

Policy Statement

# PS12/16

Financial Services Authority

## Mortgage Market Review

Feedback on CP11/31 and final rules

October 2012





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This Policy Statement reports on the main issues arising from Consultation Paper 11/31 (*Mortgage Market Review: Proposed package of reforms*) and publishes final rules.

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# Abbreviations used in this paper

<b>BIPRU</b>	Prudential sourcebook for Banks, Building Societies and Investment Firms (FSA Handbook)
<b>CBA</b>	Cost benefit analysis
<b>CCA</b>	Consumer Credit Act
<b>CP</b>	Consultation Paper
<b>CRD</b>	Capital Requirements Directive
<b>DSR</b>	Debt Service Ratio
<b>EIA</b>	Equality Impact Assessment
<b>ESIS</b>	European Standardised Information Sheet
<b>EU</b>	European Union
<b>FCA</b>	Financial Conduct Authority
<b>FPC</b>	Financial Policy Committee
<b>FSA</b>	Financial Services Authority
<b>FSB</b>	Financial Stability Board
<b>FSCP</b>	Financial Services Consumer Panel
<b>FSMA</b>	Financial Services and Markets Act 2000
<b>FTB</b>	First-time Buyer
<b>HPP</b>	Home Purchase Plan
<b>IDD</b>	Initial Disclosure Document

<b>IRB</b>	Internal Rating Based Model
<b>HNW</b>	High net worth
<b>HOLD</b>	Home Ownership for people with Long-term Disabilities
<b>KFI</b>	Key Facts Illustration
<b>LTV</b>	Loan-to-value (ratio)
<b>MCD</b>	Mortgage Credit Directive
<b>MCOB</b>	Mortgages and Home Finance: Conduct of Business sourcebook (FSA Handbook)
<b>MIPRU</b>	Prudential sourcebook for Mortgage and Home Finance Firms, and Insurance Intermediaries (FSA Handbook)
<b>MMR</b>	Mortgage Market Review
<b>PERG</b>	Perimeter Guidance Manual (FSA Handbook)
<b>PRA</b>	Prudential Regulation Authority
<b>RDR</b>	Retail Distribution Review
<b>RAO</b>	The Financial Services and Markets Act 2000 (Regulated Activities) Order 2001
<b>RTB</b>	Right-to-buy
<b>SRB</b>	Sale and rent back
<b>SVR</b>	Standard Variable Rate
<b>SYSC</b>	Senior Management Arrangements, Systems and Controls (FSA Handbook)
<b>TPA</b>	Third Party Administrator

# 1

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## Introduction

- 1.1 In December 2011, we published our proposed package of reforms for the mortgage market together with a cost benefit analysis (CBA) setting out our best estimates of the impact of our proposals (CP11/31 Mortgage Market Review: Proposed package of reforms<sup>1</sup>).
- 1.2 This Policy Statement reports on the responses to that consultation and the decisions we have reached.

### **What does this Policy Statement contain?**

- 1.3 This Policy Statement contains feedback on the responses we received to CP11/31. The main body highlights the key issues respondents raised about the proposals in CP11/31 and the decisions we have made as a result.
- 1.4 There are a number of annexes and an appendix:
- Annex 1 summarises the feedback we received to the policy questions asked in CP11/31 and our policy response;
  - Annex 2 summarises the main changes made to the draft rules in CP11/31;
  - Annex 3 restates the high-level CBA conclusions from CP11/31 and provides a regional breakdown of the impacts;
  - Annex 4 lists the non-confidential respondents to CP11/31;
  - Annex 5 contains the Equality Impact Assessment; and
  - Appendix 1 contains the amendments being made to the FSA's Handbook.<sup>2</sup>

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<sup>1</sup> CP11/31, *Mortgage Market Review: Proposed package of reforms*, (December 2011): [www.fsa.gov.uk/static/pubs/cp/cp11\\_31.pdf](http://www.fsa.gov.uk/static/pubs/cp/cp11_31.pdf)

<sup>2</sup> *Mortgage Market Review (Conduct Of Business) Instrument 2012 and Prudential Requirements For Non-Deposit Taking Lenders Instrument 2012*

- 1.5 We have also published separately an update to the Data Pack<sup>3</sup>, which was published as a supplement to CP11/31.

## Who should read this Policy Statement?

### Firms

- 1.6 You should read this Policy Statement if you are:

- a lender or other home finance provider;
- a home finance administrator; or
- a firm that advises on or arranges mortgages or other home finance products.

If you are a body that represents any of these firms, this Policy Statement will also be of interest to you.

### Consumers

- 1.7 You should read this Policy Statement if:

- you have a mortgage or other home finance product; or
- you are planning to take one out.

If you are a body that represents consumers or an interest group representing those with protected characteristics, this Policy Statement will also be of interest to you.<sup>4</sup>

## Outcome of our consultation

- 1.8 Responses to our consultation have been positive overall, with the industry welcoming the less prescriptive approach we have taken to the responsible lending requirements and acknowledging that the latest package would help achieve the MMR's overall aim of ensuring continued access to the mortgage market for the vast majority of customers who can afford it, while addressing the tail of poor mortgage lending seen in the past.
- 1.9 The entire final MMR package is summarised in Table 1 at the end of this chapter. We are taking forward, substantively unchanged, the majority of the proposals consulted on in CP11/31. This includes the removal of the non-advised sales process, the strengthened arrears charging rules, and the three key elements of the responsible lending reforms, i.e.

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<sup>3</sup> *MMR Data Pack, (October 2012):* [www.fsa.gov.uk/static/pubs/cp/mmr-datapack2012.pdf](http://www.fsa.gov.uk/static/pubs/cp/mmr-datapack2012.pdf)

<sup>4</sup> The protected characteristics are age, disability, gender, pregnancy and maternity, race, religion and belief, sexual orientation and transgender.

- **The affordability assessment:** a lender must verify income and be able to demonstrate that the mortgage is affordable taking into account the borrower's net income and, as a minimum, the borrower's committed expenditure and basic household expenditure.
- **The interest rate stress test:** the lender must also take account of the impact on mortgage payments of market expectations of future interest rate increases.
- **The interest-only rules:** the lender must also assess affordability on a capital and interest basis, unless there is a clearly understood and believable alternative source of capital repayment.

**1.10** We are also proceeding with the enhanced prudential requirements for non-deposit taking lenders ('non-banks'). In the feedback, respondents expressed a preference for standalone rules for non-banks rather than cross-referencing to the relevant existing rules for banks.<sup>5</sup> The rules made by the FSA Board are not written on a standalone basis and maintain the cross-referencing to the banking rules. However, we recognise that the banking rules, derived from EU legislation, can be complex and difficult to navigate and we will therefore continue to consider ahead of implementation how the regime could be made more accessible, while preserving delivery of the policy outcomes consulted on in CP11/31.

**1.11** Chapters 2 to 4 focus on those conduct areas where we have rethought our approach in light of the feedback. Those areas are:

- **Advice** (Chapter 2): where we clarify what we understand by regulated advice and explain that we are changing our approach to contract variations by allowing them to be completed without the need for advice, provided there is no increase in the amount outstanding under the mortgage.
- **The transitional rules** (Chapter 3): where we explain our changed approach in allowing lenders to make their own decisions about whether to make exceptions to the responsible lending rules provided there is no increase in the amount outstanding under the mortgage.
- Our approach to **high net worth and business lending** (Chapter 4): where we explain our decision not to provide a complete carve-out from the MMR proposals but instead to provide a tailored, higher-level approach for both.

**1.12** We have made one other substantive change which we explain in our response to Q14 in Annex 1. We are requiring lenders to keep **responsible lending records** for the period the mortgage remains with the lender, and not just for three years, as consulted on in CP11/31.

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<sup>5</sup> The relevant prudential rules for banks are set out in the Prudential sourcebook for Banks, Building Societies and Investment Firms (BIPRU), which forms part of the FSA Handbook: <http://fsahandbook.info/FSA/html/handbook/BIPRU>

- 1.13** Given the extensive consultation with the market previously<sup>6</sup> and the extent of consensus reached, the detail and background to the majority of the MMR reforms is not repeated in this Policy Statement. Detailed feedback to CP11/31, together with our policy response is in Annex 1. We have also summarised in Annex 2 the non-material rule changes made in light of responses and our further internal review.

### **Cost benefit analysis**

- 1.14** Respondents to the CBA included in CP11/31 felt that the estimated size of the impacts of the responsible lending proposals appeared reasonable. Annex 3 restates the high-level CBA conclusions and provides, as requested in feedback, a regional breakdown of the impacts.
- 1.15** In relation to the advice proposals, a number of respondents felt that we had underestimated the compliance costs of the removal of the non-advised sales process. We have updated our compliance cost estimate to reflect the clarifications and changes discussed in Chapter 2. The updated compliance cost estimate is in Annex 3.

### **Equality and diversity implications of the MMR**

- 1.16** The feedback to CP11/31 confirmed our analysis that none of the MMR proposals directly discriminate against any protected groups.<sup>7</sup> There are, however, some elements of our responsible lending, distribution and disclosure and niche market proposals that could cause adverse effects and possible inadvertent indirect discrimination. The detail of this and the mitigants we propose are set out in the Equality Impact Assessment at Annex 5.

### **EU and international developments**

- 1.17** In finalising our rules, we continue to pay close attention to impending European legislation. The Directive on Credit Agreements Related to Residential Property, known commonly as the Mortgage Credit Directive (MCD), is at an important stage. Both Council (representing Member States) and Parliament have now adopted views on the proposed Directive. This has allowed three-way negotiations involving the Commission, Council and Parliament to begin. Agreement through these discussions (known as a ‘trilogue’) would pave the way for the legislation. Failing that, the proposal would go through a second reading in Parliament, which might significantly extend the time before the Directive becomes law.

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<sup>6</sup> 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)

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)

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)

CP10/28, *Mortgage Market Review: Distribution & Disclosure*, (November 2010): [www.fsa.gov.uk/pubs/cp/cp10\\_28.pdf](http://www.fsa.gov.uk/pubs/cp/cp10_28.pdf)

<sup>7</sup> See footnote 4 on page 7.

- 1.18 We have been engaging with the European institutions over the possibility of a directive for many years. They have welcomed learning of the UK regulatory experience and the depth of our MMR research and analysis.
- 1.19 Many parts of the Commission's original proposal closely match MMR concerns, including the need for greater professionalism among firms, having close regard to the consumer's interests, and the need for a robust assessment of individual affordability. The changes we are making in these areas are in line with the proposed Directive.
- 1.20 In one or two respects the proposed legislation is less closely aligned with the UK proposed regulatory approach. One of these is the scope, which in the form originally proposed by the Commission would apply a standard approach to a great many niche mortgage markets (such as buy-to-let, bridging, high net worth and shared equity). Not all of these are markets that we currently regulate.
- 1.21 A second clear difference is the European proposal's greater focus on disclosure, which is likely to mean that some further rule change will be needed to introduce extra disclosure requirements. This does not mean we should not proceed with our MMR approach of re-focusing our disclosure regime on key messages, but firms should be aware that further information may be required to be given on top of this in future. In other respects, we consider that we now know enough about the likely form of the directive to finalise the MMR rules.
- 1.22 Our revised rules will also ensure UK regulation reflects key Financial Stability Board (FSB) Principles for sound mortgage underwriting.<sup>8</sup> The first two of these FSB Principles deal with assessing affordability. The MMR changes will mean that these Principles – on income verification and a reasonable debt service coverage – are clearly met. MMR requirements for lenders to have clearly documented responsible lending policies also help deliver FSB Principles requiring an implementation and supervisory framework.
- 1.23 As with the Directive, the MMR analysis has allowed us to contribute to the Principles, and ensure the approaches align.

## Implementation timetable

- 1.24 Our Board has now made the rules in Appendix 1. With the exception of MCOB11.8.1E (discussed further below), the rules will come into effect on 26 April 2014, in 18 months' time.
- 1.25 We have given careful consideration to all of the feedback received about the implementation timetable. We recognise that the cumulative impact of the MMR will lead to significant changes on the part of firms to policies, processes, systems and staff training and this will make the usual 12-month period challenging for firms, particularly the smaller firms.

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<sup>8</sup> *FSB Principles for Sound Residential Mortgage Underwriting Practices*, Financial Stability Board, (April 2012): [www.financialstabilityboard.org/publications/r\\_120418.pdf](http://www.financialstabilityboard.org/publications/r_120418.pdf)

- 1.26** We have also had regard to current market conditions. We concluded in CP11/31 that with subdued conditions persisting in the mortgage market, both the micro and macroeconomic impact of the MMR is small. This remains valid given the housing market conditions. Allowing an extra six months for implementation will not introduce significant consumer protection risks. Therefore we are giving firms 18 months to implement the MMR reforms.
- 1.27** MCOB 11.8.1E, however, comes into effect now (on 26 October 2012). This is a new evidential provision aimed at protecting those borrowers who find themselves ‘trapped’ with their current lender. We are switching this provision on with immediate effect as it is aimed at protecting not only those borrowers who may find themselves trapped in future following the implementation of the MMR, but also those borrowers who find themselves trapped today because they do not meet current tightened lending criteria. This is discussed more fully in our response to Q16 in Annex 1.

### **UK regulatory reform**

- 1.28** The FSA Board has made the rules in Appendix 1, which contain references to the FSA, to current UK financial services legislation and to other parts of the existing FSA Handbook. These references will need to be reviewed and updated to reflect the assumption of responsibility for financial services regulation by the Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA) in 2013, and to reflect any other relevant amendments to the Financial Services and Markets Act 2000 (FSMA) and to the current FSA Handbook as a result of UK regulatory reform.
- 1.29** Updated provisions will be made by the Boards of the FCA and PRA when they acquire their legal powers.

### **Next steps**

- 1.30** We are now planning a firm engagement programme for the implementation period, to help firms understand the MMR reforms, encourage firms to carefully address any systems changes that may be needed as a result of them, and to keep firms informed of the next steps in our implementation strategy.
- 1.31** We also intend to conduct a formal review of the impact of our proposals not more than five years after implementation.

**Table 1 – Summary of the MMR regulatory reform package**

<b>Mortgage Market Review</b>
<b>Key proposals consulted on and position unchanged</b>
<p><b>Responsible lending</b></p> <p><i>Lender responsible for affordability checks.</i></p> <p><i>Income to be verified in all cases.</i></p> <p><i>As a minimum, committed and basic essential expenditure to be taken into account.</i></p> <p><i>Stress testing against future interest rate increases.</i></p> <p><i>Interest-only where credible repayment strategy.</i></p> <p><b>Distribution</b></p> <p><i>All interactive sales (e.g. face to face and telephone) advised, except where the customer is a mortgage professional, or high net worth mortgage customer<sup>9</sup>, or business borrower<sup>10</sup>, where execution-only optional.</i></p> <p><i>Execution-only allowed for non-interactive sales (e.g. internet and postal).</i></p> <p><i>Requirement on intermediaries to assess affordability removed.</i></p> <p><i>Every seller required to hold a relevant mortgage qualification.</i></p> <p><i>Firms must act in the customer's best interests.</i></p> <p><b>Disclosure</b></p> <p><i>IDD replaced with a requirement for firms to disclose 'key messages' to the customer.</i></p> <p><i>The 'trigger points' for presentation of the KFI changed to reduce information overload for customers.</i></p> <p><b>Arrears management</b></p> <p><i>The number of times fees for missed payments can be charged limited.</i></p> <p><i>The arrears charges and forbearance rules widened to cover all payment shortfalls.</i></p> <p><i>The costs which can and cannot be recovered through arrears charges clarified.</i></p> <p><i>Lenders prevented from removing concessionary rates because of payment problems.</i></p> <p><b>Non-deposit taking mortgage lenders (non-banks)</b></p> <p><i>Risk-based capital requirement.</i></p> <p><i>Increase in quality of capital.</i></p> <p><i>High-level systems and controls to manage liquidity risk.</i></p> <p><i>Application on a solo-basis and not to firms in run-off.</i></p>
<b>Key proposals consulted on and position reconsidered</b>
<p><b>Responsible lending</b></p> <p><i>Transitional arrangements (see Chapter 3).</i></p> <p><i>Record-keeping requirements (see Q14 Annex 1).</i></p> <p><b>Distribution</b></p> <p><i>Need for advice in relation to post-contract variations (see Chapter 2).</i></p> <p><b>High net worth mortgage customers and business lending</b></p> <p><i>Tailored regulatory approach recognising particular lending characteristics (see Chapter 4).</i></p>

<sup>9</sup> The definition of high net worth mortgage customer has been amended. See Chapter 4.

<sup>10</sup> Business borrowers have been added as another group who can opt-out in the light of the feedback to CP11/31 (see Chapter 4)

# 2

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## Advice

### Advised sales

- 2.1 A summary of the feedback to all of the questions asked about distribution in CP11/31 and our policy responses are set out in Annex 1.
- 2.2 In this chapter, we consider two particular issues raised in the feedback:
- the boundary between providing information and giving advice; and
  - advising on contract variations.
- 2.3 This is an area where we have revised our approach in light of the feedback to CP11/31<sup>11</sup> and our subsequent discussions with respondents.

### Boundary between information provision and regulated advice

- 2.4 In CP11/31 we proposed removing the non-advised sales process and requiring that sales involving some form of ‘interactive dialogue’ between the firm and the customer should generally be advised.
- 2.5 This approach was welcomed by intermediaries and most consumer groups. However, it was a source of concern for some lenders and their representatives.
- 2.6 It is clear both from feedback to CP11/31 and our subsequent discussions with firms that there has been a misunderstanding about the scope of our advice proposals. Some firms interpreted our proposals as meaning that every customer conversation would be construed as providing regulated advice and therefore subject to our advice rules.
- 2.7 We recognise that this would have major implications for firms who use unqualified ‘pre-screeners’ to gather background information and provide general information to

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<sup>11</sup> CP11/31, *Mortgage Market Review: Proposed package of reforms*, (December 2011): [www.fsa.gov.uk/static/pubs/cp/cp11\\_31.pdf](http://www.fsa.gov.uk/static/pubs/cp/cp11_31.pdf)

customers prior to any sale commencing, as those ‘pre-screeners’ would need to be appropriately trained and qualified.

- 2.8 We did not intend that every conversation with a customer would be subject to our advice rules. The Regulated Activities Order<sup>12</sup> defines what regulated mortgage advice is, i.e. advice on the merits of the customer entering into (or varying the terms of) a particular regulated mortgage contract or contracts. As a result of this, our view is, and always has been, that where a firm steers a customer towards particular identifiable products that the customer could enter into, that is regulated advice. It is perfectly possible for a firm to have a discussion about mortgage products in general or to gather information about the customer’s general mortgage needs, without that being regulated advice.
- 2.9 The Perimeter Guidance on regulated activities connected to mortgages (PERG)<sup>13</sup> explains the distinction. Given the confusion about the boundary apparent from the feedback to CP11/31, we propose to review PERG over the course of the next year. The aim would be to ensure that any changes considered appropriate following that review would be made in time to be implemented alongside the MMR rules.

### **Contract variations by lenders**

- 2.10 The biggest challenge to our advice proposals concerned the impact on contract variations undertaken by lenders, such as rate switches, further advances, amending the term and amending the repayment type. Where we refer to contract variations we also mean new contracts with the existing lender that have the same effect.
- 2.11 Lenders and their trade bodies were concerned that all contract variations would be captured by the advice requirements and that this contradicted the near-final Approved Persons rules.<sup>14</sup> These rules explicitly exclude lender staff involved in these transactions from being Approved Persons where there is no additional borrowing. The concern was that under our advice proposals, these individuals would be required to give advice, but would not be approved to do so.
- 2.12 We agree that it would be inappropriate for this to be the case and therefore we have amended our approach to bring it into line with the Approved Persons near-final rules. We think that it is appropriate that purely administrative contract variations are undertaken on an execution-only basis, where the total sum outstanding under the mortgage will not increase. Where the total sum outstanding will increase, for example where there is a further advance, advice will be required.

12 The Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) (No. 1) Order 2003: [www.legislation.gov.uk/uksi/2003/1475/article/13/made](http://www.legislation.gov.uk/uksi/2003/1475/article/13/made)

13 <http://fsahandbook.info/FSA/html/handbook/PERG/4>

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

- 2.13** In relation to rate switches (including retention deals), we believe that requiring advice across all interactive channels is not a proportionate approach and therefore execution-only sales should be permitted in some circumstances.
- 2.14** For example, where a borrower is coming to the end of their current deal and the firm has written to them outlining all available products (without steering the borrower towards any of those products). The borrower can select the product they want and send the instructions back to the lender to make the change.
- 2.15** However, some borrowers may wish to complete the switch by telephone or in a branch. Our general approach would not allow this as a sale over the telephone or in a branch is an interactive sale and therefore advice would need to be given. However, our view is that where it is a simple product switch and nothing more, it would be acceptable for the lender to act on the borrower's instructions over the telephone, or in the branch, and proceed on an execution-only basis.
- 2.16** If the discussion with the borrower goes beyond simply acting on their instructions, however, it would become an advised interactive sale.
- 2.17** Forbearance will remain exempt from the advice requirements. We believe it is clear what constitutes forbearance and firms should refer to MCOB 13<sup>15</sup> and the guidance on mortgage forbearance<sup>16</sup> for further clarity.
- 2.18** To help demonstrate our approach, the following table outlines when firms are required to provide advice and when execution-only is permitted for typical contract variations.<sup>17</sup>

**Table 2 – The application of advice and execution-only to contract variations**

Contract variations	Advice or execution-only
<b>Rate switches</b> <b>This includes product switches and retention deals. Retention deals are usually lender driven, once the borrower comes to the end of their current product. Product switches are usually borrower driven when they will request a new product from their lender. Both have the same effect and are classed as rate switches under the final rules.</b>	
No increase in the current balance outstanding and the firm presents <b>all</b> the products for which the borrower is eligible via a non-interactive channel (e.g. in writing). The borrower selects their product via a non-interactive channel.	Execution-only
No increase in the current balance outstanding and the firm presents <b>all</b> the products for which the borrower is eligible via a non-interactive channel, but accepts the borrower's choice of product via an interactive channel.	Execution-only
No increase in the current balance outstanding, but the firm steers the borrower to a particular product or products (interactive or non-interactive).	Advice
The borrower wants to borrow more and is offered a new product.	Advice

<sup>15</sup> <http://fsahandbook.info/FSA/html/handbook/MCOB/13>

<sup>16</sup> FG11/15: *Forbearance and Impairment Provisions – 'Mortgages'*, (October 2011): [www.fsa.gov.uk/library/policy/final\\_guides/2011/fg11\\_15.shtml](http://www.fsa.gov.uk/library/policy/final_guides/2011/fg11_15.shtml)

<sup>17</sup> This table is for illustration purposes and is not an exhaustive list.

<b>Variations to existing contracts, or new replacement contracts intended to have the same effect, via an interactive channel.*</b>	
*Variations carried out on a non-interactive basis, can be offered on an execution-only basis, including where there is additional borrowing.	
<b>Further advances</b>	
This involves an increase in the current amount outstanding.	Advice
<b>Addition or removal of a party to the contract</b>	
Involving <b>no</b> increase in the current amount outstanding.	Execution-only
Involving an increase in the current amount outstanding.	Advice
<b>Change in monthly payment – (including extending term or changing the payment method)</b>	
Involving <b>no</b> increase in the current amount outstanding.	Execution-only
Involving an increase in the current amount outstanding.	Advice
<b>Porting – This involves taking the existing mortgage to a new property</b>	
Involving <b>no</b> increase in the current amount outstanding.	Execution-only
Involving an increase in the current amount outstanding.	Advice
<b>Consent to let – Allowing the borrower to let their property, which was previously owner-occupied</b>	
Involving <b>no</b> increase in the current amount outstanding.	Execution-only
Involving an increase in the current amount outstanding.	Advice

- 2.19 We are also clarifying how the responsible lending rules will apply to contract variations. This is discussed in detail in Chapter 3.

# 3

## Transitional arrangements

### Introduction

- 3.1 In this chapter we consider the transitional arrangements and the related issue of contract variations. A summary of the feedback to all questions asked about the transitional arrangements is set out under Q15 to Q19 in Annex 1.
- 3.2 This is an area where we have revised our approach in light of the feedback to CP11/31<sup>18</sup> and our subsequent discussions with respondents.

### Transitional arrangements and contract variations

- 3.3 In CP11/31 we proposed some transitional arrangements designed to mitigate the impact of the new responsible lending rules on existing borrowers who:
- cannot demonstrate affordability for their new mortgage as required by the new affordability requirements; or
  - do not have an acceptable repayment strategy, according to the new interest-only requirements.
- 3.4 We proposed several conditions that would have to be met for the borrower to qualify for the transitionals.<sup>19</sup>
- 3.5 The vast majority of respondents agreed that we should take steps to mitigate the impact of our responsible lending proposals on borrowers. However, most respondents felt that, as drafted, the proposals were too restrictive to help many borrowers and too complex to be widely adopted by lenders.

<sup>18</sup> CP11/31, *Mortgage Market Review: Proposed package of reforms*, (December 2011): [www.fsa.gov.uk/static/pubs/cp/cp11\\_31.pdf](http://www.fsa.gov.uk/static/pubs/cp/cp11_31.pdf)

<sup>19</sup> See the eligibility criteria set out at paragraph 3.358 in CP11/31.

- 3.6 We agree that it would benefit borrowers to have more flexibility than was permitted in the original proposals. For example, we can see that borrowers may benefit from taking on higher payments to fix their rate in periods where interest rates are expected to rise. Similarly, we can see that they may benefit from some material variations to a mortgage, such as a change in term.
- 3.7 We have amended the rules. The final rules:
- simplify when an affordability assessment is required for all existing borrowers when they make changes to their existing mortgage – either as a contract variation, or as a new replacement contract;
  - only require an affordability check where there is additional borrowing, or a material impact on affordability; and
  - simplify the transitional arrangements, to make them more flexible and more practical. In particular, we are allowing lenders to make their own assessment about making exceptions to the affordability and interest-only rules.

