. In cases of long-term unaffordability, this may have included a voluntary sale by the customer or, in appropriate cases, repossession by YBS.
- 2.4. YBS failed to recognise the detrimental effect to customers of delays in agreeing solutions and they failed to focus on minimising and preventing delays. While repossession was properly viewed as a last resort for customers in payment difficulties, management did not take account of the fact that where repossession is appropriate, if it is delayed this causes further significant detriment to customers and leaves them in a worse financial position. Both of these failures meant that call handlers failed to act quickly to agree longer term solutions which were appropriate to the individual customer and it meant that systems of management oversight were ineffective in identifying and preventing the delays and in testing whether the decisions made were fair to the customer.

¹ Rules 13.3.1R(2), 13.3.2A R and 13.3.4A R of the Mortgages and Home Finance: Conduct of Business Sourcebook, and Rule 1.3.1R of Dispute Resolution: Complaints

- 2.5. The Authority's rules require firms to make reasonable efforts to reach agreement with customers over the repayment of any mortgage repayment shortfall and allow a reasonable time for repayment, having regard to the need to establish a payment plan which is practical in the individual circumstances of the customer. They are also required to identify, acknowledge and address complaints.
- 2.6. Customers suffering difficulties in making mortgage repayments or whose accounts are in arrears are frequently vulnerable as a result of financial problems and may be suffering from associated difficulties such as unemployment, relationship breakdown, bereavement or illness. It is important that firms proactively engage with these customers to ascertain the cause of their difficulties and their future financial prospects and to identify swiftly payment solutions appropriate to customers' individual circumstances and which are fair. To do this effectively, staff dealing with customers need to be adequately trained, sufficiently skilled and provided with appropriate guidance.
- 2.7. YBS failed to provide sufficient procedural guidance or training to call handling staff on assessing a customer's circumstances and identifying appropriate solutions.
- 2.8. In addition, weaknesses in its quality assurance monitoring and the provision of management information meant that unfair outcomes were not identified when they should have been. YBS should have monitored and identified that the repeated refusal of customers' direct debit payments meant that some customers incurred numerous monthly fees even when it should have been apparent to YBS that this was not an appropriate payment method and that continuing to request monthly payments was leading to a build up of fees and unfairness.
- 2.9. Call handlers also failed to identify and acknowledge customer complaints, which meant that complaints went unresolved. This was unfair to individual complainants, but it also meant that YBS management was deprived of information which may have revealed underlying problems.
- 2.10. The Authority considers YBS's failings to be serious for the following reasons:

- (1) A large number of customers (approximately 9,000) were potentially affected by the failings;
- (2) Many of these customers were vulnerable because of financial difficulties or associated problems;
- (3) YBS failed to identify the failings itself: they were brought to YBS's attention by the Authority;
- (4) Despite being made aware of the problems, YBS has been slow to implement improvements to its systems and processes to prevent recurrence of the identified failings; and
- (5) On several occasions in the years preceding the Relevant Period, the Authority had communicated to firms including YBS the importance of the fair treatment of customers in arrears.

2.11. While the Authority considers the failings to be serious, it recognises that YBS did not seek to make any profits, nor avoid any losses, as a result of the breaches. Many of the failures resulted from an approach which gave customers more time to get themselves out of financial difficulties but which delayed the agreement of payment solutions. The Authority recognises that YBS has made improvements to its processes since the Relevant Period and that some of these improvements were under development before being notified of the Authority's concerns.

2.12. YBS took proactive steps to provide redress to affected customers. On 17 February 2014, YBS announced that it would refund all mortgage arrears fees, and accrued interest, charged to customers since January 2009. It is expected that approximately 33,900 current and former customers will receive back an average of £247, at a total cost to YBS of £8.4 million. It has also ceased charging mortgage arrears fees until the identified issues are resolved. YBS has conducted this exercise in a transparent manner, publishing a statement on its website and agreeing for a similar statement to be published on the Authority's website.

2.13. The Authority therefore imposes a financial penalty on YBS of £4,135,600 pursuant to section 206 of the Act.

3. DEFINITIONS

3.1. The definitions below are used in this Final Notice.

“the Act” means the Financial Services and Markets Act 2000;

“the Authority” means the body corporate previously known as the Financial Services Authority and renamed on 1 April 2013 as the Financial Conduct Authority;

“the Barnsley” means the Barnsley Building Society and the brand name used by YBS after merging with it;

“the Chelsea” means the Chelsea Building Society and the brand name used by YBS after merging with it;

“CMI” means Contractual Monthly Instalment, the usual monthly mortgage repayment to be made by customers, excluding any other payments in respect of fees, outstanding arrears or other charges (for example PPI premiums);

“DEPP” means the Authority’s Decision Procedure and Penalties Manual;

“DISP” means the Authority’s Dispute Resolution: Complaints Manual;

“MCOB” means the Authority’s Mortgages and Home Finance: Conduct of Business Sourcebook;

“MI” means Management Information;

“N&P” means the Norwich and Peterborough Building Society and the brand name used by YBS after merging with it;

“Principle” means one of the Authority’s Principles for Businesses;

“QA” means Quality Assurance;

“Relevant Period” means 1 October 2011 to 31 July 2012;

“Skilled Person” means the person appointed, pursuant to section 166 of the Act, to carry out a review of YBS’s mortgage arrears files and to report on its findings;

“the Tribunal” means the Upper Tribunal (Tax and Chancery Chamber);

“YBS” means the Yorkshire Building Society.