### **Existing borrowers – contract variations and new regulated mortgage contracts**

- 3.8 Under both our existing rules and the MMR proposals, an affordability assessment is required whenever a lender enters into a regulated mortgage contract with a customer, whether or not there is an impact on affordability. For example, an affordability assessment is required when a customer moves to a new rate with their existing lender, if the transaction is structured as a new mortgage contract, even where they are not borrowing any more money. By contrast, an affordability assessment is not required for the same transaction if it takes effect through a contract variation, even where there might be a material impact on affordability.
- 3.9 To address this, we have amended the rules so that an affordability assessment is not required for an existing borrower, staying with their existing lender, if there is no increase in the current amount outstanding (i.e. no additional borrowing) – unless there is a material impact on affordability. This is the case whether the transaction takes effect through a contract variation, or a new regulated mortgage contract.
- 3.10 So, for example, an affordability assessment will not be required for a change that does not have a material impact on affordability, such as a rate switch or retention deal; or where the borrower is porting their mortgage or moving to a new property (with no increase in the current amount outstanding).
- 3.11 However, an affordability assessment will be required where there is additional borrowing, or there is deemed to be a material impact on affordability. Whether a change has a material

impact on affordability will vary according to the circumstances of the case. We will assume, in the absence of evidence to the contrary, that the following changes are likely to be material:

- extending the term of the loan beyond the borrower's expected retirement;
- changing the repayment type; or
- removing a party to the contract.

**3.12** This approach is consistent with our approach to advice and contract variations, as discussed in Chapter 2.

**3.13** These changes to the rules will mean that the transitional arrangements are required in many fewer situations.

### **The revised approach to transitional arrangements**

**3.14** Despite this change, there will be situations where the responsible lending rules continue to bite for existing borrowers. This includes where:

- there are material changes to affordability (such as those set out in paragraph 3.11 above);
- the borrower does not have an acceptable repayment strategy for an interest-only mortgage; or
- the borrower wishes to move their mortgage to another lender.

**3.15** We recognise that in such scenarios, while an affordability assessment should apply because there may be a material impact on affordability, there may be some situations where, due to extenuating circumstances, such a change may be in the interests of the borrower and lead to a better outcome than remaining in their current situation. We also recognise that it is not possible for us to predict every such circumstance in the rules.

**3.16** Therefore, our revised approach allows lenders flexibility to make their own decisions about making exceptions to the **affordability and interest-only rules** for existing borrowers. This will apply whether or not it materially affects affordability, as long as:

- there is **no increase in the current amount outstanding** (i.e. no additional borrowing), except product or arrangement fees, which may be added to the mortgage balance (firms are reminded of the new provisions that will apply when adding fees or charges to a loan<sup>20</sup> (MCOB 4.6A); and also our existing rules on excessive charges (MCOB 12.5)); and
- the lender has judged that the proposed transaction **is in the customer's best interests**.

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<sup>20</sup> See paragraphs 5.121 to 5.130 in CP11/31.

- 3.17** These transitional arrangements will be able to be used by lenders to take on borrowers from other lenders.
- 3.18** We have considered whether additional borrowing should be allowed under the transitional arrangements. A few respondents to CP11/31 supported this. However, we cannot see a way to control the gaming issues that would arise, or the opportunity for borrowers to take on mortgage commitments which they cannot afford, which would defeat the objective of our responsible lending rules. We are not, therefore, allowing additional borrowing.
- 3.19** There is one exception to this. Where the additional funds are being advanced by the existing lender for essential repairs or maintenance work to the property, we are allowing this, subject to certain criteria, including that:
- the value of the property is at risk if the repairs or maintenance work are not carried out;
  - the additional borrowing is to be used for the repairs or maintenance work; and
  - the firm has credible evidence of the cost of the repairs or maintenance work.
- 3.20** The aim of the transitional arrangements is to help existing borrowers who are being prevented from borrowing because of the stricter MMR requirements. We are therefore retaining an eligibility condition, which states that the transitional arrangements will not apply where a borrower has, since the implementation of the MMR, taken on additional borrowing and increased the size of their mortgage (other than to finance any relevant product or arrangement fee, or essential repairs or maintenance work). This is to prevent the transitional arrangements being used where the inability to meet lending criteria is a result of changed circumstances or real underlying affordability issues and not the MMR.
- 3.21** The transitional arrangements apply to existing borrowers who have a mortgage in place when the MMR rules come into force. We have amended the transitional arrangements to make it clear that they also apply to borrowers with mortgages that were entered into before the introduction of mortgage regulation in 2004 (MCOB 11.7.1R(1)(a)).
- 3.22** We already indicated in CP11/31 that we will expect lenders to have robust systems and controls around the use of the transitional arrangements. As a result of our amended approach, we also expect firms to include:
- an exceptions policy, which should form part of the lender's wider responsible lending policy;
  - record keeping, including a record of the rationale behind each lending decision made under the transitional arrangements; and
  - producing clear management information to monitor the application of these exceptions.
- 3.23** Table 3 illustrates the circumstances where an affordability assessment is required for a post-sale contract variation, and where the transitional arrangements apply.

**Table 3 – Existing borrowers – affordability assessments and transitional arrangements**

Post-sale variations	Responsible lending requirements
<b>When is an affordability assessment required (for a variation to an existing contract, or a new replacement contract intended to have the same effect with the existing lender)?</b>	
<b>Full requirements are set out in MCOB 11.6</b>	
<b>Rate switches</b>	
This includes product switches and retention deals. Retention deals are usually lender driven, once the borrower comes to the end of their current product. Product switches are usually borrower driven, when they will request a new product from their lender. Both have the same effect and are classed as rate switches under the final rules.	
Involving no increase in the current amount outstanding.	No affordability assessment is required (even if the rate switch results in higher payments).
Involving an increase in the current amount outstanding.	An affordability assessment will be required.
<b>Further advances</b>	
Involving an increase in the current amount outstanding.	An affordability assessment will be required.
<b>Addition or removal of a party to the contract</b>	
Involving no increase in the current amount outstanding.	This is likely to be a material change, and if so an affordability assessment will be required.
Involving an increase in the current amount outstanding.	An affordability assessment will be required.
<b>Changes that have a material impact on affordability (e.g. extending term beyond expected retirement, or changing the payment method)</b>	
Involving no increase in the current amount outstanding.	An affordability assessment will be required.
Involving an increase in the current amount outstanding.	An affordability assessment will be required.
<b>Porting – This involves taking the existing mortgage to a new property</b>	
Involving no increase in the current amount outstanding.	No affordability assessment is required.
Involving an increase in the current amount outstanding.	An affordability assessment will be required.
<b>Forbearance</b>	
An affordability assessment is not required for a variation made solely for the purposes of forbearance (as per MCOB 11.6.3R(3)).	Not applicable.

Transitional arrangements	Responsible lending requirements
<p><b>When can the transitional arrangements be applied (for a variation to an existing contract, a new replacement contract intended to have the same effect, or a new contract with the same or a different lender)?</b></p> <p><b>Full requirements are set out in MCOB 11.7.</b></p>	
<p>Involving <b>no</b> increase in the current amount outstanding (whether or not there is a material impact on affordability).</p>	<p>The transitional arrangements may be applied.</p>
<p>Involving an increase in the current amount outstanding (except for essential repairs or maintenance work).</p>	<p>An affordability assessment <b>will be</b> required, so the transitional arrangements cannot be applied.</p>

# 4

## High net worth and business lending

### Lending to high net worth customers

- 4.1 In CP10/16<sup>21</sup>, we indicated that this could be a market where our approach to affordability may need to vary. Almost all respondents thought that high net worth (HNW) customers would benefit from an alternative approach because of the complex nature of their incomes and the potentially short loan terms (typically five years).
- 4.2 In CP11/31<sup>22</sup>, we therefore proposed some tailoring for HNW customers, including:
- permitting HNW customers to opt-out of advice;
  - making provision for interest roll-up mortgages; and
  - a tailored approach to disclosure.
- 4.3 We have also been considering whether a more fundamental change in our approach to HNW customers would be appropriate, including considering whether our regime should apply at all to those customers with higher levels of income or wealth, on the basis that it is perfectly reasonable for these customers to take greater risks and that regulation is not needed to protect them from the decisions they make. While they still ultimately face the loss of their home, they are more likely to have access to a range of professional advisers, and will have more options available to them in the event that they experience financial difficulties – for example, by downsizing rather than becoming homeless. So we asked an open question in CP11/31 about whether it would be appropriate to allow some form of carve-out from mortgage regulation.
- 4.4 We suggested that there might be two ways to do this – either by completely disapplying the mortgage rules or by allowing HNW customers to elect whether to forgo the protection of the rules.

21 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)

22 CP11/31, *Mortgage Market Review: Proposed package of reforms*, (December 2011): [www.fsa.gov.uk/static/pubs/cp/cp11\\_31.pdf](http://www.fsa.gov.uk/static/pubs/cp/cp11_31.pdf)

## Feedback to CP11/31

- 4.5 As we explain in more detail in Annex 1, most respondents to the consultation recognised that HNW customers merit a different regulatory approach to that proposed for the mainstream mortgage market. There was some limited support for an approach that would allow HNW customers to opt-out of mortgage regulation, although firms operating in this sector felt that this approach would be difficult to operate in practice.
- 4.6 However, many respondents felt that wealth does not necessarily equate to financial capability, and did not agree that customers with a greater degree of wealth would necessarily make sound financial decisions. They were therefore cautious about completely disapplying the protection of the mortgage rules.
- 4.7 However, many respondents involved in lending to HNW customers felt that the MMR proposals (and some aspects of existing MCOB requirements) did not fit well with the bespoke service offered to many HNW customers, and therefore would need to be amended. For example:
- firms would not generally consider it necessary or appropriate to drill down into the details of basic expenditure, such as utility bills and council tax, for very wealthy customers; and
  - wealthy customers tend to be very asset-rich, and mortgage payments may be serviced through these assets (including through their sale).

## Our approach to high net worth mortgage customers

- 4.8 We recognise that applying all the MMR proposals, particularly the full affordability checks, is not proportionate for very wealthy customers and that a different regulatory approach is appropriate. However, there has not been strong support for carving HNW customers out of mortgage regulation completely.
- 4.9 The approach we are taking, therefore, aims to recognise the characteristics of lending to HNW customers, by applying higher-level requirements than for mainstream mortgages. This will be based on the following key elements:
- **Disclosure** – A tailored approach will apply, as proposed in CP11/31.
  - **Advice** – Interactive sales may be conducted on an execution-only basis.
  - **Responsible lending** – Requirements will be set at a higher level than for mainstream mortgages.

*The definition of a high net worth mortgage customer*

- 4.10** To appropriately apply any of these elements, we first need to define who we consider to be a ‘high net worth’ customer.
- 4.11** In CP11/31, we proposed to define a HNW customer as having a minimum net annual income of £1m or minimum net assets of £3m.
- 4.12** As we explain in Annex 1, respondents broadly agreed with the proposed definition for net assets, but did not agree with the proposed definition of net annual income, as they thought £1m was much too high.
- 4.13** In response to feedback (as discussed in Annex 1, Q81) in we have amended the income part of the definition to a net income of £300,000. Therefore, we are defining a HNW mortgage customer as a customer with a minimum annual net income of £300,000, or minimum net assets of £3m.
- 4.14** This definition applies to the customer applying for the mortgage but it is also met where the obligations of that customer are guaranteed by a person who satisfies the income or assets criteria.
- 4.15** We are not being prescriptive about what assets can be taken into consideration in making up the minimum net asset figure of £3m. It is up to the lender to decide this. Therefore it would be possible for the mortgaged property to be included in the total (net of any outstanding mortgage).
- 4.16** Where there is more than one applicant, at least one of the applicants must meet the definition in their own right (as per MCOB 1.2.3BR). This means that the income or assets of two or more applicants cannot be added together to meet the definition and thereby circumvent the responsible lending rules that would otherwise apply.
- 4.17** Where assets are held jointly (such as may happen in the case of property), a lender should consider the value of the customer’s actual share of assets.<sup>23</sup>
- 4.18** We are aware that we have recently published a Consultation Paper<sup>24</sup> on restrictions on the retail distribution of unregulated collective investment schemes and close substitutes. In this paper, we refer to secondary legislation that allows financial promotions to be exempt from Financial Services and Markets Act 2000 (FSMA) marketing restrictions if certain conditions are met.<sup>25</sup> Exemptions are available in the legislation for customers who are certified as ‘high net worth individuals’.<sup>26</sup> Among the criteria for customers to be

<sup>23</sup> In the case of a property held by ‘joint tenants’ both owners are deemed to own 100% of the value of the property. Therefore, the full value of the asset could be considered for the purposes of an individual meeting the definition of a HNW mortgage customer. If the property is held by tenants in common, the actual proportion of the individual’s share of the property could be considered.

<sup>24</sup> CP12/19, *Restrictions on the retail distribution on unregulated collective investment schemes and close substitutes*, (August 2012): [www.fsa.gov.uk/static/pubs/cp/cp12-19.pdf](http://www.fsa.gov.uk/static/pubs/cp/cp12-19.pdf)

<sup>25</sup> The Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (FPO) and the Financial Services and Markets Act 2000 Promotion of Collective Investment Schemes (Exemptions) Order 2001(PCIS Order). The exemptions in these Orders are determined by HM Treasury.

<sup>26</sup> See article 48 of the FPO and article 21 of the PCIS Order.

categorised as high net worth under the orders are having an annual income of more than £100,000 or having investable net assets of more than £250,000.

- 4.19** We are choosing to apply a different definition of HNW in the mortgage market. HNW customers face the same risks when they take out a loan secured against their homes as any other customer. This includes the risk that they may ultimately lose their home. When setting the scope of mortgage regulation in 2004, the then government was not persuaded that a specific exemption for HNW customers was required and felt that they should be afforded the same protections as any other customer. Our current mortgage rules reflect this and apply to all regulated mortgage contracts, including those taken out by HNW customers.
- 4.20** Our changed approach, in the light of the market feedback, recognises that there is a very small subset of genuinely wealthy customers, whose wealth is significantly above average. This level of wealth gives these customers specific advantages, in particular, a considerably reduced risk of becoming homeless in the event that they experience financial difficulties. The HNW definition for mortgages will therefore exclude most customers, and will ensure that the tailoring is targeted at the most wealthy.<sup>27</sup>
- 4.21** To make the distinction clearer between the HNW definition that applies in relation to the mortgage rules and the HNW definitions used elsewhere in the FSA's Handbook, we have amended the defined term from 'high net worth customer' to 'high net worth mortgage customer'.
- 4.22** In CP11/31 we proposed that, before a firm could treat a customer as being HNW, they should obtain a written statement from a suitably qualified professional adviser to confirm that the customer meets the definition of a HNW mortgage customer. In response to feedback, we have amended this requirement (see MCOB 1.2.9CR(1)), to allow firms also to use evidence that they have obtained through their business relationship with the customer, for example, if they manage their assets.

### *The application of the new approach*

- 4.23** The tailoring that we proposed for lending to HNW mortgage customers for disclosure (MCOB 4.9, 5.7, 6.7, 7.7 and 13.7) and charges (MCOB 12.6) is proceeding on the basis consulted on in CP11/31. Firms may decide to either comply with MCOB in full, or to use the tailored approach, but not to mix and match, on the basis that it would be very confusing for a borrower.
- 4.24** We are applying a different approach for the new advice and responsible lending provisions for HNW mortgage customers. A firm may decide when to use these provisions independently of whether they adopt the tailored provisions for disclosure and charges. This is because we cannot see how a firm's approach to disclosure (which might be purely driven by systems or process considerations) should determine whether a lender can apply the new

<sup>27</sup> We estimate that borrowers with a net income of £300,000 accounted for around 0.2% of mortgage sales in 2011. See Exhibit 22.6 in MMR Data Pack (October 2012).

provisions for advice or responsible lending. Therefore a firm may choose different approaches to the disclosure and charges tailoring, and the advice and responsible lending provisions for HNW mortgage customers.

### *Advice*

- 4.25 As proposed in CP11/31, we are allowing a HNW mortgage customer to get a mortgage on an execution-only basis, even where the sale is interactive – provided the customer has confirmed in writing that they are aware of the consequences of losing the protections of the rules on suitability, and have made a positive election to proceed with an execution-only sale.
- 4.26 Many HNW mortgages are not commoditised in the same way as residential mortgages, so the structure of the deal and the interest rate may vary according to the individual circumstances of the customer. Therefore, it will not always be possible for a HNW mortgage customer to provide the product details that we would normally require for an execution-only sale, such as the rate of interest and the interest rate type. We have amended the rules for HNW mortgage customers so that they do not have to provide this information to purchase a product on an execution-only basis.
- 4.27 Unlike customers in the mainstream mortgage market, HNW mortgage customers are not required to get advice in the unlikely event that they fall into one of the vulnerable categories (i.e. debt consolidation, right-to-buy, equity release or sale and rent back). This is because of the greater resources available to HNW mortgage customers and the likelihood that they will have access to the services of other professional advisers.

### *Responsible lending*

- 4.28 The lender is required to assess whether the customer will be able to pay the sums due (to cover the sums advanced and the interest) and demonstrate that it is affordable for the customer, as required by the main overarching responsible lending rule (MCOB 11.6.2R). However, the rules beneath this do not drill down into the same level of granular detail as for mainstream mortgages, giving the lender some flexibility to meet the requirements in a way that is appropriate for the customer.
- 4.29 When making their assessment of affordability for HNW mortgage customers, the lender may base their assessment on both the income and the assets of the borrower. They must also consider the expenditure of the borrower, by considering whether they will have sufficient resources to cover their credit commitments, basic essential expenditure and basic quality of living costs.<sup>28</sup> However, we are not prescriptive about how they do this, and expenditure can be considered in general terms (i.e. it may be possible for a lender to develop a general approach applied across customers or particular groups of customers).

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<sup>28</sup> We are retaining the use of the terms ‘basic essential expenditure’ and ‘basic quality of living costs’ for business lending and lending to HNW mortgage customers. While developed for use in our rules for mainstream mortgages, we believe their use in business and HNW lending will be helpful for firms in understanding the types of expenditure that we expect them to consider.

- 4.30 In addition, the lender will be required to:
- obtain evidence of the income and/or assets that they are basing their affordability assessment on;
  - take account of the impact of likely future interest rates on affordability; and
  - take account of known or likely future changes to the income and expenditure of the customer.
- 4.31 The interest-only rules continue to apply in their entirety, because we believe that the interest-only rules are flexible enough to be adapted to the needs of different types of customers, including HNW mortgage customers.
- 4.32 The requirement to have a responsible lending policy, and record keeping and monitoring apply in full, subject to some minor amendments to reflect the revised approach to responsible lending.
- 4.33 As we discuss further at Q70, Annex 1, a specific exception has been made for secured overdrafts for HNW mortgage customers from the rules around extending the terms of a bridging loan (MCOB 11.6.55R).

### *Disclosure*

- 4.34 We have made some small adjustments to the disclosure rules in light of the amended approach to execution-only sales for HNW mortgage customers (see MCOB 5.4.18BR). These set out when a firm must provide a KFI, and when a customer has to be told they can request one.

## **Business lending**

- 4.35 In CP11/31, we proposed to read across the majority of the MMR proposals to business lending (i.e. regulated mortgage contracts made for a business purpose), but proposed a limited amount of tailoring, including rules in relation to interest roll-up mortgages and professional standards.
- 4.36 We also asked a wider question about whether it might be appropriate to carve out business loans from our proposed new regime entirely. There is an argument that if a business borrower and lender want to take an informed risk, and the business borrower is happy to use their home as collateral for a business venture, then why should that individual be prevented from doing so? However, we must also consider those who are less able to protect their own interests and who arguably do need regulatory protection – such as a sole trader borrowing against their home as a last resort to keep their business afloat.

- 4.37 So a key question for us was how would we draw a line between those small business borrowers who can take a risk, and should be allowed to do so, and those who cannot? Also, how would we prevent any potential carve-out from being exploited as a means of avoiding our new affordability requirements?
- 4.38 We asked for feedback on these questions and also had a number of discussions with lenders active in regulated business lending to help inform our policy approach.

### **Feedback to CP11/31**

- 4.39 As we set out at Q89 in Annex 1, respondents' views on a carve-out were polarised. Lenders and trade bodies strongly supported some form of carve-out. But consumer representatives were very concerned about the risks this would pose.
- 4.40 Consumer representatives were not convinced that potential business borrowers would always take an informed business risk, particularly where the boundary between their personal and business finances is blurred, as it might be when lending is secured on personal assets to raise business capital.
- 4.41 In addition, they had strong concerns about the risk of gaming, as customers might claim that they are borrowing for a business purpose to avoid the strengthened regime put in place through the MMR.
- 4.42 In contrast, representatives from the industry thought that business borrowers are better able to make financial decisions. They felt that the MMR proposals would not be easily transferable to business lending, as they do not reflect the way that business banking works in practice, i.e. where the focus of underwriting is the circumstances of the business, and the ability of the business to repay the loan. They also felt that application of the full set of MMR proposals to business lending would be disproportionately onerous, given the very small proportion of business lending that is regulated, and would not add any significant benefit to these customers.

### **Our approach to business lending**

- 4.43 We recognise that the full package of MMR proposals is not workable for business lending and that, to a large extent, business borrowers have higher levels of financial capability than consumers in general.
- 4.44 However, we have not been convinced that business lending should be entirely carved out of mortgage regulation.
- 4.45 Our view is that some business borrowers, particularly some of the smaller business borrowers who are captured by mortgage regulation, do need consumer protection when putting their homes at risk, and we cannot see how gaming would be prevented if business lending was completely carved-out of mortgage regulation. While we accept that much of current business lending practice is prudent in today's constrained market, we see a clear

risk of gaming developing if we were to disapply our regime completely. Particularly outside the traditional business banking environment, where lenders may see opportunities to increase market share through bypassing our affordability assessments.

- 4.46 We have therefore not carved business lending out of our mortgage regime. However, we have applied an alternative approach, which recognises the characteristics of business lending where this differs from mainstream residential mortgages. This approach will be based on the following key elements:
- **Disclosure** – The existing rules are tailored for business loans and that tailoring will continue.
  - **Advice** – Interactive sales may be conducted on an execution-only basis.
  - **Responsible lending** – Requirements are set at a higher level than for mainstream mortgages, and recognise that a mortgage may be repaid from the resources of a business.

#### *The application of the new approach*

- 4.47 Reflecting the fact that business borrowing is likely to be individually negotiated and so sits poorly with the standard approach to disclosure, our existing rules are specially tailored where the regulated mortgage contract is for a business purpose. This relates mainly to disclosure requirements (as set out in MCOB 4.9, 5.7, 6.7, 7.7 and 13.7) and to charges (MCOB 12.6). We are not changing these requirements, or the situations where they can be used. We currently require a firm to either comply with MCOB in full, or use the tailored approach in its entirety for any particular regulated business loan. This means that a firm cannot mix and match whether they use the tailored provisions or full MCOB requirements as this would be very confusing for a borrower. This approach continues for these existing tailored provisions.
- 4.48 We are, however, applying a different approach for the new advice and responsible lending provisions. These provisions apply only where the loan is **solely** for a business purpose. Examples where this might apply include:
- raising a loan solely for a business purpose on a customer's previously unencumbered home;
  - taking a further advance that is solely for a business purpose (even though the main mortgage may have been taken out for the purchase of the home, or other personal use, such as home improvements or debt consolidation); and
  - remortgaging to raise additional funds, as long as the additional funds are being raised solely for a business purpose (even though the existing outstanding mortgage balance may have been taken for purchase of the home or other personal use).

- 4.49 The new provisions will not include the following scenarios, where there is an element of personal use to the loan, and where the full MCOB requirements for advice and responsible lending will therefore apply:
- remortgaging for several purposes, e.g. debt consolidation and a business purpose; or
  - taking a further advance for several purposes, e.g. home improvements and a business purpose.
- 4.50 As with our existing tailored approach, we do not capture buy-to-let finance under the business lending rules. We do not regulate mortgages secured on buy-to-let properties. In cases where a regulated mortgage contract is secured on the borrower's home to finance the purchase of a single buy-to-let property, there is already existing guidance (MCOB 1.2.5G(2)), which states our opinion that this would not be for a business purpose and therefore falls under the main affordability rules.
- 4.51 The use of these provisions is not dependent on whether the firm is using the existing tailored approach for business loan disclosure. This is because we cannot see how a firm's approach to disclosure (which might be purely driven by systems or process considerations) should determine whether a lender can apply the new provisions for advice or responsible lending. Therefore, a firm may decide to apply the advice and responsible business lending provisions whether or not they apply the tailored disclosure provisions. We include guidance on this in the rules (see MCOB 1.2.4BG).
- 4.52 It will still be up to a firm to determine whether a loan is for a business purpose (as set out in MCOB 1.2.5G(2)). To prevent gaming of the new provisions for advice and responsible lending, we require a firm to have sight of a credible business plan before determining whether the loan is solely for a business purpose (MCOB 1.2.9DR). The aim of this requirement is for the firm to assess whether there is a legitimate business proposition that has not been fabricated for the reason of obtaining mortgage finance for other (i.e. personal) reasons – rather than for underwriting purposes (although we recognise that in practice the same business plan may also be used by the lender when assessing affordability).

### *Advice*

- 4.53 We have amended the rules to allow loans solely for a business purpose to be obtained on an execution-only basis, even in interactive sales, as for HNW mortgage customers and mortgage professionals. The customer must confirm in writing that they are aware of the consequences of losing the protections of the rules on suitability, and make a positive election to proceed with an execution-only sale.
- 4.54 Many business loans are not commoditised in the same way as residential mortgages, so the structure of the deal and the interest rate may vary according to the circumstances of the individual transaction. So it will not always be possible for a business borrower to specify the product details that we would normally require for an execution-only sale, such as the rate of interest and the interest rate type. Therefore, where the loan is solely for a business

purpose, we are not requiring this information to be given before proceeding with an execution-only sale.

- 4.55 Unlike HNW mortgage customers, business borrowers are required to get advice if for some reason they also fall into one of the vulnerable categories (i.e. debt consolidation, right-to-buy, equity release or sale and rent back). This situation is relatively unlikely to occur (given that the purpose of the loan must be solely for a business purpose), but if it does, our view is that the borrower should receive advice, given that the loan will be secured against their home.

### *Responsible lending*

- 4.56 We have applied a different approach to assessing affordability for loans solely for a business purpose. The main, over-arching responsible lending rule (MCOB 11.6.2R) will still apply, requiring the lender to assess whether the customer will be able to pay the sums due, and to demonstrate that the mortgage is affordable for the customer. However, the affordability rules beneath this will not drill down into the same granular detail as for mainstream mortgages, giving the lender appropriate flexibility in their underwriting of business loans.
- 4.57 When a mortgage is being raised for a business purpose, we recognise that the loan may be repaid from:
- the resources of a business; or
  - the personal resources of a borrower (e.g. if funds are being raised for a new business venture).
- 4.58 We are accommodating both of these situations in the rules.
- 4.59 Where the loan is being repaid through the resources of a business, we require the lender to assess whether that business will be able to repay the mortgage. We are not being prescriptive about how the lender should do this, and the rule just requires the lender to base this assessment on the strength of the resources of the business (MCOB 11.6.26R(2) (b)). This may include consideration of factors such as cash flow, assets and liabilities.
- 4.60 If the borrower is reliant on the business for their personal income, then we require the lender, as a minimum, to consider in general terms whether a business can support the borrower's basic essential and basic quality of living costs.<sup>29</sup> We are not being prescriptive about how the lender does this, and we are being clear in the rules that this can be done in general terms. Therefore, it may be possible for a lender to develop a general approach applied across borrowers, or across particular groups of borrowers. Alternatively, they might consider how much the borrower draws from the business for their personal use.

<sup>29</sup> We are retaining the use of the terms 'basic essential expenditure' and 'basic quality of living costs' for business lending and lending to HNW mortgage customers. While developed for use in our rules for mainstream mortgages, we believe their use in business and HNW lending will be helpful for firms in understanding the types of expenditure that we expect them to consider.

- 4.61** Where the loan is being repaid through the personal resources of the borrower, the lender must make their assessment of affordability through an assessment of the income, assets and committed expenditure of the borrower, and a general consideration of their basic essential expenditure and basic quality of living costs. Once again, we are not being prescriptive about how the lender should do this.
- 4.62** In addition, whether the mortgage will be repaid by business or personal resources, the lender is also required to:
- obtain evidence of the income or assets of the borrower, or the resources of the business;
  - take account of the impact of likely future interest rates on affordability; and
  - take account of known or likely future changes to the financial position of the business.
- 4.63** The interest-only rules continue to apply in their entirety, because we believe that they are flexible enough to be adapted to the needs of different types of customers, including those borrowing for business.
- 4.64** The requirement to have a responsible lending policy, and record keeping and monitoring, still apply in full, subject to some minor amendments to reflect the revised approach to responsible lending.
- 4.65** As we discuss further at Q70 in Annex 1, we have made a specific exception for secured overdrafts that are solely for a business purpose from the rules around extending the terms of a bridging loan (see MCOB 11.6.55R).

### *Disclosure*

- 4.66** We have made some small adjustments to the disclosure rules in light of the amended approach to execution-only sales for business lending (see MCOB 5.4.18BR(2)). These set out when a firm must provide a KFI, and when a customer has to be told they can request one.

## Annex 1

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# Detailed feedback on CP11/31

### Introduction

1. In this Annex we summarise the feedback received to our proposals in CP11/31<sup>1</sup> and set out our policy response. Feedback to some of our distribution proposals is discussed in detail in Chapter 2. Feedback to our proposed transitional arrangements is in Chapter 3. Feedback to our proposed approach to high net worth and business lending is in Chapter 4.

### Responsible lending and borrowing

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

2. The majority of respondents agreed in theory that anti-fraud controls should be incorporated into firms' responsible lending policies.
3. However, many lenders were concerned about including detailed information on their anti-fraud controls in what is a fairly widely circulated document, as this could actually facilitate fraudsters' understanding of how to get around fraud controls. They therefore felt that lenders should be able to keep details of their anti-fraud controls separately from their responsible lending policies, and out of the public domain.

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<sup>1</sup> CP11/31, *Mortgage Market Review: Proposed package of reforms*, (December 2011): [www.fsa.gov.uk/static/pubs/cp/cp11\\_31.pdf](http://www.fsa.gov.uk/static/pubs/cp/cp11_31.pdf)

## Our response

We want to ensure that lenders are joined up in the way they think about fraud, and explicitly consider fraud in the context of their underwriting processes.

However, we recognise that it may not be appropriate to widely circulate the details of anti-fraud controls. Therefore we have amended the rules (MCOB 11.6.20R) to allow the responsible lending policy to be set out in more than one document. This would allow cross reference to a separate document with a more restricted circulation.

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### Q2: *Do you have any comments on our income proposals?*

4. The majority of respondents were in favour of the proposals, supporting what they saw as a sensible and proportionate approach that provides lenders with an appropriate level of flexibility to income. Many lenders also welcomed the recognition of the role of electronic data and the removal of references to human intervention as a requirement in the income verification process.
5. A small group of lenders supported the continuation of 'fast-tracked' mortgages and expressed disappointment that income verification would be required across the board.
6. Some consumer representatives had concerns that the flexibility allowed in the rules could be exploited by firms to avoid undertaking a rigorous assessment of income. They also had concerns about the robustness of lenders' automated processes and risks around allowing the consideration of projected income.
7. While most respondents thought that the rules themselves would not necessarily affect the availability of mortgages to particular consumer groups, several noted the need for lenders to show a flexible approach to customers with 'non-standard' income, such as self-employed customers or contractors. However, many were concerned that uncertainty about the future supervisory approach might result in lenders adopting an overly cautious approach to such cases.
8. Several lenders thought that lenders who do not hold current accounts (mainly smaller lenders) would be at a competitive disadvantage, because they would not be able to evidence income from their own internal sources. In addition, they may not be able to access some sources of electronic income data – e.g. if bank account turnover data held by credit reference agencies is only available on a reciprocal basis, i.e. to firms who themselves supply this data to the agencies.

### Our response

We believe we have struck an appropriate balance of flexibility in the income proposals. We are therefore proceeding with the rules largely unchanged, other than some minor amendments and clarifications.

In relation to the concerns raised about supervision, we are carrying out internal training for supervisors and extensive firm engagement and education to ensure a consistent understanding of the rules.

We do not believe that implementing the income rules will significantly change the competitive situation of smaller lenders. Those lenders with current accounts can already use their own data to evidence income for their existing customers, and most smaller lenders already collect evidence of income, whether provided by the customer or an intermediary.

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

9. The expenditure proposals were welcomed by most respondents, who supported the move away from ‘free disposable income’, as proposed in CP10/16, to what they considered a more balanced, proportionate and practical approach. Several respondents, including a trade body, noted that many lenders will be able to comply with these proposals without making significant changes to their existing practices.
10. However, some trade bodies and lenders felt that this may be more difficult for smaller lenders, who may have less sophisticated systems, and less customer data available to base expenditure assumptions on. This again led to concerns that larger lenders will have an unfair competitive advantage.
11. Uncertainty over the future supervisory approach was noted, with firms reiterating concerns that this would result in lenders taking an overly conservative approach, assuming unnecessarily high levels of expenditure, which could unnecessarily restrict the amount creditworthy customers are able to borrow.
12. Several consumer representatives argued that we should adopt a more prescriptive approach to the types and levels of expenditure to be considered, for example, by requiring these to be set with reference to some form of external benchmark. They felt this would ensure a more consistent approach between lenders and reduce the potential for lenders to compete by using deliberately low expenditure assumptions.
13. In contrast, one consumer representative argued that the affordability assessment should either not include any allowance for basic quality of living costs, or confine the allowance

to a small percentage on top of basic essential expenditure. They thought the proposals might harm the borrowing opportunities of responsible and creditworthy customers, by taking account of discretionary spending that could be curtailed to repay the mortgage.

14. Some consumer representatives highlighted the potentially significant costs of childcare and suggested that they should be moved into the category of basic essential expenditure, rather than basic quality of living costs.

### Our response

Given the support received, we are proceeding with the proposed expenditure approach, subject to some minor amendments to improve the clarity of the rules.

Although lenders with large volumes of transactional data may use this to model expenditure, this is not the only way to meet the rules, and many smaller lenders already use expenditure assumptions in their affordability assessments.

In relation to the concerns raised about supervision, we are carrying out internal training for supervisors, and extensive firm engagement and education, to ensure a consistent understanding of the rules.

We believe that the rules are sufficiently tight to prevent firms from gaming the expenditure rules, particularly in conjunction with record keeping and monitoring requirements, so we are not setting any specific external benchmark.

We are not changing the categories of expenditure, for example moving childcare into the basic essential expenditure category. The guidance in the rules clearly gives childcare as an example of the type of expenditure that might form part of basic quality of living costs.

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

15. Most respondents saw the need for future interest rate rises to be factored into affordability assessments, and were broadly in favour of the proposals.
16. Some lenders were concerned that the volatility of market expectations for interest rates could make it difficult for them to manage the rates they use to test the impact of rate changes on affordability, with some asking for clarification on how often they should review their rate.
17. There was some confusion around applying the minimum 1% rate, with several firms under the impression that this minimum could be applied at any time in the economic cycle, rather than only where the market expects rates to fall or rise by 1% or less over the next five years, as stated in CP11/31.

18. Several respondents, particularly consumer representatives, saw potential for some gaming or manipulation of the market through these proposals, such as:
- fixed rates of five years or longer becoming more popular to avoid the need to consider future interest rate rises;
  - lenders competing on stress test rates, e.g. when they want to increase their market share; and
  - lenders pegging their stress test to the most favourable external source according to their needs at a particular time.
19. One consumer representative thought that the interest rate stress test may prove overly restrictive in subdued market conditions when underwriting standards are already tight, and insufficiently restrictive in boom market conditions, when underwriting standards loosen. To address this, they suggested that the minimum interest rate should be varied counter-cyclically, set at zero in subdued market conditions, and potentially set higher than the minimum 1% in boom conditions.
20. Some larger lenders argued that they should be able to use their own interest rate forecasts, as they already produce similar forecasts for other reasons.
21. A number of practical points were also raised. Some lenders were keen to keep the details of their interest rate assumptions confidential (other than for regulatory scrutiny), to prevent their affordability requirements from being gamed. Several respondents questioned the rate to which the stress test should be applied (e.g. the initial rate or the lender's standard variable rate (SVR)). Some had more general concerns about the regulatory risks of failing to accurately predict the future.

### Our response

We are proceeding with the interest rate stress test proposals without any substantive changes.

We are not prescribing how often firms must review the 'stress' rate that they use to test affordability against future interest rate increases. We expect them to manage this themselves, in the context of market expectations. However, as market expectations can be volatile, we recognise that some degree of smoothing will be undertaken by firms for practical reasons. There is no requirement for firms to amend their stress rate on every minor change in market expectations.

We believe that there are enough controls in the rules to prevent gaming, such as the record keeping and monitoring requirements. If there was a movement towards more five-year fixed rates, this would not contradict the policy intention, which is to consider affordability in the context of interest rate increases over the next five years.

The new interest rate stress test rules will come into effect after regulatory reform and any decision about whether to vary the minimum stress test counter-cyclically will be a matter for the Financial Policy Committee, and not the Financial Conduct Authority.

We indicate (in MCOB 11.6.19G) that it is not acceptable for lenders to rely on their own forecasts of interest rates. However, this does not necessarily prevent a lender from using its internal view of future interest rates, provided they can justify the basis used to form this view by reference to some independent forecast of market expectations, such as the forward sterling rate published on the Bank of England website.

There is no requirement in our rules for firms to make their interest rate assumptions public. It is up to firms to manage this as they would any other assumption used in their affordability assessment.

We will not be prescribing in the rules which rate the stress test should be tied to (e.g. the initial rate or the SVR). We expect firms to apply an appropriate approach, considering the impact of expected interest rate changes over the next five years on the customer's ability to make their mortgage payments.

The purpose of this requirement is not for lenders to predict the future, but for them to take reasonable steps to factor expected interest rate rises into affordability assessments. It will not prevent all customers from experiencing financial difficulties – but will reduce the likelihood of them finding mortgages unaffordable due to expected changes to interest rates.

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

- 22. Most respondents, including lenders and trade bodies, agreed with our assumption that 90% of lenders already apply a stress test.
- 23. Several lenders felt unable to comment on the practices of other lenders, on the basis that they did not have that information available to them, but some of these did confirm that their own firm applies a stress test.

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

- 24. Most respondents agreed that lenders are currently applying a stress test of a similar degree to that proposed. Some lenders agreed that their own stress test is similar, but felt unable to comment on other lenders' stress-tests.

### Our response

This confirms our understanding from discussions with market participants that most lenders currently do take account of interest rate rises when assessing affordability, and therefore confirms our view that our proposals will not have a significant impact on current market practice.

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

25. There was a strong consensus in favour of dropping the requirement that affordability should be assessed on a maximum term of 25 years. Respondents felt this was too restrictive, and in particular would prevent younger customers from getting on the property ladder. Instead, they felt that a customer's individual circumstances should be taken into account.
26. Respondents also noted that dropping this proposal would be consistent with increasing life expectancies and working lives of customers.

### Our response

We have dropped this requirement.

**Q8:** *Do you have any comments on our proposals to protect credit-impaired consumers?*

27. The majority of respondents supported the proposal to drop the buffer for credit-impaired borrowers, agreeing that the strengthened responsible lending requirements will provide greater protection for all borrowers, including the credit-impaired.
28. Many respondents also thought that the debt consolidation proposals, both in relation to advice and assessing affordability, would protect credit-impaired customers.

### Our response

We have dropped the credit impaired buffer proposed in CP10/16.<sup>2</sup> We will proceed with compulsory advice for debt consolidation, and the affordability requirements for credit-impaired customers consolidating debt (which we discuss further below in response to Q12).

<sup>2</sup> 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)

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

29. The majority of respondents agreed that the proposed enhanced sales standards will provide adequate protection for right-to-buy (RTB) customers, particularly when coupled with the strengthened responsible lending requirements. Nevertheless, some consumer representatives urged us to keep a close eye on this sector given past experience and the vulnerable nature of some RTB customers.
30. While the enhanced sales standards will protect RTB customers, several respondents, including trade bodies and some lenders, noted that perhaps a bigger question for RTB customers is whether they should exercise their right-to-buy at all, or remain as tenants, which falls outside the remit of mortgage advice. They therefore felt that customers should receive further advice and support in making this decision. Some lenders also felt that it should be made clear in the advice process that mortgage advice is about the loan rather than the decision to exercise the right-to-buy.
31. Some trade bodies and lenders felt that there was potential for conflict between the government's housing strategy, which aims to reinvigorate this market, and our more cautious approach (e.g. references in CP11/31 to RTB lending as being 'high risk'). They felt this could result in a reduction in lender support for this aspect of the government's housing strategy.

### Our response

In response to feedback, we intend to proceed with our proposals to require RTB customers to receive advice (except in the unlikely event that a HNW mortgage customer is exercising a right-to-buy). As we outlined in CP11/31 we believe that RTB customers have been more at risk of taking on unaffordable borrowing and additional protection is needed.

We do recognise that RTB customers may need help and support when making the decision to purchase their home. However, this is separate to mortgage advice.

There is already a wide range of information available to support RTB customers.

The Department of Communities & Local Government has recently launched a new website<sup>3</sup> and there is existing information via Directgov<sup>4</sup> and Money Advice Service.<sup>5</sup> Furthermore, RTB customers will also be pointed to these sources of information, as well as other sources of money advice as part of their RTB documentation.

<sup>3</sup> <http://righttobuy.communities.gov.uk/>

<sup>4</sup> [www.direct.gov.uk/en/HomeAndCommunity/BuyingAndSellingYourHome/HomeBuyingSchemes/DG\\_4001398](http://www.direct.gov.uk/en/HomeAndCommunity/BuyingAndSellingYourHome/HomeBuyingSchemes/DG_4001398)

<sup>5</sup> [www.moneyadviceservice.org.uk/en/articles/right-to-buy-right-to-acquire-in-england-wales-and-n-ireland](http://www.moneyadviceservice.org.uk/en/articles/right-to-buy-right-to-acquire-in-england-wales-and-n-ireland)

We have referred to RTB as being 'higher risk' in previous MMR publications, because our data shows that RTB customers have been the borrower type most likely to experience arrears and payment problems. However, we believe that the enhanced sales standards and strengthened affordability requirements will improve standards across this market. Therefore, we do not see a conflict for lenders in supporting this market, subject to appropriate sales and affordability assessments.

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

32. Most respondents thought that income multiples could only work to a limited extent under our proposed rules, in that they could sit alongside the affordability assessment, to apply a maximum cap on lending, or provide an indication of maximum loan size (for customers or intermediaries) before a full affordability assessment.
33. However, most could not see how they would work as the sole method of assessing affordability. Although income multiples can take account of committed expenditure (e.g. if a deduction is made from income before the multiple is applied), many respondents could not see how essential expenditure, basic living costs or future interest rates could be incorporated in a robust and demonstrable way. They therefore felt that income multiples would not work as a standalone method of complying with our affordability rules.
34. In addition, some respondents, particularly consumer representatives, were strongly against income multiples, because they saw them as a very blunt method of determining affordability.
35. There was some support from some smaller lenders and one trade body for income multiples being allowed to continue under our rules – particularly for low volume lenders where individual case underwriting is also employed, perhaps through some form of 'hybrid' model (i.e. where other affordability elements such as expenditure and future interest rates are considered within or alongside the income multiple). Their view was that income multiples had led to prudent lending and low arrears in the past, and replacing them with an affordability model would have significant costs and few benefits.

### **Our response**

We agree with respondents that it is difficult to see how income multiples could work as the sole method of meeting the new affordability requirements.

This does not necessarily rule out the use of income multiples completely, if a firm can demonstrate that their approach explicitly considers factors such as expenditure and future interest rate increases (see MCOB 11.6.7G). Nor does it prevent income multiples being used as a cap on lending or to provide an indication of loan size, before a full affordability assessment.

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

36. This proposal was generally welcomed, particularly the clarification that we did not expect lenders to ‘crystal ball gaze’, and that lenders would only be expected to take factors into account of which they should reasonably be aware when assessing the application. However, several specific concerns were raised by respondents.
37. In relation to retirement age, some lenders felt that the wording used within the draft handbook text was unclear, and they were unsure whether we expected lenders to assume that all customers retire at state pension age, or whether they could consider the customer’s actual expected retirement age (whether earlier or later than state pension age).
38. A few lenders also wanted more guidance about exactly when they should apply a higher degree of scrutiny of income in retirement, for example, whether this would be required perhaps five or ten years before the expected retirement date.
39. Trade bodies and several lenders were concerned about the interaction of our proposals with equalities legislation. They questioned whether the lender might contravene their equalities obligations if they ask mortgage applicants direct questions about some future events, such as their intention to start a family or return to work after maternity leave. Trade bodies suggested some specific wording that they thought was acceptable under equalities legislation, which could be used in mortgage application forms: ‘Are you aware of any changes to your circumstances that are likely to affect your ability to meet your monthly mortgage repayments?’ They asked whether this would be sufficient to meet our requirements.
40. A trade body and a lender were concerned that these requirements will cause uncertainty about how they should treat fixed-term contractors, and suggested that they would not be able to lend to them because the end of their contract is a known event.
41. Several trade bodies and larger lenders thought the future viability of shared equity loans might be affected by these proposals, if future payments on equity loans are required to be factored into the affordability assessment - given that affordability is already tight for many first-time buyers.
42. Several firms thought that lenders, through the act of underwriting the mortgage, might give the impression that they were advising on pensions or giving customers a degree of assurance that their pension arrangements were adequate.
43. A few respondents thought that lenders should be able to take account of potential positive changes to future income and expenditure, as well as negative changes. One respondent thought that such positive changes should include those arising from a customer’s expected career progression and more general developments, such as improving economic prospects and the strength of the labour market. Another respondent questioned whether significant

reductions in energy bills resulting from energy efficiency improvements to the mortgaged property could be factored into the assessment of expenditure.

### **Our response**

As we said in CP11/31, it is not our intention to prevent older customers from accessing mortgage finance. There is no reason why older customers cannot obtain a mortgage under the new rules (as long as it is affordable).

We have made some amendments to MCOB 11.6.15G(2) to make it clear that the lender can base their assessment on the customer's actual expected retirement age, taking a common sense view, with state pension age used as a default if the actual retirement age is not known.

We do not believe it would be appropriate to provide explicit guidance about when a lender should start applying more scrutiny of income in retirement, as this may vary according to the circumstances of the customer.

In response to concerns about firms breaching their equalities obligations if they ask applicants direct questions about future events, MCOB 11.6.14R requires firms to take account of future changes to the income and expenditure of the customer that they are, or should reasonably be, aware of from 'information obtained during the application process'. One way of meeting this requirement, may be to ask a general question along the lines of that suggested ('Are you aware of any changes to your income or expenditure that are likely to affect your ability to meet your mortgage payments?'). We discuss equalities issues further at Q105 to Q118.

When it comes to considering the income of fixed-term contractors, the end of a contract does not equate to the end of that customer's ability to earn an income. We do not expect a different approach to underwriting these cases than has been taken in the past. For example, a lender will have a policy setting out their approach to contractors based on factors such as their track record of past contracts, and their general view on the likelihood of obtaining future contracts.

In relation to shared equity schemes, we continue to believe that a lender providing a first charge loan should take account of the effect that a shared equity loan may have on the affordability of the first charge loan. This may arise from the following two aspects of the shared equity loan:

1. Interest payments or charges on the shared equity loan that become due during the term. In this case, the lender should consider the impact of this on the affordability of the first charge mortgage, as they would for any other financial commitment.
2. Repaying capital that becomes due during the term. While it is not the responsibility of the first charge lender to determine how the shared

equity loan will be repaid, this event could have a significant impact on affordability (e.g. if 20% of the value of the property must be repaid to the shared equity lender at a certain point during the first charge loan). In some cases, capital repayment may be due fairly soon after the loan is granted (e.g. five to ten years) and lenders should consider whether customers have a credible strategy for dealing with this and the first charge loan. We recognise that the customer might intend to sell the property to repay the loan (as per MCOB 11.6.15G(3)), but this may not always be the case. In other cases, repayment will not be due for a considerable period of time in the future (e.g. around 20 years), and the lender may be less concerned about the impact that this has on the affordability of the first charge loan. They might consider, for example, that as the shared equity loan is only a small percentage of the customer's overall borrowing secured on the property, the customer's ability to repay the shared equity loan might be assisted by reasonable increases in income over the 20-year period. We are not expecting the lender to 'crystal-ball gaze' about customers' circumstances in the future, but simply to take a view on whether the shared equity loan is likely to cause the customer difficulty in repaying their first charge loan.

We understand that the industry will be working to produce good practice guidance on how lenders can meet this obligation, and we support these efforts.

If firms are concerned about giving customers the impression that they are giving advice on pensions, when assessing a mortgage application, there is nothing to stop firms from using some form of appropriate wording in written or spoken communications to customers that this is not the case, as long as it is clear, fair and not misleading, and does not breach any other rules.

The rules do not prevent known positive changes being considered in the affordability assessment (e.g. evidence that the customer will be made a partner in their firm, or has a contract that confirms a promotion or increase in salary; or where energy efficient work has been undertaken to significantly reduce energy bills on the mortgaged property), but not uncertain developments, such as improved economic prospects. Reliance on such events would risk detriment if they subsequently fail to materialise, and run contrary to the overall MMR approach, which aims to ensure that underwriting is based on factual and credible information, supported by appropriate evidence.

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

44. The consensus view was that a definition was required, to provide consistency in approach across the market, and prevent gaming.
45. However, views about the proposed definition varied. Some agreed with the definition, but others, particularly lenders, did not. For example, some lenders felt that more emphasis should be placed on recent payment problems, or problems relating to secured commitments. Others felt customers who had suffered temporary financial difficulties would be penalised by the definition, whereas some customers with significant credit problems might fall outside the definition (e.g. where a county court judgment was registered more than three years ago, despite the fact it was still outstanding). Some consumer representatives were concerned that customers under a high degree of financial stress and just about to tip into credit problems (but with no current impaired credit) would not be caught by the definition, and so would be vulnerable as they might be very likely to consider a debt consolidation mortgage.
46. Few suggestions were made for alternative definitions.

### Our response

We recognise there is no single definition that will precisely capture the credit-impaired customers who would benefit from the extra protection of the debt consolidation rule (MCOB 11.6.16R). There are numerous ways that we could cut the definition to include or exclude certain categories and stages of credit problem, but it would never be possible to capture all possible variations, or include customers who may be about to suffer credit problems. We think the proposed definition of 'credit-impaired customer' captures the majority of customers with current credit problems.

As the sole purpose of this definition in the context of the mortgage rules is to target the application of the debt consolidation requirements, we cannot see any detriment arising from a customer falling into the definition, even if they are recovering from credit problems.

There is nothing to stop lenders from applying the debt consolidation rule more widely, if they wish to provide an extra layer of consumer protection for some customers falling outside the definition.

Therefore, we are proceeding with the definition unchanged.

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**Q13:** *Which option do you prefer? Option 1, where the lender would be required to take reasonable steps to ensure that debts to be consolidated are repaid? Or option 2 where the lender would be required to assume that debts to be consolidated remain outstanding for purposes of assessing*

*affordability? If you disagree with both options, what do you suggest as an alternative?*

47. Given the choice between the two options we proposed in CP11/31 for credit-impaired customers consolidating debt, more respondents favoured option 1, on the basis that this would be the most effective way to ensure that debts were repaid as expected, allowing customers to fully benefit from debt consolidation mortgages. Some lenders noted that they already have processes in place to repay debts directly to creditors. But many respondents, particularly lenders, recognised the administrative difficulties and additional costs involved in this, as well as the risk that the customer might immediately run up more debt once debts have been cleared.
48. Option 2 was favoured by a small number of respondents, but most thought that this option would restrict the availability of debt consolidation mortgages (because many customers would not pass the affordability test if it is assumed that debts to be repaid will remain outstanding).
49. However, many respondents suggested that both options should be available, providing lenders with flexibility in deciding how to implement this requirement, and providing more choice for customers.
50. Some consumer representatives strongly felt that these measures should be applied across all customers, not just those with an impaired credit history.

### **Our response**

In CP11/31 we concluded that it would not be proportionate to apply these measures across all customers. We recognise that many customers are able to take on the responsibility of repaying their debts directly. Our data shows that customers with an impaired credit history have significantly higher levels of arrears when consolidating debt than those who do not, which is why we are targeting only this group of customers.<sup>6</sup>

However, because we are considering all customers consolidating debt as a 'vulnerable group' for the purpose of our distribution rules, they will all be required to obtain advice.

In response to the feedback received, we are proceeding on the basis that both options will be available.