4. FACTS AND MATTERS

Background to YBS

- 4.1. YBS is a building society founded in Yorkshire. It has been authorised by the Authority since 1 December 2001. Between 2008 and 2012, YBS underwent significant growth, merging with the Barnsley in 2008, the Chelsea in 2010 and N&P in 2011. It also acquired the mortgage business of the Egg brand in 2011. It is now the UK's second largest building society.
- 4.2. YBS specialises in the provision of residential mortgages. It provides mortgages using the YBS, the Barnsley, the Chelsea and N&P brand names, as well as 'Accord Mortgages', the brand name of Accord Mortgages Ltd, an intermediary-only mortgage provider (a lender which deals only through mortgage brokers) wholly owned by YBS.
- 4.3. As of November 2013, YBS had 3.6 million customers and held residential mortgages to the value of £28.3 billion.

Mortgage arrears

- 4.4. The provision of residential mortgages has been regulated by the Authority since 31 October 2004. Since that date, administering a regulated mortgage contract has been a regulated activity. This includes dealing with customers who are suffering payment difficulties or whose mortgage accounts are in arrears.
- 4.5. The fair treatment of customers experiencing difficulties in the payment of their mortgages is of particular importance. Many such customers are experiencing financial problems and, consequently, are vulnerable. Some have associated difficulties such as unemployment, relationship breakdown, bereavement or illness. The failure of a mortgage agreement may result in them being rendered homeless.
- 4.6. Mortgage lenders may consider a range of potential solutions to customers experiencing payment difficulties. These may be:
 - (1) short-term, such as brief payment holidays, temporary conversion to interest-only repayment terms or 'negative' arrangements to pay

(where the agreed monthly repayment is less than the normal Contractual Monthly Instalment ("CMI")); or

(2) longer-term, such as 'positive' arrangements to pay (where the customer agrees to pay a monthly sum above the CMI to pay back arrears over time), the capitalisation of arrears, the extension of the mortgage term, supporting and assisting with a sale of the property by the customer or, in appropriate cases, taking possession of the property.

4.7. The suitability of any particular solution depends on the individual circumstances of a customer and relevant considerations include the particular reasons for the payment difficulties, whether they are short, medium or long-term, and the future financial prospects of the customer.

4.8. It is important that firms engaged in arrears handling activities proactively engage with their customers who are experiencing payment difficulties, identify the cause of the problems suffered by each particular customer and quickly seek to agree solutions which are appropriate to the particular circumstances of the customer.

4.9. In the absence of an arrangement to pay or other agreement being in place, YBS imposed a charge of £35 for every month that a customer had more than two months' arrears outstanding. This charge was applied even if payments of the CMI restarted and continued to be made. Other charges were made if direct debit payment requests were refused, if home visits were carried out or if cases were referred for litigation. Interest continued to be charged on arrears and on any outstanding fees.

4.10. Therefore, delays in the process of identifying and agreeing appropriate solutions risked a build-up of arrears, fees and associated interest. The imposition of solutions that were not appropriate to customers' particular circumstances risked causing significant extra cost to customers or a failure to sustain the solution, resulting in a further deterioration in the customer's financial position, potentially threatening the possession of their home.

History of YBS's mortgage arrears handling

4.11. In 2008, worsening economic conditions led to anticipation across the market of increasing levels of mortgage arrears. In August 2008, the Authority

published a thematic review of mortgage arrears handling which included a guide to good and poor practices. In November 2008, the Authority published a 'Dear CEO letter' which emphasised the importance of treating customers fairly.

- 4.12. In July 2011, the Authority visited YBS to conduct a supervisory risk assessment. As a result of the risk assessment visit, the Authority wrote to YBS explaining that their policy on arrears forbearance was unclear and that there was no qualitative or quantitative MI to assess the effectiveness of forbearance tools.
- 4.13. In August 2012, the Authority conducted outcomes testing on mortgage arrears files. Following the review, the Authority wrote to YBS in September and October 2012 stating that the review highlighted serious failings within the monitoring and oversight of arrears cases which produced unfair outcomes for customers.
- 4.14. In May 2013, the Authority issued a requirement under section 166 of the Act for a Skilled Person to conduct a review of arrears handling. One of the purposes of the review was to test customer outcomes over the course of the Relevant Period.
- 4.15. The Skilled Person carried out a review of 100 customer files (of which 87 were regulated mortgages) relating to customers that were in arrears at some point during the Relevant Period.
- 4.16. The Skilled Person found that, in 64 of the 87 (74%) regulated mortgage cases considered, customers were not treated fairly. In 52 of these cases (60%), actual customer detriment could be identified. As detailed below, the unfair treatment included:
 - (1) failing to consider the individual circumstances of customers;
 - (2) failing to consider all payment options;
 - (3) seeking inappropriate payments;
 - (4) failing to assist with voluntary sales;
 - (5) a resistance to taking possession in appropriate circumstances;

- (6) delays in determining solutions; and
- (7) failing to identify and resolve customer complaints.

Dealing with customers

- 4.17. YBS administered the mortgages provided by each of its various brands. During the Relevant Period, YBS dealt with approximately 9,000 customers whose accounts were in arrears by more than two months.
- 4.18. Responsibility for dealing with customers in arrears at YBS lay with the Collections and Recoveries department. As of November 2013, YBS employed 165 full time employees in the Collections and Recoveries Department over three sites.
- 4.19. Within this Department, call handlers communicated directly with customers. They received incoming telephone calls and conducted outbound telephone calls to customers automatically identified by a computer system. They were also responsible for issuing letters to customers and arranging home visits if customers could not otherwise be contacted.

Policy and procedures

- 4.20. In October 2009, a senior risk committee at YBS approved the arrears handling policy document. The document was approved annually thereafter.
- 4.21. The policy document was six pages long and did not contain sufficient detail to provide meaningful guidance to call handlers as to how they should approach the consideration of customers' circumstances and how they should determine the appropriate course of action.
- 4.22. The policy was supported by a number of procedural documents which were made available to arrears handling staff. However, these were agreed at an operational, rather than committee, level and there was no formal process for ensuring the consistent presentation and use of procedural documentation.
- 4.23. The result was that procedural guidance was fragmented, and designed to address specific issues rather than to consider the overall process of arrears handling in a holistic manner.

- 4.24. For example, there was no policy for dealing with non-cooperative customers, creating a risk that call handlers were unsure what to do when customers failed to cooperate and that, as a result, cases would be allowed to drift. For example, Mr and Mrs P entered arrears after they separated and Mr P moved out of the property. Although YBS maintained contact with Mr P, he stated that he was unable to make payments and contact could not be established with Mrs P for seven months. During that time, while Mrs P made some payments, no solutions were put in place and arrears charges were imposed in five of the seven months.
- 4.25. Nor was there any policy for identifying and treating customers in particularly sensitive positions, such as those with serious, terminal or mental health illnesses. As a result, staff did not always identify nor deal appropriately with such customers. Errors with the automated system for contacting customers led to YBS mistakenly continuing to contact one customer, who was seriously ill. This customer complained of feeling harassed as a result of these contacts: this would have been prevented if YBS had identified her case as sensitive.
- 4.26. In April 2012, YBS implemented a new, more thorough policy document. This provided call handlers with more detailed guidance but the policy was not always followed by arrears handling staff during the Relevant Period.

Assessment of income and expenditure

- 4.27. In September 2008, YBS made a decision not to follow the Good Practice published by the Authority which gave an example of completing an income and expenditure assessment form for customers in arrears. Although assessment tools were available for staff, it was adjudged that arrears handlers could ascertain sufficient information to assess appropriate repayment solutions through their discussions with the customer.
- 4.28. However, little detailed procedural guidance was given to call handlers as to how they should assess a customer's financial circumstances. One guidance document stated simply: '*some discussion to assess whether the amount is reasonable must take place*' before arrangements could be agreed.

4.29. YBS updated its procedures in November and December 2011 to require the completion of income and expenditure assessments in certain circumstances. However, this procedure was not always followed during the Relevant Period.

Failure to consider individual circumstances

4.30. The lack of appropriate guidance meant that call handlers did not consistently probe into individual customers' circumstances and identify the cause of their problems to establish whether they were short, medium or long-term. This was evidenced in the sample of customer cases reviewed by the Skilled Person in a number of different ways:

- (1) Call handlers failed to identify the root cause of a customer's financial difficulties and how this affected the suitability of various solutions. This included sensitive cases involving customers with serious illness: in the case of one customer who spent time in hospital, YBS failed to consider short-term solutions, despite the customer notifying it that he should be able to return to work shortly;
- (2) Call handlers often did not carry out any meaningful assessment of customers' income and expenditure and thus failed to collect a full picture of customers' circumstances;
- (3) Call handlers were willing to accept the explanations and assertions of customers without probing sufficiently into the plausibility of these explanations or the realism of the assertions: in one case, call handlers failed, on approximately 30 occasions, to challenge a customer's promises to pay the full arrears; in another, a customer's continued assertions that he was expecting an insurance payment were not questioned, evidenced or investigated for three months;
- (4) On occasions, call handlers did not discuss possible means of increasing the customers' sources of income, including their eligibility to claim under payment protection insurance contracts, or to reduce levels of expenditure;
- (5) In some cases, little or no attempt was made to establish the future financial prospects of customers and how these may affect their ongoing ability to maintain mortgage payments. In particular, there was evidence of a lack of understanding of how to probe into the financial

circumstances of customers who were self-employed and whose income therefore depended on the future business outlook.

- 4.31. Because they did not probe sufficiently into customers' circumstances, call handlers were unable to demonstrate that the various payment options had been considered and discussed with customers and that suitable solutions had been identified at an early stage.
- 4.32. An example of this concerns Customer B. Customer B missed her first mortgage payment after losing her job. Over the course of the next eight months, YBS made a total of 30 calls to her: the customer made various excuses for the missed payments and there was little attempt to understand her financial position. Although a one month payment holiday was agreed during this time, no assessment of income and expenditure was carried out, and consequently there was no sufficient understanding of how this would assist the customer. No income and expenditure assessment was undertaken until a home visit was carried out eight months after the first mortgage payment was missed. Customer B ultimately redeemed her mortgage.

Failure to consider options

- 4.33. From the sample of cases, there was frequently limited consideration of options other than arrangements to pay, even when the customer's long term financial outlook was uncertain or when the problems were demonstrably short-term and other options may have been more appropriate. The Skilled Person noted this in 25 of the regulated sample cases.
- 4.34. For example, Mr and Mrs F entered arrears following a short period of reduced income for Mr F, coupled with maternity leave for Mrs F. Despite the short-term nature of the issues, no appropriate short-term solutions appear to have been considered and no arrangements to pay were agreed because Mr and Mrs F's short-term income and expenditure assessment showed them to be in deficit. As a result, although CMI payments recommenced six months after entering arrears, arrears fees and other charges continued to be applied. A total of £296 in charges was applied during the Relevant Period.
- 4.35. As in the above example, this failure to consider the full range of options meant that opportunities to agree solutions at an early stage were missed. It also resulted in arrangements to pay being put in place in inappropriate

circumstances, often without any consideration of a customer's income and expenditure or even when income and expenditure assessments suggested they were not affordable.

- 4.36. As a consequence, arrangements were broken because customers were unable to keep up with payments. This caused them to incur further charges and potentially prolonged the time they were in arrears.

Seeking inappropriate payments

- 4.37. Rather than attempting to find overall solutions, the case sample showed call handlers seeking to take payments as a 'contribution' or 'commitment' or encouraging customers to 'make any payment' when its affordability could not be established or when the customer stated that he could not afford it at the time.