**Q14:** *Do you agree with our proposals to strengthen lender's systems and controls around responsible lending?*

<sup>6</sup> See Exhibit 16.10 in MMR Data Pack (October 2012).

51. Most respondents supported these proposals, subject to some specific concerns.
52. Some lenders thought that it would be more appropriate for the very large lenders to be able to sign off their responsible lending policies through an appropriately delegated local committee of the board which would have a better understanding of the policy, and related issues, than the main board.
53. Several lenders thought that responsible lending policies should be able to reference other documents, rather than being required to be contained in one single document. This was due to concerns about the length of the document, and the appropriateness of wide circulation of some of the more sensitive elements of the policy (e.g. details of fraud prevention measures, as discussed in Q1).
54. Some very small lenders, with no internal audit function, were concerned that the requirement to audit compliance with their responsible lending policy once a year may be very costly for them.

### Our response

We recognise that the main board of a firm may not always be the most appropriate body to consider the details of a responsible lending policy, e.g. if the firm is a global firm where the board may not be familiar with UK mortgage lending. However, we are keen to see the senior management of firms engaging with and taking responsibility for the conduct-related mortgage-lending practices within their firm.

Therefore, we are amending the wording of MCOB 11.6.20R so that it refers to the firm's governing body rather than the firm's board. 'Governing body' is a defined term, referred to elsewhere in MCOB (e.g. in MCOB 13) that is defined in the FSA glossary as 'the board of directors, committee of management or other governing body of a firm or recognised body, including, in relation to a sole trader, the sole trader'.

We understand that it may not be practical for the entire contents of a responsible lending policy to be contained in one document, as required by the new rules. We have therefore amended MCOB 11.6.20R to reflect this.

We accept that many small firms will not have an internal audit function. Therefore, we have amended MCOB 11.6.24R so that where a firm has an internal audit function (or an outsourced equivalent), the annual review of compliance with their responsible lending policy must be undertaken by that function. However, where a firm does not, the review may be undertaken by the firm's internal compliance function (or an outsourced equivalent).

In CP11/31 we proposed to extend responsible lending record keeping requirements from one year to three years. We have decided to further extend this requirement, so that lenders will be required to keep the records for the period that mortgage remains with the lender, to show how they have met our responsible lending requirements (i.e. the record keeping requirements set out in MCOB 11.6.60R).

We understand that most lenders already retain this data for this period, plus an additional period after this, so we do not believe that this change will lead to any material additional costs.

We have amended the record keeping schedule in MCOB to reflect this (see Appendix 1).

We are also extending the period for which a lender is required to keep a record of their responsible lending policy, following any change made to that policy – from three years from the date of the change, to as long as any mortgage to which it relates remains outstanding.

We do not believe that this will result in additional costs to lenders as most lenders already comply with this in practice.

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

55. The vast majority of respondents agreed with the aim of the transitional arrangements, which is to mitigate the impact of the introduction of our new responsible lending proposals on existing borrowers. However, there was a very strong consensus that, as drafted, the proposals were too complex to be widely adopted by lenders, and too restrictive to help many borrowers. Many respondents gave examples of borrowers who would benefit from a change to their mortgage, but who would not be able to do so because they did not meet the criteria for the transitional arrangements – including borrowers who want to fix their rate when rates are rising, or change from an interest-only to a repayment mortgage. Several respondents thought that increased borrowing should also be allowed, with some intermediaries suggesting 10% of the outstanding balance as an appropriate maximum for this.
56. Lenders and trade bodies felt that lenders would not use the transitional arrangements to take on borrowers from other lenders, because of their onerous nature, and because they would be unable to price for risk. In addition, some commented that the risk of taking on lending that does not fully meet the new responsible lending requirements would be considered too great by many lenders.

57. Most respondents favoured a more flexible approach to the transitional arrangements. Several trade bodies suggested that lenders should be able to adopt their own exceptions policy for existing borrowers who do not fully meet current responsible lending criteria. They felt that this approach would give lenders the flexibility to consider individual circumstances, and make sensible lending decisions, subject to appropriate controls being in place. This approach was also favoured by most lenders and consumer representatives.
58. Some mortgage intermediaries suggested that advice should be mandatory wherever the transitional arrangements were applied.

### Our response

We recognise the complexity and inflexibility in the original proposals. In response to feedback, we are adopting a more flexible approach, which will allow lenders to make individual lending decisions based on an exceptions policy, where they judge the transaction to be in the borrower's best interests – as long as there is no increase in the current amount outstanding (i.e. no additional borrowing). Further details of our approach can be found in Chapter 3.

Our approach to advice, including for contract variations, is in Chapter 2.

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

59. Many respondents reiterated their view that our proposed transitional arrangements would need to be amended as described at Q15 to provide sufficient consumer protection, but beyond this they did not suggest that any additional consumer protection would be required.
60. However, consumer representatives, and some intermediaries, were concerned about the risks of the unfair treatment of borrowers 'trapped' with their current lender, such as 'price gouging' (i.e. charging the borrower an unfavourable rate of interest to take advantage of the fact that they are not able to move to a different lender). They therefore saw the need for additional consumer protection, as they thought that relying on the principle of treating customers fairly or unfair contract terms breaches would not be enough. Consumer representatives saw the need for several specific amendments to the proposed transitional rules, including:
- converting the draft guidance in CP11/31 at MCOB 11.7.7 into a rule, so lenders would be banned from treating mortgage prisoners less favourably than other borrowers; and

- making it compulsory for lenders to use the transitional arrangements, rather than optional.

### Our response

The changes we are making to the application of the affordability requirements for contract variations, as set out in Chapter 2, along with the revised transitional arrangements, will make it easier for lenders to help existing borrowers.

We will continue to expect lenders to treat their customers fairly, in according with Principle 6 ('treating customers fairly'). In response to feedback, we are strengthening the protection for existing borrowers, by changing the guidance to an evidential provision (MCOB 11.8.1E). Under this provision, if the existing lender takes advantage of a 'trapped' borrower or treat them any less favourably than other customers with similar characteristics – for example, by offering less favourable interest rates or other terms – then this may be relied on as tending to show contravention of Principle 6.

As we explain further in the introduction, we are implementing this provision with immediate effect.

We do not believe that it is appropriate to make these transitional arrangements compulsory. Ultimately, it is for lenders to make lending decisions, and there may be sound reasons for not proceeding with individual transactions.

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

61. The consensus view was that the eligibility requirements were too restrictive, would not take into account individual circumstances, or allow lender discretion – and as a result would only help a small proportion of borrowers.
62. Many respondents pointed out that the rule preventing higher monthly payments might actually cause consumer detriment (e.g. if a customer was prevented from taking a fixed rate when rates were rising). The inability for lenders to price for risk, because of this requirement, would prevent lenders from taking on borrowers from other lenders under the arrangements.
63. Respondents therefore supported transitional arrangements that would allow increased monthly payments.

### Our response

In response to feedback, we have amended our approach to both the eligibility requirements and situations where the new monthly payment is higher (e.g. as a result of a rate switch). See Chapter 3 for more details.

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

64. There was strong support across the board for lenders being able to deal with material changes on a case-by-case basis, according to the circumstances of the borrower. Lenders noted that they already approach such changes in this way. Many respondents could not see how a prescriptive set of rules would be able to cover the full range of borrower circumstances.

### Our response

In response to feedback, we have revised our approach to how material changes are dealt with under the transitional arrangements. See Chapter 3 for more details.

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

65. As explained at Q15, the vast majority of respondents supported a more flexible approach to the transitional arrangements, based on an exceptions process.

### Our response

See Chapter 3 for more details on our revised approach to the transitional arrangements.

**Q20:** *Do you agree that the draft rules on responsible lending in the draft Mortgage Market Review (Conduct of Business) Instrument 2012, at Appendix 1, reflect the stated policy intention?*

66. Most respondents agreed that draft rules on responsible lending reflect our stated policy intention. Several respondents suggested drafting changes to make the rules clearer.

### Our response

We have taken the drafting suggestions into consideration when preparing the final rules. See Appendix 1 for the final rules, and Annex 2 which summarises the changes.

## Interest-only mortgages

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

67. The vast majority of respondents agreed with our approach to assessing affordability for interest-only, i.e. that affordability may be assessed on an interest-only basis, where there is a credible repayment strategy; and that the cost of the repayment strategy must be factored into the affordability assessment as ‘committed expenditure’.
68. Several lenders asked for clarification on whether they would be allowed to assess affordability for interest-only mortgages on a capital and interest basis, if they wanted to and, if they did, whether they would still need to include the cost of the repayment strategy as committed expenditure.

### Our response

We are proceeding with the interest-only proposals unchanged.

MCOB 11.6.48R states that a lender may assess affordability on an interest-only basis. This does not prevent lenders assessing affordability for interest-only mortgages on a capital and interest basis. If affordability is assessed on a capital and interest basis, the cost of the repayment strategy does not need to be included as committed expenditure.

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

69. The consensus view was that we should apply a consistent approach to regulating interest-only, rather than adapting our approach to different consumer types, such as first-time buyers, older customers, or high net worth (HNW) customers. Respondents thought that assessing individual circumstances should be the most important consideration, and felt that applying different approaches for different types of customer might prevent some customers from accessing interest-only mortgages, even where it is an appropriate option.

70. While most agree that the individual circumstances of a customer are the main factor in determining eligibility for interest-only, a few thought that a different approach might be required for specific niches such as HNW and business lending. A couple of respondents thought we should explicitly set out our views regarding the needs of customers with long-term disabilities, who may wish to take out a mortgage through the Home Ownership for people with Long-term Disabilities (HOLD) scheme.

### Our response

We are not adapting our approach to interest-only according to customer type.

Nor are we adopting a different approach to interest-only for HNW or business lending. We consider our existing approach offers sufficient flexibility for lenders to offer interest-only mortgages to meet a wide variety of customer needs.

We do, however, propose a tailored approach to HNW and business lending in general, which is set out in Chapter 4.

We do not intend to adopt a different approach to the HOLD scheme, as we believe that our interest-only rules are flexible enough to meet the needs of different types of customers, including disabled customers. As we discuss in our responses to Q107 and Q108, the rules do not prevent lenders from accepting the eventual sale of property, as long as the customer is not relying on a speculative repayment strategy.

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

71. The majority of respondents agreed with the non-prescriptive approach and thought it would enable lenders to meet the varied needs of individual customers and different market sectors, while providing an appropriate level of protection for customers. Some consumer representatives, however, wanted a more prescriptive approach, because they were concerned that lenders might accept inappropriate or inadequate types of repayment strategies, unless they were specifically prevented from doing so.
72. The biggest concern expressed by industry respondents related to the risks arising from the flexibility inherent in the non-prescriptive approach – such as the judgements that firms would be required to make, for example, when deciding what type of repayment strategy to accept, or when assessing the credibility of each individual repayment strategy.
73. Several lenders and intermediaries expressed concerns about the future supervisory approach to interest-only, and how we would judge firms' lending decisions with the benefit of hindsight. Respondents thought that this uncertainty would cause lenders to

adopt an overly cautious approach for new interest-only lending, and so restrict the availability of interest-only mortgages. Some thought we should be clearer about our view of interest-only (e.g. is it a niche product only, or an acceptable mainstream product?), or set out some form of minimum standards or guidance about repayment strategies that we consider acceptable.

74. Some industry respondents questioned what we meant by a ‘speculative’ repayment strategy (see MCOB 11.6.41R(3)). For example, some suggested that a repayment strategy that relied on investment returns is by its very nature speculative, and therefore would not be permitted under the rules. There was also some confusion about where the line was drawn between speculative and non-speculative repayment strategies; for example, whether bonuses or lump sum payments could be considered as an acceptable repayment strategy, or whether they would be seen as speculative.

### Our response

We are proceeding with a non-prescriptive approach to repayment strategies.

As we explained in our responses to Q2 and Q3, in relation to the concerns raised about supervision, we are carrying out internal training for supervisors and extensive firm engagement and education to ensure a consistent understanding of the rules.

As we stated in CP11/31, there is a consensus view that interest-only should be a ‘niche’ product. We expect most mainstream lending to take place on a capital and interest basis. We recognise that interest-only mortgages can be appropriate in a wide variety of circumstances, so we do not think it would be useful, or practical, to set out any form of minimum standards.

In relation to what might constitute a ‘speculative’ repayment strategy, we mean a strategy where the borrower is reliant on uncertain external events, such as property price increases or an inheritance. (We include these, in MCOB 11.6.46E, as examples of repayment strategies that, in the absence of evidence to the contrary, would breach MCOB 11.6.41R(1) if accepted by a lender). We do not mean more tangible repayment strategies, such as regular deposits into a savings or investment product, or periodic repayment of capital from irregular sources of income such as bonuses (which are included at MCOB 11.6.45G as examples of repayment strategies that might be acceptable, depending on the circumstances of the customer). The key consideration is whether the firm has evidence that the customer has a clearly understood and credible repayment strategy that, as far as the firm is reasonably able to assess at that time, has the potential to repay the mortgage.

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

75. Most respondents were in favour of this, with several citing the benefit of lenders being able to manage their own risk, subject to concerns about our supervisory approach, as discussed at Q23.

### **Our response**

We are proceeding with this proposal.

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

76. The majority of respondents were in favour of these proposals. Some specific concerns were raised by lenders, similar to those expressed at Q14, in relation to the sign-off process for large lenders, and the ability of the policy to reference other documents.
77. A few firms, mainly those active in the more niche areas, such as bridging and lending to high net worth customers, were concerned that they would not be able to document all possible repayment strategies in their interest-only policy.

### **Our response**

We are proceeding with this proposal, subject to the amendments we are making to MCOB 11.6.20R, as explained in the response to Q14.

The rules do not require every possible repayment strategy to be set out in its policy. Rather, the rules require the types of repayment strategy that the firm considers acceptable, and the controls around those strategies, to be specified. Therefore, if a lender accepts the sale of assets, we recognise that it might not be possible for them to list every possible asset type in their policy. Instead, it might be more appropriate to list different assets types, e.g. according to the controls that apply to those asset types.

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

78. There was a strong consensus in support of the high-level approach proposed, and several lender respondents welcomed the changes made to clarify the limited nature of the expected assessment (i.e. that it was not intended to be ‘crystal-ball gazing’). Nonetheless, some firms continued to be confused about what we meant by a ‘credible’ repayment strategy, believing that we intended firms to be sure that the repayment strategy would repay the capital at the end of the term.
79. Some firms thought the assessment would be so burdensome that lenders would withdraw from the market, or that the competencies required to make an assessment would not be found in smaller lenders, therefore distorting competition.
80. Many firms were also concerned that the act of assessing the credibility of a repayment strategy may:
- cause customers not to recognise that the principal responsibility for repaying the mortgage remained with them;
  - be seen by the customer as advice, or
  - somehow be seen as giving the customer an assurance that the repayment strategy will perform as expected, and therefore lead to an expectation that lender will be liable if this fails to occur. This impression was reinforced by the proposal to perform a mid-term check on the repayment strategy (as discussed in Q27).

### Our response

We want to make it clear that we are not expecting firms to predict what will happen in the future. We expect firms to assess, so far as it is reasonably able to at the time of underwriting, that the repayment strategy has the potential to repay the capital<sup>7</sup>, and nothing more. The fact that the lender has assessed the repayment strategy should not be taken as a guarantee that it will repay the mortgage. Responsibility for repaying the capital at the end of the term remains with the customer, in line with the terms of the mortgage contract.

Lenders will need to make underwriting judgements about whether the repayment strategy has the potential to repay the capital, as they already do. Lenders will have to manage the risks around this if they lend on an interest-only basis. We will expect lenders’ staff to be appropriately qualified to make the judgements they are required to make in the context of the lender’s interest-only policy. If a lender does not have staff competent to assess a particular type of repayment strategy, then we would expect them to not accept that strategy.

<sup>7</sup> Plus any interest reasonably expected to be accrued under the interest-only mortgage (e.g. in the case of an interest roll-up mortgage).

To address possible misconceptions on the part of customers about, for example:

- their responsibility for repaying the mortgage;
- whether they are receiving advice about the repayment strategy or assurances about its performance; or
- potential liability when things go wrong;

there is nothing to prevent lenders from using some form of wording in written or spoken communications to get the appropriate message across to customers, as long as it is clear, fair and not misleading, and does not breach financial promotions or other relevant rules. We do not intend to prescribe the messages that firms should use.

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

- 81.** While the majority of respondents were broadly in favour of the proposals, many raised similar issues to those discussed at Q26, in relation to assessing whether the repayment strategy still has the potential to repay the mortgage.
- 82.** In addition, lenders were particularly concerned about:
- the responsiveness of borrowers, requesting more clarity on what would constitute reasonable efforts to contact the borrower;
  - the actions they should take if it was discovered that there was likely to be a shortfall on the strategy, with a few questioning the proportionality of requiring a check when only limited options were available;
  - the potentially significant costs incurred checking on borrowers' repayment strategies (particularly for larger lenders); and
  - the risk that mid-term contact may result in a perceived further transfer of responsibility for the repayment strategy from the borrower to the lender.
- 83.** Some consumer representatives and intermediaries supported more frequent checks on the repayment strategy during the life of the mortgage, considering a single check of limited use as it provides only a snapshot in time that may change later.
- 84.** Several respondents noted that a check during the term of a mortgage might not be appropriate for mortgages with short terms (e.g. five years or less).

## Our response

We are not suggesting that a mid-term review of the repayment strategy will enable all issues to be resolved. Nor are we suggesting that the onus for solving the problem lies with the lender. As we made clear in CP11/31, the purpose of the check is to raise awareness of the potential issues to both the lender and the borrower. The responsibility for repaying an interest-only mortgage remains with the borrower. The lender cannot be held responsible if what appears to be a credible repayment strategy at the point of underwriting does not deliver. Similarly, a mid-term check cannot be taken to mean that the lender is guaranteeing that the repayment strategy will repay the capital at the end of the term.

If the mid-term check reveals a problem with the repayment strategy, it is the responsibility of the borrower to bring it back on track. As explained in Q26, all we expect a lender to do at the time of underwriting is to assess, as far as it is reasonably able to do so, that the repayment strategy has the potential to repay the capital, and nothing more.

Some borrowers will not engage with their lenders about this issue – and this is recognised in the rules (MCOB 11.6.49R(3)). We do not propose to prescribe what ‘reasonable efforts’ to contact the borrower are. This will be for the lender to determine and demonstrate, i.e. through record keeping. We have amended the record-keeping rules to make this explicit (MCOB 11.6.60R(3)(c)).

We do not believe that this check will be particularly costly or onerous for the lender. The rules do not specify the degree to which the check must be undertaken – for example, there is no requirement for the lender to obtain documentary evidence and re-underwrite the case. The rule (MCOB 11.6.49R) merely requires the lender to make contact with the borrower, to check if the repayment strategy is still in place, and check whether it is still reasonable to expect that it has the potential to repay the mortgage. So while the lender may choose to request documentary evidence of the repayment strategy from the borrower, there is no specific requirement for them to do so – therefore they could rely on information provided by the borrower.

We continue to believe there is value in the mid-term review, which will alert both parties to potential issues at a point where there is still time to consider remedial action – rather than waiting until the end of the term. This may be the catalyst that prompts some borrowers to take action. Even relatively minor changes (such as small overpayments made over several years) might significantly improve the borrower’s position and range of options by the end of the term. Therefore, we are proceeding with this proposal.

We can, however, see that there may be a limited benefit to a mid-term check with a mortgage with a very short term, so we are disapplying this requirement for bridging loans.

We are carrying out a separate piece of thematic work to assess the issues faced by existing interest-only borrowers without the means of capital repayment at mortgage maturity. The results of this work will be communicated to the market in due course.

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

85. The majority of respondents supported the change to the glossary term from ‘repayment vehicle’ to ‘repayment strategy’, noting that it is a suitably wide term. They also supported the consequential changes.

#### **Our response**

We are proceeding with the proposed change to the glossary term and the consequential changes.

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

86. Respondents broadly agreed that the rules reflect the policy. However, there were a number of suggestions to improve and clarify various specific rules.

#### **Our response**

We are proceeding with the substance of the rules as drafted, but are making some small amendments following feedback, to ensure the rules better reflect the policy intention.

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## **Distribution**

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

87. Responses from the majority of consumer groups and intermediaries were supportive of the proposal and welcomed the clarification of the responsibility for assessing affordability. However, many lenders were less supportive and believed the intermediary would need to assess affordability when giving advice.
88. These respondents were concerned that removing a regulatory responsibility from the intermediary would absolve them from any responsibility and this could have unintended consequences. As a result, lenders felt the responsibility for affordability should be shared.
89. A number of intermediary respondents suggested they will still need to see the customer's income and expenditure information to satisfy themselves that they are not supporting fraudulent applications.
90. Finally, there was a concern from a minority of respondents that it may be difficult for intermediaries to keep up with lenders' criteria.

### Our response

We believe that making the lender ultimately responsible for assessing affordability is the right way forward and we have not amended our approach.

Intermediaries will still be required to ensure they have adequate systems and controls to prevent financial crime (SYSC 6.1.1R). Therefore an element of income checking and verification will still be required to ensure the intermediary is not supporting a fraudulent application. However, this is separate to the advice requirements.

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

**Q31(ii):** *Do you have any comments on our proposed definition of a 'mortgage professional'?*

91. In response to CP11/28<sup>8</sup>, lenders and intermediaries felt that execution-only would only be appropriate for a minority of customers and suggested that this would be high net worth and mortgage professionals. However, most respondents to CP11/31 were unsupportive of allowing these proposed opt-outs.

<sup>8</sup> CP10/28, *Mortgage Market Review: Distribution & Disclosure*, (November 2010): [www.fsa.gov.uk/pubs/cp/cp10\\_28.pdf](http://www.fsa.gov.uk/pubs/cp/cp10_28.pdf)

92. Many respondents felt the definition of a ‘mortgage professional’ was too broad in scope and would capture administrative staff. There was also a concern about how the exemption would apply to joint applicants, where only one was a mortgage professional.
93. Lenders were concerned that the work and oversight required to set up a process to cater for a small group of customers was disproportionate. They noted it would be unlikely the exemption would be applied in practice. However, intermediaries were supportive of applying the proposed opt-out.
94. There was more support from both lenders and intermediaries for applying a different approach to HNW customers.

### Our response

Overall, we believe the definition of a ‘mortgage professional’ is clear and would only capture applicants who could demonstrate they hold a professional position, which would exclude administrative staff. We therefore do not intend to amend the definition.

For joint applications where only one applicant is a mortgage professional, then advice would be required for the non-professional applicant. In practice this would mean that the application would be advised.

**Q31(iii):** *Is there anything we can do to mitigate the risk of intermediaries using these exceptions to circumvent the rules?*

95. Several respondents, including trade bodies and lenders, noted that the rules make it clear that a firm should not encourage a customer to opt-out from, or reject advice in favour of, execution-only. They also felt that a relatively small number of customers will be able to opt-out, therefore the likelihood of anyone circumventing the rules is low.
96. Several respondents recommended having documentary evidence on file that establishes that a customer is a mortgage professional or a HNW customer. A small number of respondents suggested strong supervision and enforcement of these rules.

### Our response

We have included requirements for firms to keep a record of evidence that the customer is HNW or a professional. Overall, we believe that the controls we outlined in CP11/31 are adequate for the mortgage professional and HNW opt-outs.

**Q31(iv):** *Are there any other consumer types you think should be able to purchase on an execution-only basis in an interactive sale?*

97. A large number of respondents felt the proposed availability of execution-only was too restrictive and that it should be opened up more widely, with the customer being able to opt out of advice at the start of the sale.
98. They argued that other MMR proposals will provide sufficient consumer protection and the additional requirement to provide advice in almost every case is both unnecessary and very costly.
99. A number of respondents suggested extending the availability of execution-only sales to customers where the transaction is lower risk. For example, HNW, business customers, second or subsequent time buyers and straight-forward remortgagers. A few respondents suggested other consumer groups, such as first time buyers, credit impaired customers and vulnerable customers should be given advice.

### **Our response**

We have thought very carefully about the availability of execution-only. However, no one in response to CP11/31, or in our subsequent discussions with firms and their trade bodies, has been able to suggest adequate controls to avoid the gaming of execution-only if it were opened up more widely.

We firmly believe that allowing an execution-only channel, intended to accommodate a minority of customers, presents a serious risk of abuse. As evident with self-certification mortgages, our concern is that execution-only will become the norm and will be used beyond the small group for which it was created.

While monitoring and supervising the levels of execution-only business may highlight concerns to us, it is a reactive tool and would not prevent consumer detriment occurring.

As a result, we are not amending our policy approach to execution-only and intend to allow it on a very limited basis, i.e. limiting it to HNW mortgage customers, mortgage professionals and, in light of the feedback, business borrowers. Our approach to HNW mortgage customers and business borrowers is set out in Chapter 4. Our overall approach will require firms to give advice to all other customers purchasing a mortgage through an interactive sales channel.

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

- 100.** The majority of respondents generally supported our proposals to allow non-interactive sales to be undertaken on an execution-only basis.
- 101.** There were concerns, particularly from consumer representatives, that allowing an execution-only route creates a regulatory gap that could be exploited by firms to the detriment of consumers.
- 102.** Many noted that, while the online sales channel is currently small, it may grow in future, particularly where it is a means of circumventing the advised sales process.
- 103.** Lenders and their trade bodies asked if they could promote their execution-only online products without breaching our requirements not to induce customers to opt-out of advice. They also felt the rules should acknowledge that the customer can contact the firm to ask for assistance with the online application process without this triggering the requirement for advice.

### **Our response**

We recognise the concerns with execution-only rules being gamed and we intend to implement robust monitoring and supervision.

Our rules do not prohibit firms from making the customer aware of their execution-only channels, as long the information provided does not steer the customer in one particular direction, i.e. the customer is made aware of all available sales channels and is not encouraged to proceed on an execution-only basis. Our final rules make this clear (see MCOB 4.8A.5R).

Online help facilities such as 'adviser chat' functions, where the customer can interact with an adviser while applying online, will involve 'regulated advice', if the adviser steers the customer to a particular product or range of products. If the interaction is merely to help the customer navigate through the process or provide generic advice or information, this would not be considered regulated advice. Chapter 2 explains the boundary between advice and information.

Firms should also have regard to PERG (particularly PERG 4.6G) regarding the use of 'filtering' to narrow down the customer's choice of products. These requirements would also apply to aggregator and price comparison sites.

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**Q33 (i):** *We are proposing that consumers who are vulnerable (i.e. equity release, Sale and Rent Back or right-to-buy consumers and those who are consolidating debt) should always be advised and therefore will not be able to purchase their mortgage through a non-interactive process. Do you have any comments on this approach?*

104. Most respondents supported the proposal that vulnerable customers should always have advice. However, a number of respondents considered that those customers consolidating debt should not automatically be treated as vulnerable. These respondents wanted more clarity around the proposals for debt consolidation and also questioned the need for mandatory advice in situations where debt consolidation may only be a small aspect of the overall borrowing.
105. A number of respondents suggested that, for debt consolidation, there should be a cut-off point (e.g. a percentage of overall borrowing), below which advice is not mandatory.
106. A number of respondents also raised the potential for debt consolidation to be gamed, with the purpose of the loan being mis-stated to avoid the mandatory advice requirement.
107. Several respondents raised concerns about right-to-buy (RTB) and noted the key issue of whether to move from a secure tenure was outside the scope of advice. One respondent was concerned that restrictions on RTB may reduce the willingness of mainstream lenders to operate in this market.
108. Those respondents who offer Home Purchase Plans considered that these customers should be able to opt for a non-advised route.
109. The equity release respondents considered that their customers should be able to opt for a non-advised sale, particularly for contract variations.

### **Our response**

We are proceeding with our policy approach of requiring vulnerable customers to have advice (unless they are a HNW customer – see Q33(ii)). This means these customers will not be able to buy a mortgage via a non-interactive sales channel. We did not intend to capture Home Purchase Plans – we originally included these in the question by mistake and they are not included in the vulnerable category in our final rules.

We recognise that RTB customers may need help and support when deciding to buy their home. However, this is separate to mortgage advice and it is outside of our remit.

We have considered whether a value or percentage benchmark would be appropriate for debt consolidation loans, but we believe that more unscrupulous firms would take advantage of this, so we did not consider this to be an appropriate approach.

We therefore intend to proceed with our proposed approach to require advice where debt consolidation is the main purpose for additional borrowing.

Firms should also note that the existing requirements under SYSC 6.1.1R still apply and appropriate systems and controls must be in place to ensure fraudulent applications are not supported.

Our approach to contract variations is set out in detail in Chapter 2.

**Q33 (ii):** *What are your views on our proposal to allow high net worth consumers and mortgage professionals to opt-out of receiving advice irrespective of whether they are considered to be vulnerable?*

- 110. The majority of respondents thought that vulnerable customers should receive advice irrespective of HNW or mortgage professional status.
- 111. A number of respondents re-iterated their concerns with regards to our overall approach to advice and the limited availability of execution-only.

### Our response

In light of the feedback we have amended our approach to mortgage professionals and will require these customers to receive advice where they are a vulnerable customer. Our approach to HNW customers is discussed in detail in Chapter 4.

**Q33 (iii):** *Are there any other consumer types you think should always receive advice?*

- 112. The majority of respondents agreed with the proposed vulnerable groups.
- 113. First-time buyers were suggested by several respondents as another group for whom advice should be mandatory. A few respondents also suggested mandatory advice for those using transitional arrangements, older customers (those lending into retirement), shared ownership and credit-impaired customers.
- 114. A small number of respondents felt that the proposals should represent the minimum standard required and individual firms should be allowed to require other consumer groups to receive advice.

### Our response

In CP11/31 we outlined our views on FTBs and credit impaired customers. We did not think that advice should be mandatory for these customers and our views have not changed.

If firms wish to require other customers to always receive advice, in addition to our requirements, this is a commercial decision for that firm and our rules do not prohibit this.

**Q34:** *Do you agree that, except in the case of Sale and Rent Back, we should allow consumers to reject advice and proceed on an execution-only basis?*

- 115.** The majority of respondents agree that customers should have the choice to proceed without advice. Some argued that this choice should be made before the sale commences.
- 116.** A few respondents felt that the exception should apply to all of the vulnerable customer groups (equity release, right-to-buy and debt consolidation), not just to sale and rent back (SRB). One respondent would like bridging loans included in this group.
- 117.** A number of respondents pointed out that if a customer does not wish to proceed with the product being recommended, they may be simply rejecting a small part of the recommendation and not necessarily rejecting the advice. A review of products and further conversation with the adviser is likely to lead to the recommendation being adjusted, rather than the advice rejected. It is therefore very unlikely for customers to want to proceed on a rejected advice basis.

### Our response

Overall, we are proceeding with the proposal to allow vulnerable customers to reject the advice given (unless they are SRB customers).

We recognise that the customer may not reject the advice in its entirety and it is our intention to allow the firm to amend the product or products presented to the customer in light of their preferences, where appropriate. This has been reflected in the final rules. We accept that the number of instances where the customer may entirely reject the advice may be low, but we believe it is important to retain this option.

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

- 118.** Almost all respondents agreed that levels of execution-only sales should be closely monitored. However, many respondents felt that it would be difficult to accurately predict the amount of execution-only business they will do. Respondents suggested that we should require a risk-based approach, rather than hard limits.
- 119.** It was also suggested that firms should have a policy in place setting out the steps they will take if they exceed the expected level of execution-only sales, to ensure appropriate action is taken.
- 120.** Respondents also noted the importance of robust supervision of execution-only.

### **Our response**

We recognise that the amount of execution-only business a firm undertakes will vary from time to time. It is not our intention that firms set hard limits, but rather that they take a risk-based approach.

We agree with the suggestion that firms should also have a policy in place setting out the steps they will take if they exceed their expected levels of execution-only business. This is reflected in the final rules.

We intend to closely monitor and supervise the levels of execution-only business undertaken by firms and any unexpected spikes will be investigated further.

**Q35 (ii):** *Are there any other steps we should take to ensure that consumers are protected when purchasing on a non-interactive basis, e.g. should we place any other limitations on the types of consumers who are able to purchase online?*

- 121.** A number of respondents expressed concern that non-interactive sales channels could be used by firms to avoid or reduce the cost of giving advice (e.g. by offering better products online, which are not available in branch or by telephone).
- 122.** Several respondents suggested that we should monitor the levels of non-interactive sales via our reporting systems and take action if they appear excessive. Others suggested a requirement that online processes carry a clear warning for customers, pointing out that they are not receiving advice.

123. There was recognition that using the internet through a variety of methods is becoming more popular as a way of both obtaining information and making purchases. Respondents suggested that we should ensure regulation does not stifle innovation or technological advances that benefit customers.

### Our response

Our rules requiring the customer to be made aware of the consequences of proceeding on an execution-only basis apply equally to online sales.

We recognise that some firms and customers may try to circumvent our rules, which is a major concern for us. Our final rules prohibit execution-only channels being promoted over advice channels and all firms are required to monitor levels of execution-only business.

Firms will need to consider how their products are made available to ensure compliance with our rules.

## Disclosure

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

124. The majority of respondents agreed with our approach. The importance of there being transparency in what the firm's fee would be was considered important.
125. Respondents also welcomed CP11/31 clarifying that, when the firm's remuneration is disclosed, this need not include the individual remuneration of sales staff.

### Our response

We are proceeding with our proposal to specify how non-flat fees are disclosed.

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

126. Most respondents had no objections to our approach to bring out key messages about a firm's service in a clear and prominent manner. However, many also felt there was a need for the information to be given in writing – with firms wanting to have a record that they had told customers these messages. One respondent considered that standard documents were helpful when it comes to teaching customers about comparing services.
127. There were mixed views on the guidance we provided in relation to how compliance with oral disclosure requirements could be evidenced (e.g. by including it in staff training, inserting prompts into sales systems). Some respondents were reassured by this. However, others did not feel that compliance could be demonstrated in this way and thought the solution was to require firms to give the consumers the information in a written form.
128. Some respondents considered that there should also be disclosure about whether a firm gives advice or not. There were also calls for reassurance that firms could specifically tell customers that they offer an execution-only service as well as an advised service without breaching our rules.

### Our response

We are proceeding with our proposals to require the key messages about a firm's product range and remuneration to be given clearly and prominently.

We understand that many firms will want to continue to give customers written information about their service so there is a record that the customer has received the messages. We are not seeking to prevent firms from doing this and we have updated the combined Initial Disclosure Document (IDD) in our Handbook to help firms who want to take the option of also giving information in written form (and those required to do so because the sale is a distance contract). This can be used by firms offering mortgages and other products or firms just offering mortgages. We will also retain the tool on our website that helps firms build their own mortgage IDD.

However, we do not want to require firms to give information in written form (for sales that are not distance contracts). Our consumer research has demonstrated that customers tend not to use the IDD<sup>9</sup>, so we do not see a customer benefit in keeping it or any other similar document as a requirement.

In response to comments that we should require firms to tell the customer whether they provide advice or not, we did not see the need for such a disclosure because, under our reforms, most sales will be advised. Where it is an execution-only sale, the firm must inform the customer of the details and consequences of taking that particular sales route.

<sup>9</sup> Disclosure in the prime mortgage market – Research report, Illuminas, (December 2008): [www.fsa.gov.uk/pubs/consumer-research/cpr81.pdf](http://www.fsa.gov.uk/pubs/consumer-research/cpr81.pdf) and Mortgage effectiveness review – Stage 2 report, (March 2008): [www.fsa.gov.uk/pubs/other/MER2\\_report.pdf](http://www.fsa.gov.uk/pubs/other/MER2_report.pdf)

There is nothing in our rules to prevent firms from telling customers that they offer both an execution-only service and an advised service. However, firms will need to keep in mind that the execution-only route is only available in specified circumstances, and that under rule 4.8A.5R, a firm must not do anything that specifically encourages a customer to opt-out of or reject advice. The simple act of informing the customer that the firm offers some products on an execution-only basis would not be considered to be encouraging them down this route.

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

- 129.** The majority of respondents supported keeping the combined IDD template so firms can use it if they want to.

### Our response

We asked this question to gauge the ongoing usefulness to mortgage firms of having the combined IDD in our Handbook. It will no longer be compulsory to use the combined IDD given that we are not requiring messages about a firm's service to be given in writing (other than for sales that are distance contracts).<sup>10</sup> Given the positive response we received from firms regarding the combined IDD, we have updated it in the Handbook.

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

- 130.** A majority of respondents considered our revised approach to disclosure about a firm's product range to be the correct one. They agreed that a simple explanation that could be tailored to the situation and the market is more likely to be understood by customers than a label.
- 131.** Those respondents who disagreed noted that there are risks that firms will use the flexibility in our approach to misrepresent their service or that customers could be confused by seeing explanations in multiple formats.

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<sup>10</sup> We have retained requirements for firms to provide specified information in a durable medium where this is required under the Distance Marketing Directive.

132. Some respondents made suggestions to add to our approach. These included: having standards for what it means to be a ‘whole of market’ firm; requiring firms to explain if they use a panel for their product range; providing more specific guidance on what lenders should say; and not allowing the term ‘adviser’ to be used for non-advisory staff.

### Our response

We are proceeding with our proposals on describing a firm’s product range, given the positive response. This includes the proposed guidance on when a firm can describe its service as being ‘unlimited’, including when a panel is used. Our approach is intended to be equally applicable to lenders and intermediaries and where lenders only offer their own products, they can simply state this (using one of the relevant examples we provide if they wish).

While allowing flexibility, our approach does not allow firms to describe their product ranges in a misleading or unclear way. (See MCOB 4.4A.7G).

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

133. The majority of respondents agreed with our changes to the product disclosure rules. It was acknowledged that the reduced trigger points for providing Key Facts Illustrations (KFIs) would help to prevent customers from being overloaded with information. Respondents also welcomed the additional flexibility to provide customers with specific product information outside of the KFI.
134. A few respondents took the opportunity in response to this question to note their explicit support for removing from CP11/31 the proposal consulted on in CP10/28 that would have required two KFIs to be given where fees may be rolled up into a loan.

### Our response

We are proceeding with our changes to the product disclosure rules in light of the positive feedback on this approach. We have made some small adjustments to the rules consulted on in CP11/31 (see Annex 2). This is to provide trigger points, within the contract variation execution-only sales route and the tailored execution-only sales route for high net worth mortgage customers and business borrowers, for when a KFI is given and when a customer has to be told they can request a KFI.

**Q41:** *Do you have any comments on the draft rules on distribution and disclosure as set out in the draft Mortgage Market Review (Conduct of Business) Instrument 2012 at Appendix 1?*

- 135.** A significant number of respondents used this question to highlight their concerns with the definition of advice and how our proposals work within the context of the Perimeter Guidance (PERG). The boundary between advice and information is explained in Chapter 2. The advice process and other issues raised by respondents are summarised below.

### **Consumer choice**

- 136.** We received strong feedback from a consumer representative, lenders and their trade bodies that customers should retain the ability to choose the service they receive. They did not think that customers should be forced to receive advice when speaking to an adviser. Some respondents called for the non-advised sale process to remain and others called for execution-only to be opened more widely.

### **Our response**

In CP10/28, we consulted on proposals to strengthen sales standards by requiring an assessment of appropriateness for non-advised sales. The vast majority of respondents to that consultation supported those proposals, with many confirming that they already included an appropriateness check as part of their non-advised sale process.

Given that determining appropriateness lies at the heart of giving advice, we viewed our proposals in CP11/31 to require all interactive sales to be advised, as not being a substantive change. We expected the major concern for firms to be the costs of ensuring that staff were suitably qualified to provide advice. However, the feedback suggests that not only have firms interpreted our proposals as changing the scope of advice (which is clarified in Chapter 2), they have also interpreted the advice process as being much wider than we intend it to be.

Lenders suggested the requirement to provide advice could add over an hour to the sales process, increasing costs to the firm and possibly disengaging customers from the process. This is not our intention and in our view the differences between the two sales processes in terms of time and the steps involved will be minimal.

#### ***The advice process***

Our new proposals do not change the process that firms can follow. The current non-advised sale process requires the firm to script any questions it asks about

the customer's needs and circumstances. This enables the firm to provide the customer with one or more products, from which they are left to make their own choice. Under the current approach, if the firm goes one step further and makes the choice for the customer (i.e. a personal recommendation), it becomes an advised sale.

We are proposing that firms ask questions (that can be scripted) in all interactive sales, about the customer's needs and circumstances, to ensure they shortlist suitable products (as they may well have done under the non-advised sales process currently). The difference is that our advised sales standards will apply.

Staff will need to be appropriately qualified, which may have increased costs for some firms. However, in CP10/28, we had already proposed that all mortgage sellers should be appropriately qualified and this was supported by the majority of respondents. The proposals in CP11/31 did not fundamentally alter this.

We appreciate that some firms will be affected by our proposals more than others, particularly if they do not have an advised sale process currently and do not consider appropriateness as part of their non-advised sale. However, we believe that the overall benefit to customers outweighs the costs to firms.

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### *Small lenders with a limited product range*

137. A number of small building societies and their trade association did not think it would be possible to give advice where they only offer one product, as they would only be assessing whether the customer met their eligibility criteria.
138. Others were concerned that only offering a limited product range (e.g. only variable rate products) would mean they would have to advise the customer to purchase a mortgage from another firm.

### **Our response**

PERG 4.6.7G sets out the position where the lender only offers a single product. In this instance, the lender would inevitably be steering the customer towards a particular product, therefore this would be advice.

Lenders, who offer a limited product range, should never offer the 'least worst' product. This has always been the case under our rules. If a fixed rate would be appropriate for the customer, based on their needs and circumstances, the lender would be in breach of our existing rules by only offering a variable rate product.

There is no requirement for the firm to advise on products offered by other firms.

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### *Scope of advice*

139. One trade body questioned our overall approach to advice and criticised it for being too product focused. Instead their preference would be for the advising and selling process to be focused on holistic financial advice and/or information to ensure the mortgage is appropriate.

#### **Our response**

The Regulated Activities Order<sup>11</sup> (RAO) defines regulated mortgage advice as advice on the merits of the customer entering into (or varying the terms of) a particular mortgage contract. Our proposals are in line with the RAO.

### **Arrears management**

140. CP11/31 set out a number of proposals relating to arrears management. These included further clarification on how firms should be calculating arrears charges, limiting the number of times direct debits can be presented each month, widening the arrears charges rules to cover all payment shortfalls and the removal of the rule allowing firms to remove borrowers from concessionary interest rates if they go into payment shortfall.
141. Overall there was support for the arrears management proposals, although concerns were raised about specific aspects of the arrears management rules.

**Q42:** *Do you have any comments on the proposed policy approach on the calculation of payment shortfall amounts?*

142. Most respondents were in favour of the proposals. The remaining respondents were broadly supportive of the general policy intention, but had concerns about specific aspects of the proposals.
143. Concerns included the possibility that executive staff at larger firms, with high arrears levels, or who are running down a 'backbook'<sup>12</sup>, may be involved in the day-to-day management of arrears or that executive staff may spend time reviewing and agreeing day-to-day arrears business processes and direction, and that this was a reasonable cost to recover through payment shortfall charges.
144. Certain respondents wanted more clarification on what arrears calculations are required to be performed and how often these should be reviewed. It was argued that we should not create an overly complicated solution.

<sup>11</sup> *The Financial Services and Markets Act 2000 (Regulated Activities) Order 2001*: [www.legislation.gov.uk/ukxi/2001/544/contents/made](http://www.legislation.gov.uk/ukxi/2001/544/contents/made)

<sup>12</sup> For example, a lender may not be actively lending and may be managing a tranche of existing mortgages until the borrowers remortgage or the tranche is sold on.

## Our response

We are proceeding with the proposed arrears charges rules in CP11/31.

For executive staff costs, the proposed rules already require these costs to be included in arrears charges only if they are objectively justifiable and relate to the day-to-day management of customers in payment shortfall. We would expect this to apply only in relation to very small firms, where executive staff may be justifiably involved in the management of individual cases. Executive staff costs relating to company strategy, including arrears strategy, are not costs that should be recovered through arrears charges, as they relate to the general oversight of the firm and are not sufficiently related to the day-to-day management of arrears cases. This includes executive staff costs relating to developing arrears management policy. More generally, we consider that, while it may be beneficial to profile and analyse borrower groups who are not in arrears, these costs are not an additional administration cost of borrowers in arrears.

We do not think it is appropriate to set out compliant and non-compliant arrears charges calculation methods.

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

145. Most respondents were in favour of the proposals, although there were specific concerns raised about the rules. Consumer representatives continued to recommend that firms should be allowed to charge for only one missed payment.
146. Certain respondents noted that reviewing and replacing direct debit as a mode of payment could generate an increase in the use of alternative payment methods (e.g. debit card payments) and possibly create more circumstances for missed payments. These respondents considered that this may be detrimental to the borrowers and increase costs to firms.
147. Some respondents queried if the proposed rules would require firms to suspend missed direct debit fees across two months even if payments are subsequently collected through direct debits in each of those months. They also questioned if the draft rules will require firms to refund missed direct debit fees levied in month one once a further payment is missed in month two.
148. Several respondents sought confirmation from us that missed direct debit charges for customers in arrears constitute charges covered by MCOB 12.4.

## Our response

We are proceeding with the proposals.

We consider that it is reasonable for lenders to request a second direct debit in a month where the first request fails. The rules prevent lenders from presenting direct debit requests more than twice a month for more than two months without considering whether the payment method remains appropriate.

While there is potential for the rules to result in an increased use of other payment methods, we do not consider that this is a sufficient reason not to require lenders to consider the appropriateness of direct debit as a payment method where there have been failed direct debit requests in each of the last two months.

MCOB13.3.1A R requires that where firms are considering whether the method of payment remains suitable, the firm may not pass on any costs to the customer which were incurred as a consequence of presenting direct debit requests during 'this period of consideration'. This does not mean that charges for missed payments in the whole two-month period need to be refunded, it merely means that while the lender is considering the appropriateness of the payment method, costs incurred as a result of presenting direct debits should not be charged to the customer.

Charges for missed direct debit payments to borrowers in payment shortfall are covered by the arrears rules in MCOB 12.4.

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

- 149.** Most respondents were in favour of the proposal. However, some respondents raised important points about the potential impact of the rules on the record keeping requirements.
- 150.** Respondents suggested that, for record keeping requirements, there should be a common sense and proportionate approach to small payment shortfalls or short-term payment shortfalls. Respondents were concerned about the requirement to record all telephone conversations where the borrower was technically in payment shortfall, but was not in arrears or payment difficulty.
- 151.** Certain respondents noted an inconsistency between the proposed rules in CP11/31 and the Forbearance and Impairment Provisions guidance, which allows for the automatic capitalisation of small payment shortfalls subject to certain conditions. The draft rules in CP11/31 prevent automatic capitalisation of all payment shortfalls.

## Our response

We are proceeding with the proposed approach, subject to the following modifications.

The main purpose of widening MCOB 12.4 and 13.3 to cover payment shortfalls and not just arrears was to prevent firms front loading arrears charges. The payment shortfall definition in CP11/31 captures shortfalls against what the lender is expecting to receive within a given month.

In CP11/31 we proposed record keeping requirements under MCOB 13.3.9 requiring firms to make and retain an adequate record of its dealings with a customer whose account has a payment shortfall. This record would include all telephone conversations between the firm and the customer which discuss the sums due. Our intention is not to capture all conversations with customers who technically have a payment shortfall. Our intent is only to capture the meaningful contacts with customers in financial difficulty. To achieve this we have amended MCOB 13.3.9 R (1), so that all telephone conversations discussing any amount that is in arrears or any amount attracting payment shortfall charges need to be recorded. This will prevent a situation where firms are obliged to record all telephone calls discussing immaterial payment shortfalls (unless the shortfall is attracting a charge) or where the payment shortfall occurs where the customer is not in financial difficulty.

It is also not necessary to capture parts of telephone calls that are not relevant to accounts in arrears or subject to payment shortfall charges. For example, if a borrower, with an account in arrears, phones a lender's branch to discuss another account or a matter other than the payment shortfall, then this part of the call would not need to be recorded. However, if the telephone call moved onto a discussion about the arrears, we would expect the customer to be transferred to the collections department and the conversation would be recorded.

We have made an amendment to MCOB 13.3.4AR and MCOB 13.3.4AA to align the rules with the Forbearance and Impairment Provisions guidance.<sup>13</sup> The rule change will allow firms to automatically capitalise small payment shortfall amounts provided the combined effect of the capitalisation and previous automatic capitalisations are immaterial (see MCOB 13.3.4AA).

We have also made a small amendment to the definition of 'payment shortfall' so that it more clearly reflects the policy intention, i.e. to prevent firms from front loading arrears charges on payment shortfalls that occur during the term.

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<sup>13</sup> FG11/15: *Forbearance and Impairment Provisions – 'Mortgages'*, (October 2011): [www.fsa.gov.uk/library/policy/final\\_guides/2011/fg11\\_15.shtml](http://www.fsa.gov.uk/library/policy/final_guides/2011/fg11_15.shtml) (page 34)

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

- 152.** A significant majority of respondents were in favour of the proposal. Of the respondents who were neutral or not in favour, several identified that, while they never removed customers in arrears from concessionary rates, they could see the benefit of being able to do so. This could be to act as an incentive to borrowers or where borrowers are in serious arrears and refuse to engage with the firm.
- 153.** A few respondents wanted more clarification on what qualifies as a concessionary rate and what constitutes a material breach of a mortgage contract.

### Our response

We are proceeding with our proposed approach. We do not accept that the removal of concessionary rates for borrowers in serious arrears could be appropriate. This position is supported by the current market practice of the vast majority of lenders and by most respondents to CP11/31.

Concessionary rates covered by MCOB 2.6A-1 R will include all initial mortgage product rates included in the mortgage contract, including lifetime tracker products, stepped products, capped products, fixed rate products, discounted variable products and other products with concessionary rates. The rule prevents lenders artificially increasing borrowers' interest rates because of a payment shortfall. Examples of material non-payment shortfall-related breaches of mortgage contracts that could justify the removal of concessionary rates may include borrowers letting out their property without the authorisation of the lender, or borrowers providing deliberately misleading information in their mortgage application.

**Q46:** *Do you have any comments on the draft rules on arrears management as set out in the draft Mortgage Market Review (Conduct of Business) Instrument 2012 at Appendix 1?*

- 154.** Many respondents were comfortable with the draft arrears management rules, and although there were specific concerns raised, most of these were dealt with under the feedback to Q42 to Q45.
- 155.** It was noted by one lender that it is common for some lenders to outsource the collection of payment shortfalls to external and specialist collection agencies, and that some agencies

operate a fee structure based on receiving a percentage of the loan collected. The lender argued that MCOB 12.4.8 R should allow lenders to charge an arrears charge based on a percentage of the loan.

156. One respondent noted an inconsistency between MCOB 12.4.1A E – where a payment shortfall charge, for a customer adhering to an arrangement to pay, may be relied on as tending to show a contravention of MCOB 12.4.1 R – and MCOB 13.5.2 G (3), where firms must provide a statement if the payment shortfall is attracting charges where there is an arrangement to pay.

### Our response

We do not propose to amend MCOB 12.4.8R. It is a commercial decision for lenders whether they employ specialist collection agencies, but irrespective of the contractual arrangements in place between the lender and the agency, customers must not be charged arrears charges that are calculated as a percentage of the payment shortfall.

We have deleted MCOB 13.5.2 G (3). We do not expect firms to impose a payment shortfall charge where a customer is adhering to an arrangement to pay under MCOB 12.4.1A E and therefore there is no need for a firm to send the customer a written statement of those charges.

## Prudential reform

### *Impact of Basel III*

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

157. A majority of respondents agreed with us that the Basel III requirements for banks are unsuited to meeting the objectives of the MMR, specifically in deterring high-risk lending (and that additional conduct requirements are therefore necessary).
158. However, while respondents generally agreed that the prime vehicle for meeting the MMR objective of consumer protection should be through conduct measures, it was also acknowledged that prudential requirements designed to ensure that firms hold sufficient risk-based capital would impact on and help deter higher-risk lending. Overall, the responses highlighted that there is a complex interaction between conduct

considerations and additional prudential tools introduced under Basel III and the macro-prudential overlay.

### **Our response**

We consider it inappropriate to simply rely on the future prudential reforms in Basel III to meet the objectives of the MMR. The additional reforms on the conduct of business side discussed in Part 1 of CP11/31 are required to reduce the risk of consumer detriment in the mortgage market due to relaxed lending standards and over-rapid credit expansion in a boom period.