- 4.38. Similarly, YBS accepted payments from friends or family, or payment on credit cards, without sufficient consideration of how that may impact on the customer's debt burden or the ongoing sustainability of payment arrangements.

- 4.39. This may have been done in order to avoid arrears on a customer's account falling beyond a limit which would incur a fee or result in an adverse credit rating report but its effect was to prioritise the collection of ad hoc payments ahead of the agreement of a long-term, sustainable solution.

- 4.40. Although this practice was not prescribed by YBS's policy, it was nonetheless common practice and accepted by management as such.

Voluntary sales

- 4.41. If a customer's financial position means that he or she is unable to afford mortgage repayments and is realistically unlikely to be able to do so in the future, a prompt sale of the property may be the best solution. In these circumstances, delays in effecting the sale may lead to a rapid build-up of arrears and interest and a significant deterioration in the customer's financial position. Yet, because they failed to ascertain customers' circumstances, call handlers failed to identify cases in which a voluntary sale may have been the most appropriate solution.

4.42. Customer J advised YBS that she had been made redundant, that she was unlikely to find employment at the same salary level and that she would be unable to afford future mortgage payments. YBS failed to consider the option of a voluntary sale. No further payments were made and arrears fees were charged for seven consecutive months. Eventually, litigation began and the property was sold at a shortfall a further five months later.

Reluctance to Take Possession

4.43. Similarly, there was a general reluctance in the four relevant cases reviewed to take possession of a property even when the customer had moved out and the property was empty. While taking possession was properly viewed as a last resort, in cases where it was the appropriate remedy, delays in taking action resulted in customers accumulating further interest and fees.

4.44. An example is that of Customer E. Customer E contacted YBS prior to entering arrears, to inform it of the unaffordability of the mortgage. YBS did not pro-actively discuss exit strategies with Customer E at that stage, despite knowing that the position was not going to change. Once her account entered arrears, because an arrangement to pay was deemed unaffordable and no other options were considered, YBS charged her arrears fees monthly. Interest of approximately £2,500 per month continued to accrue. Total charges of £394 were applied in the Relevant Period and the account was at one stage almost £20,000 in arrears.

4.45. Despite knowing that Customer E had moved out, YBS failed to take possession of the property for a further six months. The property was eventually sold with a shortfall the following year.

Delays

4.46. As a result of the failings outlined in the paragraphs above, there was evidence, in the sample of cases reviewed, of significant and unexplained delays in determining appropriate actions. Some of these delays lasted months, with no clear exit strategy and with little review taking place. Contact with customers often simply involved 'updates' or the seeking of a 'contribution'. For example, between November 2011 and July 2012, 36 telephone calls were conducted with one customer without any assessment of

income and expenditure being made and without any solution being put in place.

- 4.47. It was not recognised at a managerial level that delays in the process of agreeing solutions was detrimental to a customer's financial position, and therefore unfair to the customer. One senior manager believed that delay was detrimental to YBS, which was bearing the risk, rather than to the customer. As a consequence, there was a lack of focus on minimising and preventing delays.

Repeated charging of direct debit refusal fees

- 4.48. A further example of a failure to consider customer circumstances was the repeated charging to some customers of direct debit refusal fees. YBS encouraged customers to make mortgage payments by direct debit. These payments were automatically requested from the customer's bank account each month. If there were insufficient funds in a customer's bank account, the bank might refuse to make the direct debit payment. On the first occasion this happened to any customer, YBS did not charge a fee. However, on each subsequent occasion, YBS charged the customer £25. This charge was in addition to any charge made for being in arrears.
- 4.49. Although YBS did not re-present the same direct debit payment request more than once a month, it did continue to present monthly direct debit payment requests (and to charge fees for the refusal of such requests) no matter how many such requests had been declined.
- 4.50. In 2008, YBS had specifically rejected the possibility of implementing a policy to limit the presentation of payment requests which were repeatedly refused, reasoning that it was the responsibility of the customer to cancel a payment arrangement if it was inappropriate.
- 4.51. There was no specific procedure in place to monitor the fairness of continuing to present direct debit payment requests. Because of this, and because of the delays in determining arrears solutions, there was a risk that some customers would be charged direct debit refusal fees repeatedly, even when it should have been apparent to YBS that this means of payment may have been inappropriate.

- 4.52. As a result, the direct debit payment requests in respect of some customers were refused on numerous occasions, often in consecutive months. Although call handlers were expected to attempt contact with a customer after each direct debit payment refusal, contact was not always successfully made and, when it was, call handlers did not always address the suitability of the direct debit payment method. Consequently, payment requests continued to be presented and, if refused, fees charged.
- 4.53. In respect of some customers, this resulted in the imposition of significant fees on which interest then accrued. During a 34 month period leading up to, and including, the Relevant Period, 324 customers were charged direct debit refusal fees more than four times a year. One customer, Mr R, was charged a direct debit refusal fee on 32 occasions, the fees totalling £800. Call handlers at YBS made concerted efforts to contact Mr R, attempting 150 outbound calls and sending 32 letters during the 34 month period. Yet, despite 16 telephone contacts with the customer during this period, a call handler identified and addressed the incurring of a direct debit fee on only one occasion, at which time the date of payment request was changed.

Failure to identify and acknowledge customer complaints

- 4.54. From the sample, the Skilled Person identified 28 cases in which an expression of dissatisfaction amounting to a complaint was made by a customer. In 23 of these cases, complaints were not dealt with appropriately.
- 4.55. In most of these cases, expressions of dissatisfaction were made during the course of arrears handling telephone calls, yet often call handlers did not identify nor acknowledge that a complaint had been made. Consequently, such complaints were not recorded nor investigated.
- 4.56. On other occasions, although call handlers acknowledged the customers' dissatisfaction, nonetheless they failed to log or record it as a complaint and consequently it was not investigated. Several customers complained on multiple occasions: one customer from the cases reviewed repeatedly complained that a sale process was proceeding slowly and causing her distress and depression. These complaints were not logged nor recorded as such.