## **Non-deposit taking mortgage lenders**

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

159. Respondents' feedback addressed the following points:

- risk-based framework;
- credit risk;
- securitisation and other credit risk mitigation techniques;
- operational risk; and
- limits denominated in Euros.

### **Risk-based framework**

160. Respondents in principle supported risk-based capital requirements. However, they emphasised key differences between the simpler business models of non-deposit taking mortgage lenders (non-banks) and those more complex business models of banks and building societies.
161. In particular they have no depositors, a plain vanilla balance sheet and they do not perform a maturity transformation function, so they are not subject to liquidity risk in the same way.
162. Respondents agreed that achieving a level playing field across all lenders was a key deliverable. However, as there are some key differences in the prudential risks of each

business model, it would not be proportionate to simply import all of the BIPRU<sup>14</sup> prudential requirements into MIPRU.<sup>15</sup>

163. To help navigate the sub-set of BIPRU requirements that will apply to MIPRU firms, respondents proposed copying these directly into MIPRU rather than rely on cross-referencing to BIPRU. They also suggested that the requirements should be drafted into ‘plainer English’. The result would be to reduce the compliance cost for firms who would otherwise have to navigate large volumes of complex BIPRU requirements, much of which will not apply.

### Our response

In principle, we are sympathetic to copying across the requirements into MIPRU and where possible redrafting the text to improve clarity. In practice this is a substantial piece of work and one with significant risks attached.

BIPRU represents part of the UK’s domestic transposition of the EU Capital Requirements Directive, which is a complex piece of legislation, with many interactions. Any substantial redrafting and simplification of the text, especially on a stand-alone basis (in MIPRU), would need to consider carefully, not only the purpose and intent of each individual requirement, but also their interactions to avoid unintended consequences, errors or important omissions.

On balance, therefore, we will proceed with implementing the risk-based prudential requirements for non-bank lenders through cross-referencing the relevant BIPRU rules within MIPRU, as part of the overall package of MMR reforms.

However, at the same time we will continue to explore whether and how the same policy requirements could be delivered through a simplified, stand-alone set of rules in MIPRU (without cross-reference) in a way that makes them more accessible to non-bank lenders. Detailed consultation would be necessary for any such revision. The objective of such work would be to help make the rules more accessible and not to change the impact or application of the risk-based capital requirements derived from applying the relevant BIPRU rules as consulted on in CP11/31. So until then, firms should use the navigation tables provided for securitisation (see MIPRU 4.2B.4) and credit risk mitigation (see MIPRU 4.2C.4) to help them understand the application of the relevant parts of BIPRU and to prepare for implementation of the requirements.

14 Prudential sourcebook for Banks, Building Societies and Investment Firms: <http://fsahandbook.info/FSA/html/handbook/BIPRU>

15 Prudential sourcebook for Mortgage and Home Finance Firms, and Insurance Intermediaries: <http://fsahandbook.info/FSA/html/handbook/MIPRU>

## Credit risk

164. One respondent proposed further minor simplifications of the standardised approach, but most argued for greater complexity by allowing non-banks to use the Internal Ratings Based approach (IRB models) for calculating credit risk.

### Our response

The standards for IRB model recognition are set out in BIPRU Chapter 4 and the requirements are complex, extremely robust and impose correspondingly high requirements on firms. It is therefore important that firms are aware of how resource intensive, both in terms of time and money, the model recognition process can be for lenders. Added to this are the significant resources required to continue meeting the necessary standards after approval. Furthermore, any material failure in this respect is likely to result in the immediate removal of model recognition and the application of the standardised approach, which would likely result in significantly increased capital requirements.

The cost of allowing IRB models is expected to be greater complexity, due to:

- a. more approaches for calculating credit risk requirements;
- b. more complex methods for calculating credit risk requirements;
- c. likelihood of industry demand for corresponding IRB sections of BIPRU 9 to be added to MIPRU; and
- d. resource intensive model recognition process and ongoing compliance supported by specialist and highly expert staff both at the FSA and firms.

Other considerations include the possible benefits for the non-banks whose lending business model is based on the originate-and-distribute model. This means that, beyond the warehousing period, most of the risk will likely be mitigated by techniques such as securitisation (subject to holding any element of risk retention<sup>16</sup>). The net credit risk position should be such that any potential reduction in the capital required is immaterial enough that it makes maintaining an IRB model less cost-effective.

In CP11/31 we decided not to allow the IRB model approach to calculate the credit risk requirement. Our general experience of model recognition and the challenges faced by firms in showing that they meet the required standards, led us to conclude that this would not be a viable solution for non-bank lenders. This decision should also be seen in the context of deciding not to apply any additional capital requirements under a 'Pillar 2' approach.

<sup>16</sup> Under Article 122a of the Capital Requirements Directive (CRD), in order for EU banks to be able to invest in a securitisation (whether in the primary or secondary markets) the originator or original lender – which would include a non-bank – must retain a minimum 5% net economic interest.

Despite this, we are willing to discuss on a case-by-case basis, the necessary conditions that might allow an individual firm to consider whether or not it could make a future application to operate the IRB approach to mortgage credit risk (and if so, how to implement it, for example through the waiver process).

165. One respondent asked for clarification of the loan-to-value (LTV) calculation for shared ownership lending. In particular where, in the event of default, the lender had a priority claim over the whole property.

### Our response

The LTV calculation will be a question of fact based on the contractual terms governing the loan. To illustrate the point for shared ownership lending, a £100,000 property is jointly owned by Party A (80%) and Party B (20%) and Party B has a £5,000 deposit, so borrows £15,000. If Party B defaults and the lender to Party B has a first claim on the whole property (i.e. ahead of Party A) and has the unfettered right to immediately sell the property, then the LTV is 15%. If the lender's claim is limited to the percentage of the property lent against (i.e. 20%) then the LTV is 75%.

## Securitisation and other credit risk mitigation techniques

166. All respondents commented on the complexity of the BIPRU Chapter 9 Securitisation requirements and the difficulty in navigating them, particularly as only part of BIPRU 9 is relevant to non-banks. To address this, respondents proposed copying across just the relevant sections into MIPRU and redrafting them so that they are clearer. One respondent proposed retaining the cross-references to BIPRU and supplementing them by providing guidance on how to identify and navigate the relevant sections.
167. All respondents argued that MIPRU should allow forms of credit risk mitigation other than securitisation, as set out in BIPRU Chapter 5.

### Our response

In the draft Handbook text (section 4.2C Appendix 1) we said:

- a. Section 4.2B deals with securitisation and includes a navigational table (see MIPRU 4.2B.4) which cross-references back to BIPRU 9.
- b. Section 4.2C deals with credit risk mitigation and includes a navigational table (see MIPRU 4.2C.4) which cross-references back to BIPRU 5.

Section 4.2C permits other forms of credit risk mitigation.

We agree that a standalone version of MIPRU would remove the need for cross-referencing to other parts of the Handbook. We will consider this issue as a separate exercise. Meanwhile, we will continue with cross-referencing to the source material and use the Tables 4.2B.4 and 4.2C.4 to navigate between MIPRU and BIPRU.

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### Operational risk

168. We proposed that there would not be an operational risk requirement. Respondents supported this approach.

#### Our response

We are not imposing an operational risk requirement.

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### Limits denominated in euros

169. Respondents challenged setting limits in euros when the firm's business was wholly UK-based.

#### Our response

The particular references are in BIPRU 3.2.10R and 3.2.19G in respect of the retail exposure class. We agree that applying euros limits to a business with predominately sterling assets and liabilities is not proportionate. We will therefore restate the limit in sterling. The €/£ exchange rate has varied significantly since the time the limits were first set. The limits have also not been updated to capture inflation. To avoid spurious accuracy we have decided to simply translate the limits so that the €1m limits become £1m limits.

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

170. One respondent argued that non-banks had the potential to destabilise market confidence so 25% or 30% of eligible capital should be share capital and reserves less intangible assets (rather than the 20% proposed).

171. Other respondents argued that there should be no minimum share capital and reserves requirement (or in one respondent's view, at least where subordinated loans were of a maturity of at least 12 months longer than the corresponding lending to customers). Their main argument was that subordinated loans, which provide a form of 'gone-concern' capital that is effective where a firm winds down its operations rather than continuing, should be adequate for this business model and better suited to the typical sources of capital and funding that are available in this market.

### Our response

These lenders are significant market participants and they can cause significant consumer detriment. Our view is that we should increase the quality and quantity of capital required for these lenders to increase their loss absorbency, which was a key failing across the market during the crisis. Holding a minimum amount of share capital and reserves should help a firm absorb losses while either continuing to trade or to help prepare for a more orderly wind-down and withdrawal from the market.

So we will retain the requirement that at least 20% of eligible capital should be share capital and reserves less intangible assets.

We have removed the proposed new rules 4.4.1R(3) and (4) from the Instrument as they are not necessary given that the requirement is set out in rule 4.4.8R.

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

172. Respondents agreed with the proposed qualitative liquidity regime.

### Our response:

We are proceeding with the proposed policy as set out in the consultation.

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

173. Respondents agreed in principle that the policy should apply for 'new lending'.
174. Their main concern, however, was the definition of 'new lending' for existing borrowers. Respondents were unanimous in their view that forbearance should not be deemed new

lending. There was broad agreement that the new requirements should only apply to the increase and not the whole loan.

175. Some respondents argued that additional borrowing should not include further advances on existing mortgages or facilities including lifetime mortgages (or equity release), in particular where a firm is closed to new business. One respondent suggested that ongoing monitoring of future drawdowns would be administratively burdensome and another suggested excluding further advances under 10% of existing borrowing.

### Our response

Firms that conduct new lending will be subject to the new MIPRU prudential requirements. Whereas requirements such as eligible capital and the qualitative liquidity regime will apply to the firm as a whole, the BIPRU credit risk capital requirements (with the risk weight determined by factors such as the LTV) will apply only to new lending.

New lending includes the following:

- Any payment of new funds by the firm to the borrower, directly or indirectly, including a future drawdown on existing facilities, on the basis that such facilities should be kept under review; and
- Any change to the contractual terms to mitigate the risk of lenders rolling-over loans and passing it off as old lending. The only exception being if there has been forbearance, with expected losses fully provided for.

Portable loans where the borrower can change the collateral (e.g. move house) is not deemed new lending.

Firms that are closed to new business (i.e. in run-off) should not be undertaking new lending. The new requirements will not apply to such firms. They will be excluded from the proposed limit in the eligible capital calculation and the liquidity regime by being subject to a restriction to their permission preventing them from undertaking new lending.

We regard the use of a *de minimis* limit, such as 10% of existing borrowing, as an unnecessary complication and it would create tiering of new lending (i.e. above and below the 10% limit). We consider that the routine monitoring of future drawdowns is required to meet our systems and control requirements.

We have expanded Rule MIPRU 4.2A.5R to clarify that where a loan is increased, the new capital requirement only applies to the increase and not the whole loan. We have also introduced additional guidance in MIPRU 4.2A.5AG to confirm that the new capital requirement does not apply to any loans that are acquired by a firm after the implementation date if they had been made before that date; and to arrangements made as a result of forbearance procedures.

**Q52:** *Do you have any comments on the draft rules set out in the MIPRU instrument at Appendix 1? Do you think the rules reflect the stated policy intention?*

176. The points raised by respondents have been addressed at Q48 to Q51.

### **Our response**

We have amended the drafting of Rule MIPRU 4.2.23R(2) (2)(b)(ii) to clarify that the 1% charge is not applied to assets that have already been subject to a risk-based charge under the requirements of MIPRU 4.2A. To achieve this result, the reference in the rule is to items 'subject to' MIPRU 4.2A.4R rather than 'excluded' from it.

## **Equity release**

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

177. The majority of respondents agreed with the proposed read-across or had no specific comments in reply to this question.

### **Our response**

We will proceed with the read-across in our final rules. Some minor changes to rules applying to equity release are shown in the table in Annex 2.

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

178. The industry already operates as if the equity release market is a single market, so there was strong support for this proposal, with no objections.

### Our response

We are proceeding with the proposals to treat equity release as a single relevant market.

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

- 179.** The majority of respondents agree with our proposals. Several respondents did not agree with allowing customers to reject advice, as simply having the product details and a property value does not demonstrate that the customer fully understands the implications.

### Our response

Equity release customers cannot opt-out of advice. However, we do not want to prevent equity release customers from having the freedom to make their own choices. To provide what we believe is the right level of protection for equity release customers, they will all need to go through an advised sales process first. This will ensure that they have considered the implications of equity release with a qualified adviser before they are able to reject the advice and make their own choice. Because of the nature of the product and the standards imposed by the industry trade body, we would not expect many equity release sales to be on an execution-only basis.

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

- 180.** Around half of the respondents saw no need for any other tailoring. The main suggestions from the remaining responses were:

#### Roll-up of fees and charges

- 181.** Concern was raised over the read-across of our proposal that firms must offer customers a choice of whether to roll-up fees into the loan and record the customer's positive election. Equity release customers are typically releasing equity because they do not have funds available elsewhere and are unlikely to be able to pay any upfront fees. Having to offer a choice would mean unnecessary and costly changes to systems, such as producing illustrations.

### Existing customers

182. Several respondents felt that existing equity release customers should have access to certain types of transaction without the need for advice. Examples given included pre-agreed increments or drawdown facilities within lifetime mortgages; further releases to home reversion plans; and moving home without increasing the borrowing.
183. Respondents pointed out that customers are likely to have already received advice about access to additional funds or drawdown facilities when they first entered into the contract. They also noted that the amounts involved are often quite small, which means that the cost of obtaining advice could be disproportionate to the benefit gained by the customer. Finally, drawdown facilities give quick and easy access to funds. Having to go through an advice process could considerably slow this down.

#### Our response:

##### Roll-up of fees and charges

We agree with the feedback and have changed the application of the rules on rolling-up fees or charges into the loan so that, where the lifetime mortgage is structured on an interest roll-up basis from the outset, they do not apply (MCOB 8.3.1R (1)(c)). Where regular payments are involved, the rules would apply (MCOB 4.4A).

##### Existing customers

In light of the feedback, we have amended our approach to contract variations and will not require advice to be given if the total sum outstanding does not increase. Our rules do not require advice to be given where the customer is drawing down from an agreed facility, which was part of the original product recommendation. However, where the total sum outstanding will increase, for example where there is a new agreement to advance further funds, advice would be required. Our general approach to contract variations is discussed in Chapter 2.

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

184. No substantial comments were made and most respondents were in favour of our overall approach to reading across the MMR to equity release.

#### Our response

We are proceeding with the read-across of the MMR to the equity release market.

## Home Purchase Plans

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

**185.** No substantial comments were made in reply to this question.

### Our response

We are proceeding with the read-across of the MMR to the Home Purchase Plan (HPP) market.

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

**186.** Most respondents were either supportive of our proposals or did not have any comments.

**187.** A few respondents believe HPP sales should either be on an execution-only basis, or allow customers to opt-out of advice, because providers only offer one product, which the customer is either eligible for or not. They believe advice is unlikely to be needed, or is not possible, because the customer does not have a choice.

### Our response

We have not changed the current position on advice set out in our Perimeter Guidance Manual (PERG 4.6.7 G<sup>12</sup>). This explains that if the provider offers the customer only one product, then the seller is implicitly steering the customer towards that product, and this constitutes regulated advice.

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

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

188. The majority of respondents were supportive of our overall approach to HPPs. A number had commented in response to earlier questions, so did not add any further comments here.

### Our response

We are proceeding with the tailored rules for the HPP market.

## Sale and rent back

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

189. Most respondents were either supportive of our approach or did not have any comments. A small number of respondents asked us to clarify our advice proposals, as the table we published in CP11/31 suggests advice can be rejected, while our proposals confirm that it cannot.

### Our response

We are proceeding with our proposals that all sales to SRB customers must be advised.

The table showed that we were adopting a tailored approach to execution-only for SRB. We thought this would highlight better the fact that SRB customers cannot reject advice and there is no execution-only route available.

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

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

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

190. All respondents who commented were strongly in support of the proposals.

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**Our response**

We are proceeding with our proposals for the SRB market.

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## Bridging finance

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

191. The majority of respondents agreed with the proposed definition.

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**Our response**

We are proceeding as proposed.

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

192. The majority of respondents agreed with our read-across of the affordability proposals to bridging finance.

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**Our response**

We are proceeding as proposed.

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

193. The majority of respondents agreed with our read-across. A few pointed out that it is not clear how our periodic checking requirement will apply to short-term lending. Others

commented that repayment strategies for bridging loans will differ from mainstream mortgages and this needs to be taken into account.

### Our response

Given that the loan is for 12 months or less, we do not see a need to check on the repayment strategy during the term and we have therefore changed MCOB 11.6.49R to make this clear.

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

194. Respondents were on the whole in favour of our proposals. A number pointed out that documenting every customer type and every possible exit strategy in a lending policy is not possible.
195. Concern was raised about lenders obtaining evidence of a guaranteed offer for bridging loans used for credit repair (see MCOB 11.6.53E in Appendix 1). It was felt that this was not achievable, as normal mortgage lenders will not be able guarantee an offer so far in advance. They thought this would effectively ban bridging loans from being used for credit repair purposes.

### Our response

We addressed the concern over keeping lending policies up to date with all valid repayment strategies in CP11/31.<sup>17</sup> We explained that we would allow lenders to consider all types of repayment strategy as long as they operated within a framework of appropriate controls, set out in their lending policy.

Regarding credit repair, we continue to believe that it is highly speculative for a customer to take out a bridging loan and expect their credit status to be repaired sufficiently to enable them to refinance to a mainstream mortgage. So we have retained the evidential provision MCOB 11.6.53E. Therefore, accepting credit repair as a repayment strategy, without evidence of a guaranteed offer for a longer-term contract, would tend to show a breach of MCOB 11.6.41R(1).

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

<sup>17</sup> See paragraph 4.45 to 4.49 in CP11/31.

196. Almost all respondents agreed with our proposals. A few were concerned that, as the majority of bridging loans are taken out on a retained interest basis, extending the term would involve borrowing more money. They felt that it is not clear from our proposals whether this additional borrowing would be a sale for which advice was required.
197. Some firms involved in HNW and business lending were concerned that these proposals would apply to some HNW and business loans (particularly secured overdrafts, which often have an assumed term of 12 months). They felt this would be overly onerous for these types of lending.

### Our response

We recognise that, where the loan is taken on a retained interest basis, an additional amount is added to the loan when the term is extended. However, this extra amount is interest on the loan that the customer has already received and is not additional borrowing.

We have explained in Chapter 2 that, as long as the customer is not taking out additional borrowing when varying a mortgage contract, then advice does not need to be given. When the term of a bridging loan is extended without any additional borrowing, we regard this as a variation that benefits from the exception in MCOB 4.8A.10R.

We have amended MCOB 11.6.55R so that it does not apply to secured overdrafts for HNW mortgage customers or loans made solely for a business purpose. However, as set out in MCOB 11.6.56G, we will expect firms to act honestly, fairly and professionally, in accordance with the best interests of their customer, when they extend such loans.

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

198. Most respondents had nothing to add and several expressed their support for the enhanced consumer protection that our proposals would bring.

### Our response

We are proceeding with our proposals.

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

199. Most respondents agreed with our proposal. A few were concerned that describing their service could become complicated or impossible for intermediaries, especially if they have to name all of the lenders, as some lenders will not be known to all and there is no comprehensive list. They suggest a higher level explanation of their service.

### **Our response**

We are proceeding as proposed. The intermediary can say that they offer products from a comprehensive range of providers as long as they can demonstrate access to a sufficiently representative number. If they use a limited panel of lenders, we would expect them to know their names.

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

200. Responses were polarised. Those not directly involved with the sector, such as mainstream mortgage lenders and trade bodies, were generally content with the proposals. However, those directly involved argued strongly that the proposal to apply BIPRU requirements to these generally smaller-sized firms is not proportionate and for many firms would mean a significant increase in the capital required. The preference by providers of capital for subordinated loans means that firms' ability to raise share capital would be either very restricted or very expensive.
201. They argued that there have been few failures and the market remained strong in the downturn, meaning there is no significant risk to be addressed by more complex and costly requirements.
202. There is also concern that the rules are far too complicated and smaller firms would not be able to cope without specialist advice.

### **Our response**

We agree there is a risk of consumer detriment in the bridging loan sector and that the loan periods, while initially short-term, can be and are routinely rolled-over and extended. The risk-based requirements set out in BIPRU 3 determine the risk-weights based on LTV not maturity. And while it could be argued that

in some circumstances the probability of default of a short-dated loan may be lower, this does not mitigate against event risk, which can happen over a very short time. There are also other risks that are particular features of bridging finance (e.g. the inability to finance long-term and repay bridging loans) that also need to be adequately captured by the risk-weights used. Given this, and without any evidence to the contrary, the risk-weights applied under BIPRU 3 are deemed to be adequately risk-based. It should also be noted that these loans, even if short-term, should be subject to adequate ongoing review.

Our response on the navigability and complexity of the rules is also covered by Q48. Navigational tables have been included (see Tables in MIPRU 4.2B.4 and 4.2C.4) within the draft Handbook text. These cross-reference back to the source material and provide the means by which to navigate between MIPRU and BIPRU. As noted in our response to Q48, we continue to consider whether it may be possible to make the rules more accessible without changing their substance.

Consistent with our response to Q49 on eligible capital, these lenders are significant market participants and can cause significant consumer detriment. Our view is that we should therefore increase the quality and quantity of capital required for them to improve their loss absorbency, which was a key failing across the market during the financial crisis. The same arguments apply to bridging loan firms for holding a minimum amount of share capital and reserves, which should help a firm absorb losses whilst either continuing to trade or to prepare for a more orderly wind-down and withdrawal from the market. We will therefore retain the requirement that at least 20% of eligible capital should be share capital and reserves less intangible assets.

Given this, we will include bridging lenders within the scope of the new MIPRU requirements.

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

- 203.** Most respondents agreed with our summary. One trade body and several lenders are concerned that our read-across will have a detrimental impact on the bridging market. They agreed with our aim of protecting vulnerable customers, however, they asked for greater flexibility to allow for the wide variety of scenarios where bridging can be used. Suggestions included making advice mandatory for anyone in arrears or who is otherwise credit-impaired while allowing lenders to make their own risk assessments.

### Our response

We do not believe our rules prevent bridging lenders from lending in a wide variety of scenarios. We would expect firms' lending policy to reflect the nature of the market they are in.

*Q75: In addition to the proposed tailoring set out above, is any other tailoring required for the bridging finance market?*

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

204. A number of respondents commented that the draft rules did not appear to exempt bridging lenders from having to get evidence of income. Bridging loans are typically repaid on the sale of a property and there are no payments due during the term.

### Our response

In light of the feedback we have changed MCOB 11.6.59G to make this clearer.

## High net worth and business lending

205. The following sections summarise the feedback received to the questions asked in CP11/31 about high net worth (HNW) and business lending. We have included only brief responses to some of the feedback here. Further discussion of the responses and full details of our approach to HNW and business lending is set out in Chapter 4.

### Lending to high net worth customers

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

206. Most respondents recognised that HNW customers need a different regulatory approach to that proposed for the mainstream mortgage market. However, many respondents did not agree that the wealth of a customer necessarily correlates with financial capability or the

ability to make sound financial decisions – particularly where wealth is not generated by the individual concerned, e.g. if inherited or received through a windfall.

207. So, while respondents favoured a more free-market approach than would apply under the full MCOB rules, most preferred an approach where key consumer protections would still apply.

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

208. Some lenders and intermediaries favoured an elective approach, where HNW customers would be able to opt-out of certain elements of regulation. However, for practical reasons, banks engaged in this sector did not on the whole favour an optional approach. Some banks felt that discussing the disapplication of consumer protections would not be a conversation that would fit well in the wider client care ethos of many HNW relationships. They generally preferred a tailored approach, which would allow consumer protection to fit with the bespoke process offered to their HNW customers.

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

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

209. Some firms favoured disapplying the mortgage rules, particularly where the customer agrees to this (i.e. through an elective approach). But the majority of respondents, including both firms and consumer representatives, felt that some consumer protection should apply in all cases. Many suggested a minimum acceptable level of protection made up of applying the Principles (such as Principle 6 – ‘treating customers fairly’) and the rules around redress, compensation and arrears handling.
210. A few respondents commented that if a HNW customer was able to opt-out of some aspects of regulation (such as advice or the responsible lending rules), they should not expect to receive consumer protection when things go wrong.

### **Our response**

We have carefully considered the feedback received. We are adopting a tailored approach to lending to HNW customers, which recognises the characteristics of this type of lending. We explain our approach in Chapter 4.

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

- 211.** The majority of respondents agreed with the proposed net assets definition (£3m), although some larger banks favoured a lower amount. However, many respondents felt that the proposed net income threshold (£1m) was much too high. They thought that this level of income was extremely uncommon, and did not correlate to the wealth levels of customers likely to have net assets of £3m.
- 212.** Most suggestions for a more appropriate net income threshold ranged between £300,000 and £500,000. A few respondents, including some trade bodies, suggested aligning our definition with the Consumer Credit Act (CCA) definition that applies to second charge lending (income of £150,000 or net assets of £500,000), for the sake of consistency between the two regimes. Some saw gaming opportunities if we did not do this (i.e. customers fitting the CCA definition might take small first charge mortgages and top them up with large second charge mortgages, to avoid our rules).
- 213.** Many respondents questioned how the income and assets figures should be met. For example: whether net assets can include the main residence; how the requirements apply to joint applicants; and how joint assets are treated.

### Our response

In response to feedback, we have reconsidered the proposed definition of a HNW mortgage customer, and are amending it to a net income of £300,000 or net assets of £3m. At least one applicant must meet this definition in their own right. We explain more about the definition in Chapter 4.

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

- 214.** Respondents had mixed views about this proposal. They felt HNW guarantors merited a different approach to guarantors in the mainstream market. But some saw heightened risks for HNW guarantors if mortgage regulation was disapplied – given that the lending was not advanced for their benefit, but that they would still be responsible for the loan.

### Our response

We are extending our definition to include customers whose obligations are guaranteed by a person who meets the HNW criteria.

We are not disapplying our mortgage rules, but adopting a tailored approach to HNW lending. Guarantors meeting the HNW definition will be subject to the same affordability assessments as HNW mortgage customers.

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

- 215.** Many respondents (both lenders and intermediaries) saw the need for flexibility in affordability assessments for HNW customers, given that such assessments often consider the wider financial position of the customer, beyond just their income (e.g. assets and wealth available to them through structures such as trusts).
- 216.** Respondents also had concerns about the expenditure approach proposed for the mainstream market. They thought that when dealing with very wealthy customers, it is irrelevant and unnecessary to consider expenditure down to the level of utility bills.
- 217.** Therefore, most respondents thought a different approach to affordability assessments would be necessary for HNW customers, either through disapplying the affordability assessment rules, or applying some kind of tailored approach.

### **Our response**

We are applying a tailored approach to affordability assessments for HNW mortgage customers. We discuss this in more detail in Chapter 4.

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

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

- 218.** The majority of respondents were in favour of extending the tailored disclosure rules to HNW customers. However, several lenders active in the HNW market considered that, while the tailored disclosure rules will help them to some extent, some HNW mortgage products will still not fit with our disclosure requirements, and therefore the tailored approach may not greatly diminish their need for waivers to some disclosure rules. A small number of respondents felt that all rules, including disclosure rules, should be forgone for HNW lending.

219. Respondents did not express strong views about whether the tailored disclosure should be achieved through an elective approach.

### Our response

We are proceeding with the tailored approach to disclosure for HNW mortgage customers. As with the existing business lending provisions, firms can opt to apply all of the tailored disclosure provisions, or to ignore them and apply the full disclosure rules. But they cannot choose to apply some tailored disclosure provisions and not others. It is up to the lender to decide which approach to adopt.

We are making some small adjustments to the HNW disclosure rules about the trigger points for providing a KFI (see MCOB 5.4.18BR(2)) in light of the amended approach to the HNW execution-only sales process.

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

220. The majority of respondents agreed with the view summarised in this table, subject to their views about the wider regulation of HNW lending, as discussed in responses to Q77 to Q85.
221. Some comments were made on the relevance of particular rules to HNW lending. These included:
- the difficulty of reading across the execution-only rules to HNW lending, due to the non-commoditised nature of HNW mortgages, which would prevent customers from being able to specify the product characteristics required by MCOB 4.8A.14R before arranging a sale on an execution-only basis; and
  - the short-term nature of some HNW mortgages, which might result in the need to apply some of the bridging loan requirements.

### Our response

We have taken this feedback into account when developing the tailored approach to HNW lending. For example, we have adapted the HNW execution-only rules to recognise the nature of HNW mortgages, therefore we are not requiring HNW mortgage customers to specify the product details that would normally be required.

As we discuss in Chapter 4, we are also making an exception from the rules around extending the term of a bridging loan (MCOB 11.6.55R) for secured overdrafts made to HNW mortgage customers.

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

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

222. No further issues of substance were raised in response to these questions.

### **Business lending**

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

223. Respondents' views were polarised. Lenders and trade bodies strongly supported some form of carve-out, but consumer representatives were very concerned about the risks this would pose.

224. Those in favour of a carve-out thought that business borrowers were better able to make financial decisions. They felt the MMR proposals would not be easily transferable to business lending, as they do not recognise the way business banking works, or reflect the differences between regular mortgages and secured business lending. For example, the requirement to assess income does not recognise that, for business lending, payments can be made through the resources of the business, rather than the income of the borrower. When assessing the affordability of a loan made to a business, many factors are taken into account, such as historic trading performance and future expectations, cash flows, business commitments and the drawing requirements of the borrower – rather than the personal income and expenditure of the borrower.

225. Some lenders thought that mortgage regulation can cause unnecessary delays (e.g. while disclosure documents are produced), which they think can be confusing for the customer, while adding no significant benefits – particularly as the speed of execution can also be vital to some business lending.

226. Respondents also felt that the application of the proposed MMR requirements would be disproportionately onerous given the very small proportion of business lending that is regulated. Several lenders felt that the difficulty and costs of developing compliant processes may lead some lenders to withdraw from regulated business lending.
227. In contrast, consumer representatives thought that the MMR requirements would be vital to ensure that small business owners and sole traders are protected. They disagreed that these customers are able to better protect themselves, because it can be difficult for them to separate out their personal and business affairs, therefore affecting their ability to make objective financial decisions.
228. Consumer representatives were also particularly concerned that a carve-out would create a loophole for gaming, by providing an opportunity to bypass affordability checks, and undermine the ban on self-certification mortgages.
229. Various options for carving out business lending were suggested, but there was no clear consensus view. Some supported a complete carve-out of regulation for all business lending. Some supported a partial carve-out (e.g. with some aspects of consumer protection, such as arrears handling, continuing to apply). Others felt a tailored approach could work if, for example, the affordability and advice proposals were more relevant to the needs of business lending.
230. An elective approach was not generally favoured, as respondents felt that our affordability proposals in their current form were completely inappropriate for business lending.

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

231. Most respondents thought that it would be very difficult to draw a line between business borrowers who are able to take the risk and those who are not – with no clear correlation between, for example, the size of a business and its capacity to understand risks.
232. However, several suggestions were made about where to draw the line. These included:
- **Turnover.** Protection might be required where annual turnover was low, for example, below £250,000.
  - **Type of business.** Sole traders might need more protection than other business types.
  - **Loan size.** Smaller loans might need more protection.
  - **Loans made within a business banking relationship.** Loans made through a business banking relationship to a business might need less protection, on the grounds that the business is likely to have a degree of financial sophistication, and the bank will apply an appropriate underwriting process.

- **Purpose of loan.** Loans made solely for a business purpose could be treated in a different way to loans for a mixed use (e.g. a business and personal purpose).

*Q91: How would we prevent this proposal from being exploited as a means of circumventing our affordability proposals?*

233. Common suggestions included that the lender should have clear evidence that the loan is for a business purpose, or that business loan advances should only be paid into a business bank account.
234. Banks who offer business lending believed they already have sufficient safeguards in place to prevent any gaming, as lending is typically done through managed relationships where the lender already knows and understands the businesses they are lending to. They thought this would be difficult to exploit.
235. Consumer representatives reiterated their concern that the risk of gaming is too great. They thought that the only way to protect against exploitation is to insist that affordability checks apply equally to all types of mortgage borrowing, including for business purposes. Therefore, they thought that business loans should not be exempt, or be allowed to opt-out of our affordability requirements

*Q92: Would it be appropriate for all mortgage rules to be foregone or should some, for example the arrears rules, be retained?*

236. Responses to this question were mixed. Around half supported a carve-out for business lending from our mortgage rules, although the majority of these respondents agreed that the MCOB 13 arrears rules should be retained.
237. The remaining respondents felt strongly that MCOB protections should apply to business lending as it is secured on the borrower's main residence and therefore the borrower is equally (if not more) at risk.

### **Our response**

We have given careful consideration to the feedback received. We recognise that some of the MMR proposals, particularly in relation to responsible lending and advice, are not workable for business lending and that business borrowers are generally more financially capable. However, we have not been convinced that business lending should be entirely carved out of mortgage regulation.

We have therefore developed a tailored approach to business lending, which recognises the particular characteristics of business lending where this differs from mainstream residential mortgages.

We set out details of this approach in Chapter 4.

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

238. Many respondents thought the affordability proposals should not be applied to business borrowers. Business loans are underwritten based on an assessment of the business, rather than an individual customer, and therefore our affordability proposals do not work.

#### **Our response**

We have taken this feedback into account when developing the tailored approach to business lending, which recognises that the loan may be repaid through the resources of a business rather than, or as well as, the personal resources of an individual.

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

239. The majority of respondents agreed that business lending staff should be excluded from the requirement to obtain a professional mortgage qualification. They were supportive of including them in the training and competency regime, which would require firms to ensure individuals selling business loans are competent to do so.

#### **Our response**

We are proceeding with our proposed approach to professional standards in business lending.

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

240. Responses to this question generally disagreed with the read-across of proposals to business lending, for the reasons outlined above.

### Our response

We have taken respondents comments into account when developing our tailored approach to business lending.

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

**241.** No other substantive issues were raised.

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

**242.** Some comments were made on the relevance of particular rules to business lending. These included:

- the difficulty of reading across the execution-only rules to business lending, due to the non-commoditised nature of business mortgages, which would prevent customers from being able to specify the product characteristics required by MCOB 4.8A.14R before arranging a sale on an execution-only basis; and
- the rules around extending the term of a bridging loan may apply to some secured business overdrafts caught within the definition of a bridging loan.

### Our response

We have taken this feedback into account when developing the tailored approach to business lending. As with HNW lending, we have adapted the execution-only rules to recognise that it may not be possible for mortgage applicants to specify the product details that would normally be required. We are also making an exception for secured business overdrafts from the rules around extending the term of a bridging loan (see MCOB 11.6.55R).

**Q98:** *Do you have any comments on the draft rules specific to niche mortgage markets in the draft Mortgage Market Review (Conduct of Business) Instrument 2012 at Appendix 1? Do you think the rules reflect the stated policy intention?*

**243.** No other substantive comments were made that have not been picked up in previous questions.

## Cost Benefit Analysis (CBA)

**Q99:** Do you have any comments on our estimates for the impacts of the affordability assessment? Do you have any data and/or analyses that could be informative about these impacts?

**Q100:** Do you have any comments on our estimates for the impacts of the interest rate stress test? Do you have any data and/or analyses that could be informative about these impacts?

**Q101:** Do you have any comments on our estimates for the impacts of the interest-only proposals? Do you have any data and/or analyses that could be informative about these impacts?

**Q102:** Do you have any comments on our estimates of the combined impacts of the responsible lending requirements? Do you have any data and/or analyses that could be informative about these impacts?

**Q103:** Do you have any comments on our estimates for the lending impacts of the responsible lending requirements? Do you have any data and/or analyses that could be informative towards estimating these impacts?

**Q104:** Do you have any views on whether this balance between winners and losers is acceptable, given the importance of the protection obtained by the winners?

- 244.** Responses to these questions were largely overlapping and we have therefore summarised the responses together.
- 245.** Respondents recognised the difficulty of modelling the mortgage market and the inherent uncertainty in the available data and analysis. Most respondents were complimentary about the level and detail of analysis which has gone into the CBA.
- 246.** **Overall impacts** – Respondents mainly criticised the use of a number of key assumptions in modelling the responsible lending and the well-being impacts. Respondents raised concerns about whether the results are reliable given these assumptions. However, despite these concerns, most respondents said that the estimated size of the impacts of the responsible

lending proposals appeared to be reasonable. None of the respondents provided data or additional analysis on the impact of the proposals.

247. Some specific issues were raised regarding measuring the impacts of the affordability assessment, the interest rate stress test, the interest-only proposals and the well-being analysis.
248. **Affordability assessment** – Some respondents commented that the ‘Quality of Underwriting’ methodology was based on the assumption that the proposals correctly target unaffordable lending. They argued that this may not be the case in practice, especially in the short and medium term, when there will be great uncertainty on how the rules will be supervised. A couple of respondents argued that uncertainty about implementation and supervision of the proposals will lead to higher impacts as lenders may be overly cautious in their lending decisions.
249. **Interest rate stress test and interest-only proposals** – A number of respondents questioned our decision to revert back to the Debt-Service-Ratio methodology for the modelling of the interest rate stress test and interest-only proposals. They argued that this adds a further level of approximation to the estimates. One respondent considered that short-term loans will be more impacted by the interest-only proposals.
250. **Well-being analysis** – A number of respondents advocated the need for further explanation of the methodology behind the well-being analysis. One consumer representative questioned our choice of methodology and commissioned two reviews of the methodology. Those reviews provided useful insights and suggestions, but we felt that neither provided a viable alternative that we could have adopted in the circumstances. Apart from this respondent, the majority of consumer representatives were supportive of the results.
251. In CP11/31 we also explained that the Executive and Board of the FSA had accepted the balance of winners and losers from the MMR on the basis of our CBA. Some respondents also asked for further detail behind this judgement.

### Our response

We have been fully transparent in CP11/31 about the need to make a number of key assumptions in estimating the impacts of MMR, including the well-being study. The CBA was very complex and any such estimates are inherently uncertain. The CBA we presented sets out our best estimate of these effects, and of the expected change in consumer welfare which might result. The basis for estimating benefits was that the proposals would successfully target unaffordable lending in about 30% of cases.

We explained the reasons why we used the Debt-Service-Ratio (DSR) methodology for modelling the interest rate stress test and interest-only proposals. Using

the 'Quality of Underwriting' methodology to model the impact of the interest rate stress test and interest-only proposals would have been very complex. We also stressed that DSR is used as a proxy rather than as a precise measure of affordability. We also explained the reasons why a traditional welfare analysis was not carried out and the limitations of the well-being analysis.

Overall, there is no evidence from the responses that the impacts recorded in the CBA for the responsible lending proposals are likely to be materially different to what was estimated.

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## Other CBA responses

252. In relation to the advice proposals, a number of respondents argued that we have underestimated the compliance costs of removing the non-advised sales process. Respondents argued that the requirement to give advice in the vast majority of interactive sales will extend the timing of the sales process and will lead to recruitment costs as well as higher salary levels. Some respondents argued that these proposals could result in the competitive environment being changed. One respondent also stated that removing the fast-track process will be very costly.

### Our response

Since the consultation closed we have had further discussions with a number of respondents. We believe that some of the criticism regarding the costs of the advice proposals is based on an incorrect understanding of the proposals. However, we have updated our compliance cost estimate. The updated estimate is reflected in the CBA summary in Annex 3 of this Policy Statement.

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## Equality impact assessment

253. In CP11/31 we presented our initial assessment of the impact our proposals will have on the various groups with protected characteristics (gender, disability, age, pregnancy and maternity, race, religion and belief, transgender and sexual orientation). This took into account feedback we had received from previous consultations. We asked several further questions (Q105 to Q118 in CP11/31) on the issues identified.
254. Overall, respondents agreed that our proposals do not result in direct discrimination for any of the groups. No new concerns were identified, but there were several issues over indirect discrimination that respondents felt required further consideration.

255. We have now completed our final equality impact assessment, which takes into account all of the comments in response to all of our MMR consultations. This can be found in Annex 5.

## Age

*Q105: Do you have any comments on the age-related issues discussed above?*

*Q106: Are there any other age-related impacts from our proposals not highlighted above? If yes, please provide details.*

256. Consumer groups believe the MMR reforms will benefit older customers by preventing them from taking unaffordable mortgages into retirement, thereby avoiding financial problems following a drop in income in the future.

### Our response

We agree with this assessment. We want to prevent older customers carrying unaffordable debt into retirement.

## *Responsible lending proposals*

257. Concerns were raised over the requirement for lenders to consider future changes in income and expenditure, as this may result in them applying tighter criteria to older customers. Equally, a requirement for lenders to assess the repayment strategy for interest-only mortgages may mean some older customers cannot get a new mortgage or remortgage. This is because lenders may not accept the eventual sale of the property as a repayment strategy. This could push older customers towards more expensive sources of borrowing.
258. In addition, a requirement to verify income could prevent younger customers who do not have an income history from obtaining a mortgage. This is because lenders may set minimum periods on the length of time a customer must have been in their existing employment (e.g. six months for employed applicants, two years for self-employed, etc.).

### Our response

Lenders must consider whether the customer can continue to afford the mortgage following a known change in their income, such as at retirement. Our

aim is to prevent unaffordable lending in retirement, not to prevent all lending into retirement.

Our analysis has established that our proposals affect first-time buyers (FTBs) less than other groups of customers. This is because lenders have always taken a more stringent view when underwriting loans to FTBs as they do not have a repayment history. We do not require any fixed minimum periods of employment under the MMR.

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### *Advice*

259. Some consumer representatives were worried that requiring advice in all equity release sales may force financially capable consumers to go through a lengthy process that they do not want. Equity release customers should not be described as ‘vulnerable’ as it suggests they are less financially capable.

#### **Our response**

We do not regard equity release customers as less capable. In fact our research suggests the opposite. They are vulnerable, however, to the wider and longer term implications of equity release on which they need appropriate advice.

The industry already recognises the importance of advice and almost all equity release sales are advised due to the code of conduct imposed by the Equity Release Council.

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### *Professional standards*

260. There was some concern that a requirement for all intermediaries to obtain a qualification could be difficult for older advisers and for younger people entering the industry.

#### **Our response**

We continue to believe that customers are entitled to expect anyone selling mortgages to be appropriately qualified, regardless of their age.

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### **Disability**

*Q107: Do you have any comments on the disability-related issues discussed above?*

**Q108:** *Are there any other disability-related impacts from our proposals not highlighted above? If yes, please provide details.*

### *Evidence of income*

261. Concern was raised that disabled customers receiving benefits, or in part-time or irregular work, may find it more difficult to provide evidence of sources of income that are acceptable to lenders.

#### **Our response**

In making their affordability assessments, we allow firms to take account of income derived from sources other than employment, which could include benefits, for example. We are not prescriptive about the type of evidence that lenders may accept.

### *Interest-only repayment strategies*

262. Many disabled home-owners have interest-only mortgages where the loan will be repaid following the eventual sale of the property. Concerns were raised in previous consultations that disabled customers may not be able to demonstrate a repayment strategy for their interest-only mortgage that is acceptable to lenders as a result. This is particularly relevant to the HOLD scheme, where lending is typically on an interest-only basis.

#### **Our response**

We have already acknowledged that customers may have a wide variety of repayment strategies. We do not prevent lenders from accepting the eventual sale of the property as the repayment strategy, providing the customer is not relying on a speculative strategy, such as property price increases.

### *Access to non-interactive channels*

263. Visually impaired customers, or those with hearing problems, may find it difficult to access non-interactive channels such as the internet. There was concern that by making execution-only available through non-interactive channels, we may be forcing customers with certain disabilities into taking advice.

**Our response**

Firms have a duty to make reasonable adjustments so that all customers can access their services. These adjustments should make it possible for disabled customers to use the non-interactive channels, such as the internet. We understand that it may be more difficult, but not impossible, for disabled people to use these channels.

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*Transitional arrangements*

264. Concern was raised that disabled customers requiring alterations to their home may not be able to borrow additional funds because of our transitional arrangements.

**Our response**

We considered making an exception for disabled people borrowing funds for essential alterations. However, we are concerned about the practical difficulties in identifying when such an exception would apply. We are also concerned about the potential abuse of such an exception and the detriment to customers if they are unable to afford the additional lending. Our rules do not prevent lenders from lending additional funds to disabled customers, provided the appropriate affordability checks are completed.

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*Professional standards*

265. There was some concern that a requirement for all intermediaries to obtain a qualification could prove difficult for disabled advisers.

**Our response**

As we have said previously, qualification and training providers have a duty under legislation to provide alternative means of obtaining qualifications.

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**Gender**

*Q109: Do you have any comments on the gender-related issue discussed above?*

**Q110:** *Are there any other gender-related impacts from our proposals not highlighted above? If yes, please provide details.*

266. Concern has been raised that our proposals may have a negative impact on women, as they make up more of the temporary workforce. This may cause problems for them in establishing regular income to support a mortgage. Lenders may not accept income from part-time or temporary contracts, or women may find it more difficult to provide evidence of sources of income that are acceptable to lenders.

#### **Our response**

We are not prescriptive about the type of income or evidence that lenders can accept. Our rules do not prevent lenders accepting income from part-time work or temporary contracts.

### **Pregnancy and maternity**

**Q111:** *Do you have any comments on the pregnancy and maternity-related issue discussed above?*

**Q112:** *Are there any other pregnancy and maternity-related impacts from our proposals not highlighted above? If yes, please provide details.*

#### *Evidence of income*

267. There was concern that pregnant customers or those on maternity leave or taking career breaks may find it more difficult to provide evidence of income that is acceptable to lenders.

#### **Our response**

Lenders are subject to equalities and discrimination legislation and should not have processes that discriminate against customers in this way.

#### *Future changes to income*

268. A number of lenders and their trade bodies were concerned that the requirement to take into account future changes to income and expenditure may conflict with lenders' obligations

under equalities legislation, as they would have to ask women about the potential impact of pregnancy and maternity leave on their income.

### Our response

Our requirements do not conflict with lenders' duties under equalities and discrimination legislation. There is no reason why lenders can't ask applicants a high-level question about future changes to their circumstances. If the customer replies they are pregnant, or planning to start a family, or are taking maternity leave, then the lender is not prevented from asking specific questions about how the customer expects their income and expenditure to change, as long as their approach is in line with their approach to other types of customer in situations where future income and expenditure might be changing.

### Faith or belief

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

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

269. There was a concern that, for Islamic Home Purchase Plans, removing the requirement for an Initial Disclosure Document (IDD) could have a negative impact. It might mean that Islamic customers would not receive information on the product's compliance with Sharia Law.

### Our response

Firms can continue to use the IDD or any other method of disclosure to inform customers of important information such as compliance with Sharia Law.

### Other protected characteristics

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

*Q116: Are there any sexual orientation-related impacts from our proposals not highlighted above? If yes, please provide details.*

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

270. Respondents agreed with our assessment that there is no impact on **Race, Sexual Orientation, Gender Reassignment or Marital Status**. No new concerns were identified for these groups.

### **Data**

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

271. Respondents did not come forward with any additional statistics regarding the mortgage needs and habits of the groups with protected characteristics. However, a number offered to help us monitor the ongoing impacts by gathering data.

## Annex 2

# Table of changes from the draft rules to the final rules

General
<p>This table shows the changes we have made from the draft rules (published in CP11/31) to the final rules to clarify points raised in responses to the consultation.</p> <p>This table only shows significant changes to the text and not changes to the numbering, as these are only a consequence of provisions being added or removed.</p>

Glossary	
Handbook reference	Comment
Execution-only sale	The definition has been expanded to include a variation of an existing home finance transaction.
High net worth mortgage customer	The definition has been expanded from 'high net worth customer' in order to distinguish mortgage customers from customers of other services and products.
Interest roll-up mortgage	The words 'or anticipated' have been added so that lifetime mortgages that allow the customer to avoid rolling up the interest by making voluntary payments are not captured.
Payment shortfall	The words 'during the term of' have replaced 'under' to make it clear when the payments would be due.

Business lending and high net worth		
Draft MCOB rule	Final MCOB Rule	Comment
Throughout the MMR instrument	Throughout the MMR instrument	<p>Some references to loans for business purposes in the new rules have been changed to refer to loans <b>solely</b> for business purposes. This change makes it clear that if any part of a mortgage is not for business purposes, the new rules that apply to the sales process and responsible lending for business lending do not apply.</p> <p>References to high net worth customers throughout MCOB have been changed to 'high net worth mortgage customers' in line with the new glossary term.</p> <p>The section headings 'Business loans and loans to high net worth customers' have been changed to 'Business loans and loans to high net worth mortgage customers: tailored provisions' to make it clearer which sections contain the tailored provisions (mainly relating to disclosure).</p>
1.2.3R	Same	The new text 'or an elective business customer' has been deleted to reflect our revised approach to business lending set out in Chapter 4.
1.2.3A R	1.2.3B R	This rule sets out how MCOB applies to joint borrowers or potential borrowers where at least one of them is a high net worth mortgage customer.
1.2.4G	Same	This explains where the tailored provisions for business loans and high net worth mortgage customers can be found in each chapter of MCOB.
N/A	1.2.4A G and 1.2.4B G	These explain the application of tailored and other provisions for high net worth mortgage customers and transactions for business purposes.
N/A	1.2.5G	This explains that the firm has responsibility in determining whether the mortgage is for business purposes.
N/A	1.2.9B G	We have added this guidance to explain that firms have greater flexibility when dealing with professional customers.
1.2.9-A R	1.2.9C R	This has been expanded to allow firms to use evidence already in their possession as evidence that a customer is a high net worth mortgage customer.
N/A	1.2.9D R	We have added this rule to make it clear that firms must obtain a credible business plan from the customer before treating the loan as being solely for a business purpose.
N/A	1.2.9E R	We have added this rule to make it clear that firms must obtain credible evidence from the customer that they meet the definition before treating them as a professional customer.
1.2.9 -B R	1.2.9F R	This sets out the record keeping requirement for the three preceding rules.

Advised sales		
Draft MCOB rule	Final MCOB Rule	Comment
4.2.1G (2)(c)	Same	This has been expanded to include loans solely for business purposes.
N/A	Before 4.4A.2R	The heading 'Range of products' has been added.
N/A	Before 4.4A.8R	The heading 'Basis of remuneration' has been added.
4.7A.1G (2)	Same	This has been redrafted and expanded to include variations of existing regulated mortgage contracts.
4.7A.1G (3)	Same	This has been expanded to refer firms to the guidance in PERG 4.6, which sets out what is meant by regulated advice.
N/A	4.7A.1G (4)	We have added this new provision in relation to contract variations, to clarify that execution-only is permitted for certain variations which do not involve additional borrowing.
4.7A.4G	4.7A.4G (1)	The reference to Principle 9 has been removed as the guidance elaborates on the specific rule to which it refers.
N/A	4.7A.4G (2)	We had added this new provision to make it clear that firms are not precluded from advising a customer to enter into a different mortgage if their initial advice is rejected.
4.7A.5R (3)	Same	This has been redrafted to make the rule clearer.
4.7A.6R (8)	Same	We have replaced 'credit profile' with 'credit history' to reflect that customers may not be aware of their profile held by credit reference agencies and that intermediaries do not generally have access to this information.
4.7A.24R	Same	This has been expanded to clarify that where advice is rejected the customer may enter into a different mortgage on an execution-only basis.

Execution-only sales		
Draft MCOB rule	Final MCOB Rule	Comment
4.8A.1G	Same	This has been expanded to include varying an existing regulated mortgage contract and to refer firms to the guidance in PERG 4.6, which sets out what is meant by regulated advice.
4.8A.2G	Same	This has been expanded to include variations of existing regulated mortgage contracts and where the loan is solely for business purposes.
4.8A.3G	Same	This has been expanded to provide guidance on internet sales.
4.8A.6G	Same	This has been expanded and redrafted to make the guidance clearer.
N/A	4.8A.9R	This new provision makes it clear that 4.8A.7R does not apply to high net worth mortgage customers, and 4.8A.7R(3) does not apply to professional customers and loans solely for business purposes.
N/A	4.8A.10R	This new provision sets out when execution-only is permitted for contract variations.
N/A	4.8A.11G	This is new guidance to give examples of contract variations and rate changes and to remind firms when our rules on advice will apply.