4.57. As a result, not only did individual customers not have their complaints investigated, but YBS management was not provided with information which may have indicated a more wide-spread problem.

Failures in oversight

4.58. YBS's systems of oversight should have identified or prevented the shortcomings identified above. Instead, the lack of managerial focus on the detrimental effects to customers of delay created weaknesses in these systems which, in turn, contributed to the poor treatment of customers.

Training and competence

4.59. The identification and implementation of appropriate payment solutions requires call handlers to have the requisite skills, knowledge and expertise and the ability to make reasoned and considered judgements. It is important that lenders provide call handlers with the necessary training and maintain appropriate levels of monitoring to ensure standards remain high.

4.60. While YBS's training of call handlers covered the questioning of customers, the sessions were not of sufficient breadth or length to provide trainees with the necessary expertise to ascertain customers' circumstances in adequate detail, to consider the range of payment solutions and to make appropriate judgments based on those circumstances.

Quality assurance

4.61. During the Relevant Period, assurance of the quality of YBS's call handling staff was conducted by their team managers, who monitored a specified number of telephone calls per month conducted by each call handler. No formal training was provided as to how they should judge the call handlers in assessing the customers' individual circumstances and providing advice on the available options. As a result, it was impossible to assess whether a consistent approach was used.

4.62. YBS did not conduct an 'end to end' assessment of individual mortgage cases in the collections process. The QA carried out by YBS did not routinely consider evidence from outside the particular call or work event being reviewed. It did not generally consider other calls or correspondence with the same customer. As such, YBS did not test the outcomes experienced by

customers over a period of time, and throughout the collections process. As a result, the QA process was insufficient to identify issues concerning the overall fairness of customer outcomes over time.

Management information

- 4.63. A consequence of the inadequacies of the QA regime was that the information provided to management was insufficient to allow it to determine whether the system was producing unfair outcomes.
- 4.64. The analysis of the information collated as a result of the QA process was directed towards identifying the performance of each call handler, rather than to identifying common issues or problems which may lead to unfair customer outcomes.
- 4.65. Even when significant numbers of calls failed to adhere to YBS standards (as in March 2012 when 28% of calls were deemed to have failed to meet the required standards), no analysis was conducted to identify whether customer detriment resulted. Throughout the Relevant Period, no common issues were reported to senior management.
- 4.66. Because no end-to-end assessment of arrears cases was carried out, little information was available to enable management to assess outcomes effectively. While YBS collated and reported data on the numbers of customers entering various payment solutions, it did not report the numbers remaining within each solution and did not carry out customer level monitoring to assess the length of time customers remained within a particular solution. Consequently, the ability of management to identify delays in the system and trends in the use or success of various payment solutions was limited.

Improvements and Redress

- 4.67. Since the Relevant Period, YBS has developed and implemented improvements to its systems for handling customers in arrears. In June 2014, the Skilled Person undertook a further review of arrears handling at YBS to determine whether the changes had resulted in improved customer outcomes.

- 4.68. The Skilled Person considered the questioning of customer circumstances and the consideration of payment solutions to have improved and observed the elimination or reduction of many of the poor practices identified above. As a consequence, where contact was made with customers, improved outcomes resulted. However, the Skilled Person still found that customers were subjected to some unfair treatment in half of the cases reviewed. The principal reason was identified as a lack of resourcing in the Collections and Recoveries department which had led to delays in contacting customers. This was attributable in part to YBS having moved call handlers from operational duties to oversight and QA duties, thus reducing the staffing levels available to handle customer calls. Customer detriment was significantly less because YBS did not charge customers arrears fees.
- 4.69. On 17 February 2014, YBS announced that it would refund all mortgage arrears fees, and accrued interest, charged to customers since January 2009. These refunds cover charges made in respect of both regulated and unregulated mortgages. YBS has made the refunds on a proactive basis, meaning that customers do not have to apply: current customers have automatically had credits applied to their accounts, while former customers have been traced and payments sent to them. It is expected that approximately 33,900 current and former customers will receive back an average of £247, at a total cost to YBS of £8.4 million. Further, YBS has not charged mortgage arrears fees since that time and will not do so until the improvements are sufficiently embedded.
- 4.70. In undertaking the redress exercise, YBS has been transparent with its customers throughout. In addition to writing to affected customers, YBS published a full statement about the redress exercise which it displayed on its website and agreed with the Authority for the publication of a similar statement on the Authority's website.

5. FAILINGS

- 5.1. The regulatory provisions relevant to this Final Notice are referred to in Annex A.

Breach of Principle 6 and associated rules

- 5.2. Principle 6 requires a firm to pay due regard to the interests of its customers and to treat them fairly.
- 5.3. Additionally, during the Relevant Period:
- (1) MCOB 13.3.2A R required a firm to make reasonable efforts to reach an agreement with customers over the method of repaying a payment shortfall and to allow a reasonable time to repay the shortfall, having particular regard to the need to establish, where feasible, a payment plan which was practical in terms of the circumstances of the customer; and
 - (2) in complying with this requirement, MCOB 13.3.4A R required a firm to consider whether a number of potential options were appropriate, given the individual circumstances of the customer.
- 5.4. From the sample of cases, YBS breached these requirements in that:
- (1) By failing to probe sufficiently into individual customer circumstances, YBS failed to determine whether a particular customer's financial problems were short, medium or long-term;
 - (2) As a result, it was unable to determine the suitability of payment plans in the circumstances of individual customers;
 - (3) YBS failed to give due consideration to the full range of potential payment solutions and concentrated on arrangements to pay. This meant that potentially suitable options were not considered and that inappropriate arrangements to pay were agreed;
 - (4) Rather than seeking overall solutions, YBS call handlers frequently sought ad hoc payments. As well as contributing to the failure to address and solve the underlying problems, little consideration was given to the effect these payments may have had on customers' overall debt burden and consequently risked making their financial situations worse;
 - (5) YBS failed to identify circumstances in which a voluntary sale was appropriate; and

- (6) YBS failed to take possession of properties, even when it was appropriate.
- 5.5. The effect of these failings was that YBS did not identify nor agree appropriate payment plans at an early stage and, accordingly, customers remained in arrears for longer periods of time. As a consequence, they were exposed to higher levels of fees and interest, and arrears were allowed to build up. Delays in the process worsened customers' financial positions and made realistic and appropriate solutions more difficult to obtain.
- 5.6. Accordingly, because of these failings, YBS breached not only Principle 6 but also MCOB 13.3.2A R and 13.3.4A R.
- 5.7. DISP 1.3.1R requires firms to maintain effective procedures for complaint handling. By failing to identify complaints, or to treat them as such, YBS failed to handle complaints effectively. This meant that customers were deprived of the right to have their complaints investigated competently, diligently and impartially and the opportunity to remedy particular problems experienced in the arrears handling process was missed.
- 5.8. Because complaints were not recorded, there was no opportunity for management to consider and address any root causes which the complaints might have identified. Accordingly, in addition to breaching Principle 6, YBS breached DISP 1.3.1R.

Breach of Principle 3 and associated rules

- 5.9. Principle 3 requires that a firm take reasonable steps to ensure that it has organised its affairs responsibly and effectively, with adequate risk management systems. During the Relevant Period, MCOB 13.3.1R(2) required a firm to put in place, and operate in accordance with, a written policy and procedures for dealing fairly with any customer who was in arrears and which reflected the requirements of MCOB 13.3.2A R and 13.3.4A R.
- 5.10. YBS failed to take such reasonable steps or to put in place and operate in accordance with such a policy and procedures in that:
- (1) Prior to April 2012, YBS failed to put in place and maintain an adequate policy for dealing with customers with payment difficulties or in arrears. In particular, YBS's policy was not sufficiently detailed to give

appropriate direction to the call handlers in its collections department as to how they should assess customers' financial circumstances;

- (2) There was no formal process for ensuring that the documentation governing mortgage arrears handling procedures was presented and maintained in a consistent manner;
- (3) There was no process for monitoring the fairness of repeatedly charging direct debit refusal fees;
- (4) The training of call handling staff paid insufficient attention to the need to establish customer circumstances and consequently failed to prepare call handlers adequately;
- (5) The QA conducted by YBS was inadequate to measure and assess the quality of customer outcomes; and
- (6) The information provided to management was insufficient to allow management to determine that unfair customer outcomes were resulting and to take action to remedy the problems.

5.11 These weaknesses, some of which dated back to before the Relevant Period, both contributed to the failure by YBS to treat its customers fairly, in the ways identified above, and to preventing YBS from identifying and remedying these failures. As such, in addition to breaching Principle 3, YBS also breached MCOB 13.3.1R(2).

6. SANCTION

- 6.1. The Authority's policy on the imposition of financial penalties is set out in DEPP. In determining the financial penalty, the Authority has had regard to this guidance.
- 6.2. The principal purpose of a financial penalty is to promote high standards of regulatory conduct by deterring firms who have breached regulatory requirements from committing further contraventions, helping to deter other firms from committing contraventions and demonstrating generally to firms the benefits of compliant behaviour.
- 6.3. For the reasons set out above, the Authority considers that YBS failed to comply with Principles 6 and 3 and breached MCOB 13.3.1R(2), 13.3.2A R

and 13.3.4A R and DISP 1.3.1R. In determining that a financial penalty is appropriate and proportionate in this case, the Authority has considered all the relevant circumstances.

- 6.4. Changes to DEPP were introduced on 6 March 2010. In respect of conduct occurring on or after 6 March 2010, the Authority applies a five step framework to determine the appropriate level of financial penalty. DEPP 6.5A sets out the details of the five step framework that applies in respect of financial penalties imposed on firms.

Step 1: disgorgement

- 6.5. Pursuant to DEPP 6.5A.1G, at Step 1, the Authority seeks to deprive a firm of the financial benefit derived directly from the breach where it is practicable to quantify this.
- 6.6. It is not practicable for the Authority to quantify any financial benefit that YBS may have derived directly from its breach. However, as YBS has agreed to repay all arrears charges and capitalised interest thereon imposed during the Relevant Period, the Authority is satisfied that this negates any direct financial benefit that may have accrued to it from its arrears handling activities.
- 6.7. Step 1 is therefore £0.

Step 2: the seriousness of the breach

- 6.8. Pursuant to DEPP 6.5A.2G, at Step 2, the Authority determines the figure that reflects the seriousness of the breach. Where the amount of revenue generated by a firm from a particular product line or business area is indicative of the harm or potential harm that its breach may cause, the figure will be based on a percentage of the firm's revenue from the relevant product or business area.
- 6.9. The Authority considers that the total level of fees and interest payments received from customers only while their accounts were in arrears during the Relevant Period is indicative of the harm or potential harm which may have been caused by the breaches. The Relevant Period is only a ten month period therefore, in accordance with DEPP 6.5.A.2G(2), revenue figures have been taken for the 12 month period prior to the end of the Relevant Period.

6.10. Over the course of the 12 month period prior to 31 July 2012, this figure amounted to £47,264,890.

6.11. In deciding on the percentage of the relevant revenue that forms the basis of the Step 2 figure, the Authority considers the seriousness of the breach and chooses a percentage between 0% and 20%. The range is divided into five fixed levels which represent, on a sliding scale, the seriousness of the breach; the more serious the breach, the higher the level. For penalties imposed on firms, there are the following five levels:

Level 1 – 0%

Level 2 – 5%

Level 3 – 10%

Level 4 – 15%

Level 5 – 20%

6.12. In assessing the seriousness level, the Authority takes into account various factors which reflect the impact and nature of the breach, which include:

(1) The loss or risk of loss caused to individual consumers (DEPP 6.5A.2G(6)(c));

(2) Whether the breach had an effect on particularly vulnerable people, whether intentionally or otherwise (DEPP 6.5A.2G(6)(d));

(3) The inconvenience or distress caused to consumers (DEPP 6.5A.2G(6)(e));

(4) The nature of the rules, requirements or provisions breached (DEPP 6.5A.2G(7)(a));

(5) The frequency of the breach (DEPP 6.5A.2G(7)(b));

(6) Whether the firm, in committing the breach, took any steps to comply with the Authority's rules, and the adequacy of those steps (DEPP 6.5A.2G(7)(h)).

6.13. DEPP 6.5A.2G(11) lists factors likely to be considered 'level 4 factors' or 'level 5 factors'. The Authority considers the following factors to be relevant:

(1) The breach caused a significant loss or risk of loss to individual consumers (DEPP 6.5A.2G(11)(a)). The extent of individual losses is difficult to quantify, the potential impact (both in monetary terms and the potential loss of a home) to individual consumers through poor arrears handling is considerable, particularly given the vulnerability of many such customers; and

(2) The breach revealed serious weaknesses in the firm's procedures relating to all or part of the firm's business (DEPP 6.5A.2G(11)(b)).

6.14. DEPP 6.5A.2G(12) lists factors likely to be considered 'level 1 factors', 'level 2 factors' or 'level 3 factors'. Of these, the Authority considers the following factors to be relevant:

(1) Little, or no profits were made or losses avoided as a result of the breach, either directly or indirectly (DEPP 6.5A.2G(12)(a)); and

(2) The breach was committed negligently or inadvertently (DEPP 6.5A.2G(12)(e)).

6.15. Taking all these factors into account, the Authority considers the seriousness of the breach to be level 3 and so the Step 2 figure is 10% of £47,264,890.

6.16. The figure at Step 2 is therefore £4,726,489.

Step 3: mitigating and aggravating factors

6.17. Pursuant to DEPP 6.5A.3G, at Step 3 the Authority may increase or decrease the amount of the financial penalty arrived at after Step 2, but not including the amount to be disgorged as set out in Step 1, to take into account factors which aggravate or mitigate the breach.

6.18. The Authority considers that the following factors aggravate the breach:

(1) YBS did not identify the breaches itself. The breaches were brought to YBS's attention by the Authority and by the Skilled Person;

- (2) Despite having designed and developed improved systems and controls, YBS has been slow to implement some of the improvements and to devote sufficient resources to ensure the resolution of all the identified issues, as noted in the findings of the review by the Skilled Person in June 2014;
- (3) The Authority issued published guidance on arrears handling on several occasions in the years prior to the Relevant Period. In respect of the failure to complete income and expenditure assessments and the repeated presentation of direct debit payment requests, YBS made deliberate decisions not to follow this guidance but failed to implement sufficient alternative safeguards;
- (4) In June 2014, the Authority imposed a financial penalty of £1,429,000 on YBS for failing to ensure that financial promotions for a structured product were clear, fair and not misleading.

6.19. The Authority considers that the following factors mitigate the breach:

- (1) YBS acknowledged the failings raised by the Authority and voluntarily embarked on an extensive and pro-active redress exercise prior to the Enforcement referral, refunding all arrears fees and related interest applied to any customer's account from 1 January 2009 to February 2014;
- (2) In undertaking this redress exercise, YBS has been transparent with its customers throughout: YBS published a statement on its website with details of the exercise and agreed for a similar statement to be published on the Authority's website;
- (3) In addition, YBS has voluntarily suspended charging mortgage arrears fees for customers until improvements to procedures and controls are sufficiently embedded.

6.20. The Authority has considered the various aggravating and mitigating factors and, having done so, considers that the Step 2 figure should be subject to a 25% uplift at Step 3.

6.21. Therefore, the Step 3 figure is £5,908,111.

Step 4: adjustment for deterrence

- 6.22. Pursuant to DEPP 6.5A.4G, if the Authority considers the figure arrived at after Step 3 is insufficient to deter the firm who committed the breach, or others, from committing further or similar breaches, then the Authority may increase the penalty.
- 6.23. The Authority considers that the Step 3 figure represents a sufficient deterrent to YBS and others, and so has not increased the penalty at Step 4.
- 6.24. The figure at Step 4 therefore remains £5,908,111.

Step 5: settlement discount

- 6.25. Pursuant to DEPP 6.5A.5G, if the Authority and the firm on whom a penalty is to be imposed agree the amount of the financial penalty and other terms, DEPP 6.7 provides that the amount of the financial penalty which might otherwise have been payable will be reduced to reflect the stage at which the Authority and the firm reached an agreement. The settlement discount does not apply to the disgorgement of any benefit calculated at Step 1.
- 6.26. The Authority and YBS reached agreement at Stage 1 and so a 30% discount applies to the Step 4 figure.
- 6.27. The figure at Step 5 is therefore £4,135,678 which has been rounded down to £4,135,600.

Penalty

- 6.28. The Authority therefore imposes a total financial penalty of £4,135,600 on YBS for breaching Principles 6 and 3, MCOB Rules 13.3.1R(2), 13.3.2A R and 13.3.4A R and DISP Rule 1.3.1R.

7. PROCEDURAL MATTERS

Decision maker

- 7.1. The decision which gave rise to the obligation to give this Final Notice was made by the Settlement Decision Makers.
- 7.2. This Final Notice is given under, and in accordance with, section 390 of the Act.

Manner of and time for payment

7.3 The financial penalty must be paid in full by YBS to the Authority by no later than 11 November 2014, 14 days from the date of the Final Notice.

If the financial penalty is not paid

7.4 If all or any of the financial penalty is outstanding on 12 November 2014, the Authority may recover the outstanding amount as a debt owed by YBS and due to the Authority.

Publicity

7.5 Sections 391(4), 391(6) and 391(7) of the Act apply to the publication of information about the matter to which this Final Notice relates. Under those provisions, the Authority must publish such information about the matter to which this Final Notice relates as the Authority considers appropriate. The information may be published in such manner as the Authority considers appropriate. However, the Authority may not publish information if such publication would, in the opinion of the Authority, be unfair to YBS or prejudicial to the interests of consumers or detrimental to the stability of the UK financial system.

7.6 The Authority intends to publish such information about the matter to which this Final Notice relates as it considers appropriate.

Authority contacts

7.7 For more information concerning this matter generally, contact Stephen Robinson at the Authority (direct line: 020 7066 1338).

Megan Forbes

Financial Conduct Authority, Enforcement and Financial Crime Division

ANNEX A

RELEVANT STATUTORY AND REGULATORY PROVISIONS

1. RELEVANT STATUTORY PROVISIONS

- 1.1 Pursuant to sections 1B and 1C of the Act, one of the Authority's operational objectives is securing an appropriate degree of protection for consumers.
- 1.2 Pursuant to section 206 of the Act, if the Authority considers that an authorised person has contravened a requirement imposed on it by the Act, it may impose on that person a penalty in respect of the contravention of such amount as it considers appropriate.

2. RELEVANT REGULATORY PROVISIONS

- 2.1 In exercising its power to impose a financial penalty, the Authority has had regard to the relevant regulatory provisions published in the Authority's Handbook. The main provisions that the Authority considers relevant are set out below.

Principles for Business ("Principles")

- 2.2 Principle 6 provides:

"A firm must pay due regard to the interests of its customers and treat them fairly."

- 2.3 Principle 3 provides:

"A firm must take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems."

- 2.4 During the Relevant Period, the following rules applied:

Mortgages and Home Finance: Conduct of Business Sourcebook ("MCOB")

- 2.5 MCOB 13.3.1R provides:

(1) A firm must deal fairly with any customer who:

- (a) is in arrears on a regulated mortgage contract or home purchase plan;
 - (b) has a sale shortfall; or
 - (c) is otherwise in breach of a home purchase plan.
- (2) A firm must put in place, and operate in accordance with, a written policy (agreed by its respective governing body) and procedures for complying with (1). Such policy and procedures must reflect the requirements of MCOB 13.3.2AR and MCOB 13.3.4AR.

2.6 MCOB 13.3.2A R provides:

A firm must, when dealing with any customer in payment difficulties:

- (1) make reasonable efforts to reach an agreement with a customer over the method of repaying any payment shortfall or sale shortfall, in the case of the former having regard to the desirability of agreeing with the customer an alternative to taking possession of the property;
- (2) liaise, if the customer makes arrangements for this, with a third party source of advice regarding the payment shortfall or sale shortfall;
- (3) allow a reasonable time over which the payment shortfall or sale shortfall should be repaid, having particular regard to the need to establish, where feasible, a payment plan which is practical in terms of the circumstances of the customer;
- (4) grant, unless it has good reason not to do so, a customer's request for a change to:
 - (a) the date on which the payment is due (providing it is within the same payment period); or
 - (b) the method by which payment is made;and give the customer a written explanation of its reasons if it refuses the request;
- (5) where no reasonable payment arrangement can be made, allow the customer to remain in possession for a reasonable period to effect a sale; and

- (6) not repossess the property unless all other reasonable attempts to resolve the position have failed.

2.7 MCOB 13.3.4A R provides:

- (1) In complying with MCOB 13.3.2AR(6): a firm must consider whether, given the individual circumstances of the customer, it is appropriate to do one or more of the following in relation to the regulated mortgage contract or home purchase plan with the agreement of the customer:
 - (a) extend its term; or
 - (b) change its type; or
 - (c) defer payment of interest due on the regulated mortgage contract or of sums due under the home purchase plan (including, in either case, on any sale shortfall); or
 - (d) treat the payment shortfall as if it was part of the original amount provided (but a firm must not automatically capitalise a payment shortfall); or
 - (e) make use of any Government forbearance initiatives in which the firm chooses to participate;
- (2) a firm must give customers adequate information to understand the implications of any proposed arrangement; one approach may be to provide information on the new terms in line with the annual statement provisions.

Dispute Resolution: Complaints (“DISP”)

2.8 DISP 1.3.1R provides:

Effective and transparent procedures for the reasonable and prompt handling of complaints must be established, implemented and maintained by:

- (1) a respondent; and
- (2) a branch of a UK firm in another EEA State.

Decision Procedure and Penalties Manual (“DEPP”)

- 2.9 Chapter 6 of DEPP, which forms part of the Authority’s Handbook, sets out the Authority’s statement of policy with respect to the imposition and amount of financial penalties under the Act.

Enforcement Guide

- 2.10 The Enforcement Guide sets out the Authority’s approach to taking disciplinary action. The Authority’s approach to financial penalties is set out in Chapter 7 of the Enforcement Guide.