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N/A	4.8A.12R	This makes it clear that 4.8A.7R does not apply when advice has been rejected.
4.8A.9G	4.8A.13G	This makes it clear when and how the exceptions in 4.8A.7R apply.
4.8A.10R	4.8A.14R	This has been changed to cater for the new provisions at 4.8A.10R and 4.8A.7R.
N/A	4.8A.15R	This specifies which of the execution-only requirements apply for business lending and high net worth mortgage customers.
4.8A.11R	4.8A.16G	Part (1) has been integrated into 4.8A.14R. Part (2) has been changed to guidance.
4.8A.14R	4.8A.17R	This has been expanded to make it clear firms must have a policy that includes the steps they would take if they exceed the expected levels of execution-only sales.
4.8A.15R	4.8A.18R	This has been expanded to confirm that the record keeping period applies also from the date of a variation.
N/A	4.8A.19R	This new provision makes it clear that the restrictions in MCOB 4.8A do not apply in forbearance cases.

**Disclosure**

Draft MCOB rule	Final MCOB Rule	Comment
5.4.1R, 5.4.2R and 5.4.3R	N/A	The proposed changes are not required and have been removed from the final rules.
5.4.18B R and 5.5.1R (2)	Same	These rules have been expanded to provide for the contract variation execution-only sales route and the tailored execution-only sales route for high net worth mortgage customers and loans that are solely for a business purpose.

**Home Purchase Plans**

Draft MCOB rule	Final MCOB Rule	Comment
4.10.5C G	Same	The reference to Principle 9 has been removed as the guidance elaborates on the specific rule to which it refers.
4.10.9D R (2)	N/A	Removed to bring the execution-only requirements for home purchase plans in line with 4.8A.14.
5.8.1R (2) (e) and 5.8.13R	Same	We have changed the references from 4.8A.10R to MCOB 4.10.9DR in these provisions to make the execution-only requirements clearer for Home Purchase Plans.

**Equity Release**

Draft MCOB rule	Final MCOB Rule	Comment
8.2.2G (2) (d)	Same	This has been expanded to allow for the exceptions set out in 8.6A.5R.
8.3.1R	Same	We have added (c) to make it clear the affordability rules in MCOB 4.6 only apply to a lifetime mortgage if payments are being made by the borrower.
8.3.4R	Same	This makes clear the execution-only rules in MCOB 4.8A are modified by MCOB 8.6A for equity release sales.

Equity Release		
8.6A.4R	Same	This has been expanded to clarify the conditions for execution-only sales, including the exceptions for rate switches and variations. This is a read across of changes to 4.8A.
N/A	8.6A.5R	This makes it clear that 8.6A.4R does not apply to rate switches and contract variations.
N/A	8.6A.6G	This new guidance gives examples of rate switches and variations that benefit from the exception in 8.6A.5R. The guidance also reminds firms that steering the customer towards a product such as to constitute advice would not benefit from the exception.
8.6A.5R	8.6A.7R (1)	This has been expanded to allow for the exception in 8.6A.5R.
8.6A.7R	8.6A.9R	The record keeping requirements have been expanded to include information about rejected advice that precedes an execution-only sale.
N/A	8.6A.10R	This new provision makes it clear that the restrictions in MCOB 8.6A do not apply in forbearance cases.
N/A	9.3.1R (2)	This has been changed to make it clear how the modification table in 9.3.2R applies to equity release transactions.
9.3.2R	Same	The table has been expanded to make it clearer how the changes to the disclosure rules in MCOB 4 and 5 should be read for equity release transactions.

Responsible lending, and responsible financing of home purchase plans		
Draft MCOB rule	Final MCOB Rule	Comment
N/A	Throughout MCOB 11	References to further advances have been removed and replaced with 'variation' or 'variations'. Further advances are a type of variation so it is clearer and simpler to refer to all variations. Our approach to variations is set out in Chapter 3.
11.4.4R	N/A	This has been deleted in line with the above.
11.6.1G	Same	This has been expanded to explain certain rules are modified for high net worth mortgage customers and loans that are solely for a business purpose.
11.6.2R	Same	This has been expanded so that the assessment of affordability rule applies to variations as well as new mortgages and guarantors as well as borrowers.
N/A	11.6.3R	This new rule reflects that the affordability assessment rule does not apply if no additional borrowing is being taken on beyond the current amount outstanding, and there is no change to the terms of the mortgage that would impact on affordability.  The rule also makes it clear that the affordability requirements in 11.6.2R do not apply in forbearance cases.
N/A	11.6.4E	Linked to the above, this provides that not treating certain changes to the mortgage as not impacting on affordability may be relied on as tending to show a breach of 11.6.2R.
11.6.6R	11.6.8R	This has been expanded to reflect that firms must obtain evidence of income with all variations, not just further advances. We have also added a requirement that evidence of income must be subject to appropriate anti-fraud controls.

Responsible lending, and responsible financing of home purchase plans		
11.6.7G	11.6.9G	Text has been added to make it clear that income can be derived from sources other than employment, such as pensions or investments.
11.6.8R	11.6.10R	(3) has been reworded to clarify what the basic quality-of-living costs are.
11.6.9G	11.6.11G	This has been expanded to make clear the cost of a repayment strategy does not need to be included as committed expenditure if affordability has been assessed on a capital and interest basis.
11.6.12R	11.6.14R	This has been amended to require firms to take into account future changes that there will be or <i>are likely to be</i> (rather than that there <i>may be</i> ).
11.6.13G	11.6.15G	(2) has been expanded to reflect that post-retirement changes to income should be taken into account either where the term extends beyond the customer's expected retirement date, or beyond state pension age if their expected retirement date is not known.
11.6.14R	11.6.16R	This has been changed to allow firms to use either approach (set out in CP11/31) to debt consolidation mortgages for credit-impaired customers.
11.6.16R	11.6.18R	The words 'beginning of' have been replaced with 'expected start of' to make it reflect that the lender will not know the exact start date of the mortgage.
11.6.18R	11.6.20R	We have made an amendment to allow a firm's responsible lending policy to be contained in more than one document. We have also replaced 'board' with 'governing body' so that an appropriate body can approve the firm's lending policy instead of the main board of the firm.
11.6.20R and 11.6.21G	11.6.22R and 11.6.23G	These provisions have been expanded to make it clearer how firms should monitor their lending against their policy.
11.6.22R	11.6.24R	This has been expanded to reflect that the review of a firm's lending policy must be by their internal audit function if they have one, or their compliance function if they don't (or in either case an outsourced equivalent).
N/A	11.6.25R to 11.6.32R	These set out the alternative responsible lending requirements for loans that are solely for a business purpose.  Our approach to business lending is set out in Chapter 4.
N/A	11.6.33R to 11.6.39R	These set out the alternative responsible lending requirements for loans to high net worth mortgage customers.  Our approach to high net worth mortgage customers is set out in Chapter 4.
11.6.28G	11.6.45G	This has been expanded to include regular deposits into a savings product as an example of a repayment strategy that may be acceptable.

<b>Responsible lending, and responsible financing of home purchase plans</b>		
11.6.29E (3)	11.6.46E (3)	This has been expanded to clarify when the sale of the customer's main residence may be acceptable as a repayment strategy.
11.6.30G	11.6.47G	'at the time of consideration' has been added to make the guidance clearer.
11.6.31R	11.6.48R	This has been expanded to reflect that alternative provisions for high net worth mortgage customers and loans solely for a business purpose may apply when assessing the affordability of an interest-only mortgage.
11.6.32R	11.6.49R	A review of the repayment strategy during the term is not required for bridging loans.
11.6.38R	11.6.55R	This has been expanded to reflect that this rule does not apply when extending the term of a bridging loan if it is a secured overdraft for a high net worth mortgage customer or is used solely for a business purpose.
N/A	11.6.56G	Linked to the above, this guidance has been added to remind firms of their responsibilities towards the customer.
11.6.39R	11.6.57R	This has been expanded to clarify none of the affordability provisions applicable to MCOB 11.6.2R apply to interest roll-up mortgages.
11.6.41G	11.6.59G	The words 'or anticipated' have been added to reflect the change in the glossary definition of an interest roll-up mortgage.
11.6.42R (2)	11.6.60R (2)	This has been expanded to allow for the alternative provisions for high net worth mortgage customers and loans solely for a business purpose.
11.6.42R (2)	11.6.60R (3)	This has been expanded to reflect that firms must keep details of their attempts made to contact the customer.
11.6.42R (5)	11.6.60R (5)	Part (b) has been deleted to reflect the revised record keeping requirements.
11.6.42R (6)	11.6.60R (6)	This has been changed to reflect in the record keeping requirements the changed transitional arrangements rules.
11.6.42R (7)	11.6.60R (7)	This has been changed to reflect that firms should keep a record of their lending policy for as long as mortgages underwritten under that policy remain outstanding.
N/A	11.8.1E	This is a new provision to ensure firms treat their existing customers fairly if they cannot remortgage.

<b>Transitional arrangements</b>		
<b>Draft MCOB rule</b>	<b>Final MCOB Rule</b>	<b>Comment</b>
11.7.1R to 11.7.7R	11.7.1R to 11.7.5G	<p>We have updated the section on transitional arrangements to reflect other changes shown above and to confirm our final position.</p> <p>Our approach to transitional arrangements is set out in Chapter 3.</p>

<b>Arrears, payment shortfalls and repossessions</b>		
<b>Draft MCOB rule</b>	<b>Final MCOB Rule</b>	<b>Comment</b>
13.3.4A R	Same	This has been expanded to clarify that firms must not automatically add a payment shortfall to the loan if the impact would be material.
N/A	13.3.4AA R	Linked to the above, this new rule explains the circumstances where the impact would be material.
13.3.9R	Same	This has been expanded to clarify that any discussions about arrears or payment shortfalls should be recorded.

<b>Other parts of the handbook</b>		
<b>Draft MCOB rule</b>	<b>Final Rule</b>	<b>Comment</b>
MCOB Schedule 1  Sch 1.3G	Same	This has been expanded to make it clear what the firm's records should contain, when the records should be made and for how long they should be kept, including the extended record keeping requirements that apply to MCOB 11.  This has also been changed to reflect other changes in MCOB shown in this table.
N/A	SUP 16 Annex 18BG	This has been modified to reflect the fact that firms are no longer required to describe their service using 'labels'. When mortgage firms are asked whether they offer advice for different categories of product ranges, they should simply answer 'No' for each category.

<b>Non-bank mortgage lenders capital requirement</b>		
<b>Draft MIPRU rule</b>	<b>Final MIPRU Rule</b>	<b>Comment</b>
4.2.23R(2)(b)(ii)	4.2.23R(2)(b)(ii)	Amended to clarify that the 1% charge is not applied to assets subject to a risk-based charge under the requirements of 4.2A.4R
4.2A.1R	4.2A.1R	Deleted reference in the rule to credit risk capital requirement as it is not necessary.
4.2A5R	4.2A5R and 4.2A.5'A G	4.2A.5R expanded to clarify the new requirement only applies to the increase and not the whole loan. Additional guidance introduced in 4.2A.5AG to confirm that the new requirement does not apply to loans acquired by the firm after the implementation date if they had been made before that date; and to arrangements made as a result of forbearance.
4.2A.8R	4.2A.8R	The references to €1 million in BIPRU 3.2.10R and 3.2.19G are replaced by £1 million as applying Euro limits to a business with predominately sterling assets and liabilities is not proportionate.
4.2D.9(3)	4.2D.9(3)	Requirement introduced for the written record to be made as soon as practicable after the test has been performed.
4.4.1R(3) and (4)	N/A	Proposed 4.4.1R (3) and (4) removed as not necessary given the requirement is set out in 4.4.8R.
N/A	Schedule 1	Record keeping requirements in respect of the stress tests required under 4.2D.9R(3) are set out in this Schedule.

## Annex 3

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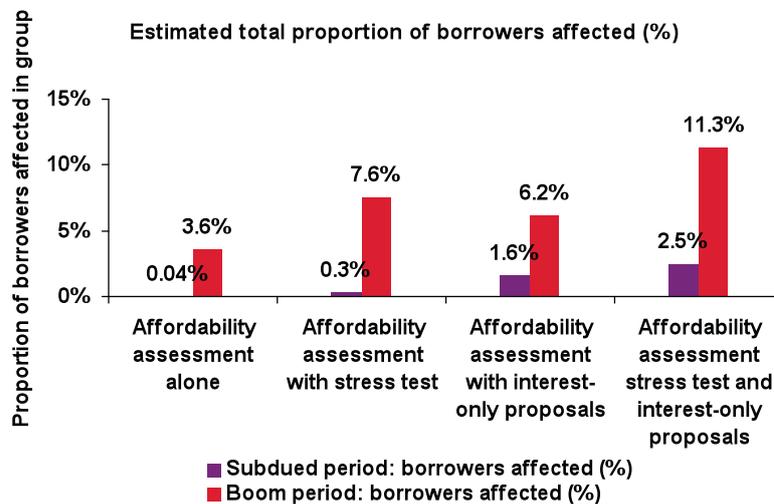
# Cost benefit analysis

1. The respondents to the Cost Benefit Analysis (CBA) in CP11/31 felt that the estimated size of the impacts of the responsible lending proposals appeared reasonable. The changes made to the transitional arrangements described in Chapter 3 do not materially change the results.
2. Regarding the advice proposals, a number of respondents felt that we had underestimated the compliance costs of removing the non-advised sales process. The policy approach has been amended in light of the feedback, as described in Chapter 2. We have updated our compliance costs estimate as set out below to reflect our changed approach and the feedback received.
3. The approach to high net worth (HNW) lending also does not materially affect the CBA. We noted in the CBA of CP11/31 that the impacts of the MMR on mortgage finance for business development may be negative, but that we lacked the data to quantify these impacts. The proposed approach to business lending is likely to mitigate potential negative impacts. There is, however, still no data available to quantify the impacts on mortgage finance for business development.
4. We therefore believe that our CBA as set out in CP11/31 remains valid, subject to the revised compliance cost estimate for the advice proposals. The high-level CBA conclusions are restated below together with a regional breakdown of the impacts, as requested in feedback.

### **The overall impact on borrowers**

5. The affordability assessment, the interest rate stress test and the interest-only proposals together are estimated to affect 2.5% of borrowers in subdued market conditions and 11.3% in boom market conditions. Figure 1 shows the combined impact of the affordability assessment, interest-rate stress and the interest-only proposals, as well as of two other combinations and of the affordability assessment by itself.

**Figure 1 – Responsible lending proposals – estimated total proportion of borrowers affected<sup>1</sup>**



6. Our analysis of the affordability assessment alone shows that its impact is minimal in the subdued period. In both the subdued and the boom period, the impact is less on first-time buyers (FTBs) than on remortgagors. Throughout the sample period, the greatest impact is on self-certified borrowers and the credit-impaired, with credit-impaired by far the most affected. Because many self-employed borrowers were self-certified, there is also a significant impact on this group from the affordability assessment in the boom period.

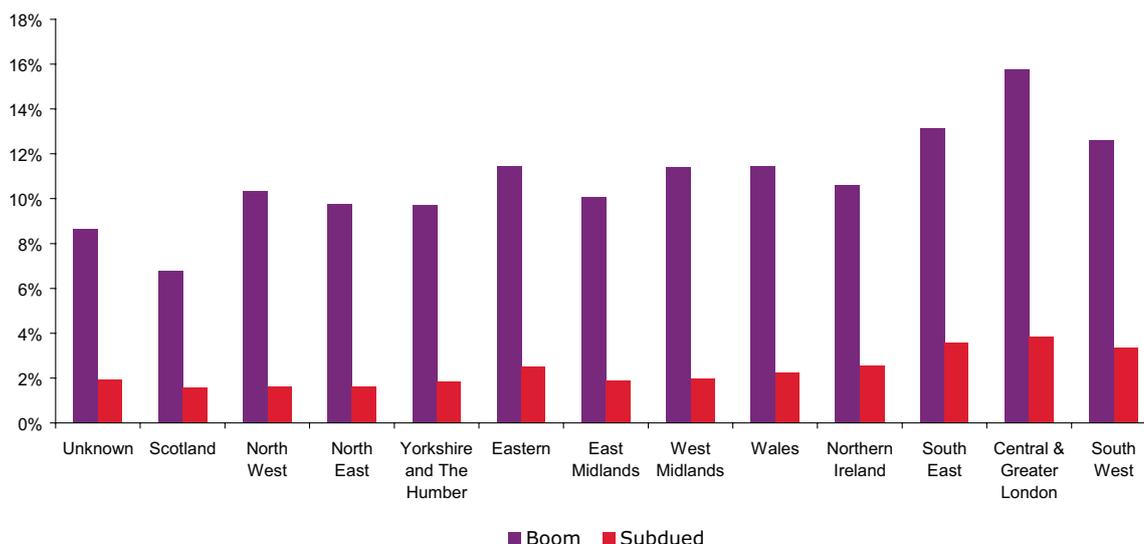
## Regional impacts on borrowers

7. Figure 2 shows the combined impact of the responsible lending proposals by region. For all borrower categories, except self-certified borrowers and credit-impaired borrowers, Greater and Central London, the South-East and the South-West are the regions that are most affected by the responsible lending proposals both in the boom and subdued period.
8. For self-certified borrowers, the North-East is most affected by the responsible lending package over the boom period and the South-East over the subdued period. For credit-

<sup>1</sup> The incremental impact of the interest-rate stress and interest-only proposals together (2.5% in subdued, 7.7% in boom) is greater than the sum of the incremental impacts of the interest-rate stress and the interest-only proposals (1.8% in subdued, 6.6% in boom). This is due to the interest-only and interest-rate stress tests proposals acting together to affect borrowers who would not be affected by either of the two proposals alone. For example, an interest-only borrower may pass an affordability assessment with the interest-rate stress, and may also pass an affordability assessment with the interest-only proposals, but not pass an affordability assessment where both the interest-rate stress and the interest-only proposals are applied. Modelling the combined impact of the three proposals together captures further borrowers.

impaired borrowers, Wales is most affected by the responsible lending package over the boom period and Northern Ireland over the subdued period.<sup>2</sup>

**Figure 2 – Responsible lending proposals – proportion of borrowers affected in different regions**



## Compliance costs from the MMR

9. In CP11/31 we explained that we expect the total ongoing compliance costs of the MMR proposals to range between £47m and £170m a year and total one-off costs to be between £40m and £65m.
10. In light of the consultation feedback, we have updated the compliance cost estimate for the advice proposals. On the basis of research that Oxera conducted for us and the Council of Mortgage Lenders, in CP11/31, we expected one-off compliance costs of this proposal to be around £0.8m and ongoing compliance costs to be around £1m. However, we have revised our estimate to take into account the fact that some lenders have a much larger percentage of non-advised sales at the moment and may need to recruit additional staff. We now expect one-off compliance costs to be around £2.8m and ongoing compliance costs to be around £3m.
11. Therefore we now expect the total ongoing compliance costs of the MMR proposals to range between £49m and £172m a year and total one-off costs to be between £42m and £67m.

2 The regional impact of the individual requirements is slightly different to the overall impact. We set out the differences below:

- The affordability assessment alone impacts Northern Ireland, Wales and the North-East more than the other regions over both periods in the sample.
- When the interest only rule is added to the affordability assessment Wales and Northern Ireland remain the most impacted regions while Central and Greater London replaces the North-East over the boom period. In the subdued period the most impacted regions are Central and Greater London and the South.
- When the interest rate stress test rule is added to the affordability assessment the impact shifts to Central and Greater London, Wales and West Midlands over the boom period. In the subdued period, Central and Greater London remains highly impacted followed by the South-East and the South-West.



## Annex 4

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# List of non-confidential respondents to CP11/31

Arbuthnot Latham & Co. Limited  
Association of Accounting Technicians  
Association of Bridging Professionals  
Association of Finance Brokers  
Association of Mortgage Intermediaries  
Association of Short Term Lenders  
Aviva  
Baigrie Davies  
Bank of Ireland  
Bath Investment & Building Society  
Brian Bollen  
Bridgewater Equity Release Limited  
British Bankers Association  
Building Societies Association  
C Hoare & Co  
Chartered Institute of Housing  
Chartered Institute of Taxation  
Citizens Advice  
Clive Jones  
Co-operative Banking Group

Council of Mortgage Lenders  
Coventry Building Society  
Cumberland Building Society  
Daniel Burn  
Darlington Building Society  
David Turner  
Defaqto Limited  
Duncan Lawrie Limited  
EA Consulting Group  
EFG Private Bank Limited  
Ecology Building Society  
Enness Private Clients  
Evan Owen  
Experian  
Finance & Leasing Association  
Financial Services Consumer Panel  
Frank Eve Consulting Limited  
Furness Building Society  
GE Money Home Lending  
Gentoo Genie Limited  
Genworth Financial  
Graham Radband  
Home Saver Mortgage Lifeline  
IFS School of Finance  
Ian Watters  
Institute of Certified Practising Accountants  
Institute of Chartered Accountants in England and Wales  
Intermediary Mortgage Lenders Association

Ipswich Building Society  
Jackson Cohen Associates Limited  
Jeremy Foster  
Karel Herman  
Key Retirement Solutions Limited  
Knight Frank Finance LLP  
Leeds Building Society  
Lloyds Banking Group  
London & Country Mortgages  
Lonsdale Mortgages Limited  
Loughborough Building Society  
Mansfield Building Society  
Marsden Building Society  
Metcalf Moat IFA Limited  
Money Advice Trust  
National Association of Commercial Finance Brokers  
National Counties Building Society  
National Housing Federation  
Newbury Building Society  
Nottingham Building Society  
Openwork Limited  
Paragon Group of Companies  
Penrith Building Society  
Permjit Singh  
Prudential  
Quantum Alpha Limited  
rightmortgageadvice.co.uk  
Royal Bank of Scotland Group

RS Mortgage Consultancy

SA Compliance

Santander UK plc

Scottish Building Society

Sesame Bankhall

Shelter

SHIP

Skipton Building Society (including Homeloan Management Limited)

SPF Private Clients

St James's Place Wealth Management

Stephen Holroyd

Stonehaven

Teachers Building Society

Tenet Group Limited

The Association of Professional Compliance Consultants

The Association of Taxation Technicians

The Chartered Insurance Institute

The Consumer Council for Northern Ireland

The Mortgage & Insurance Shop

Thornhill Solutions Limited

Towergate Financial/John Charcol

Trisha Justin

Virgin Money

West Bromwich Building Society

Which?

Yes Financial Services Limited

Yorkshire Building Society

## Annex 5

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# Equality Impact Assessment (EIA)

### 1. What are the main and secondary aims, purposes and outcomes of this policy/function?

The mortgage market has worked well for most consumers. However, the lead up to the financial crisis (2005 to 2007) saw poor lending practices, which led to a significant tail of consumers facing the distress of arrears and repossessions. The Mortgage Market Review (MMR) has two broad aims:

- to have a mortgage market that is sustainable for all participants; and
- to have a flexible market that works better for consumers.

The MMR can be broken down into the following sets of proposals, which are designed to meet these aims, mainly through changes to our conduct of business requirements:

- responsible lending;
- distribution and disclosure;
- arrears management; and
- niche markets.

The outcome, in broad terms, will be to ensure the continued provision of mortgage credit for the great majority of consumers who can afford it, while preventing the re-emergence of the tail of poor lending practices, which led to consumer detriment.

### 2. Is this policy/function related to other policies or areas of work?

#### **Non-deposit taking lenders**

The MMR proposes the introduction of a new prudential regime for non-deposit taking mortgage lenders, which is based on the relevant parts of BIPRU. Respondents to CP11/31

did not raise any equality or diversity concerns about these prudential requirements. An initial assessment was completed prior to consultation and as no new issues were raised we have concluded there are no equality or diversity implications.

### 3. **What are the main activities, stages or steps of this policy/function?**

Below is a high-level summary of all the MMR policy proposals.

#### **Arrears management practices**

- Firms must not apply a monthly arrears charge where an agreement is already in place to repay the arrears.
- Payments by customers in financial difficulties must first be allocated to clearing the missed monthly payments, rather than to arrears charges, which can be repaid later.
- Firms must consider all options for borrowers. Repossessions should always be the last resort.
- All telephone calls regarding arrears handling must be recorded and kept for three years.

Rules bringing the above into effect came into force on 25 June 2010. Rules for the remaining proposals below are not yet in force.

#### **Approved Persons**

All mortgage advisers and those who arrange mortgage sales will be individually held accountable and required to demonstrate they are 'fit and proper'.

#### **Responsible lending**

- **Affordability assessment.** Lenders must verify income and demonstrate the mortgage is affordable for the borrower, taking into account income and expenditure. This includes any known future changes to income and expenditure.
- **Interest rate stress test.** Lenders must take into account market expectations of possible future interest rate increases.
- **Interest-only mortgages.**
  - Lenders must assess affordability on a capital and interest repayment basis unless there is a clear repayment strategy in place to repay an interest-only mortgage. If affordability is assessed on an interest-only basis, the lender must take into account the cost of the repayment strategy.

- Lenders must obtain evidence of the repayment strategy.
- Lenders must contact borrowers at least once during the mortgage term to check on the status of the repayment strategy.
- **Transitional arrangements.** Lenders will be allowed to waive certain affordability rules for existing mortgage holders where it is responsible and appropriate to do this.
- Lenders must have in place a responsible lending policy, **which has been approved by their governing body**, which sets out their approach to all of the above.

### **Distribution and disclosure**

**Advice.** All vulnerable consumer groups (those purchasing equity release, right-to-buy, sale and rent back and those consolidating debt) must get advice. All other borrowers must get advice if the sale involves interaction between the lender and consumer, except for high net worth (HNW), professional and business borrowers who can elect for an execution-only service.

**Execution-only.** Consumers can reject advice (except in sale and rent back sales) and purchase on an execution-only basis. Non-interactive sales (for example via the internet) may be execution-only. Consumers must know precise details of the product and the loan they require in order to proceed. Execution-only can also be used for post-sale contract variations (for example if porting to a new property) providing no new money is advanced.

**Sales standards.** Firms have additional responsibilities to borrowers regarding further advances and the rolling-up of fees.

**Professional standards.** All mortgage intermediaries must hold a relevant mortgage qualification.

**Service disclosure.** The Initial Disclosure Document (IDD) is no longer required. Instead firms must explain whether there are any limitations in the product range they provide and how they will be remunerated.

**Product disclosure.** The Key Facts Illustration (KFI) does not need to be produced until the product has been recommended/chosen, or the consumer requests it.

### **Arrears management**

**Arrears charges.** Lenders must not attempt to collect more than two direct debits in a month.

**Concessionary rates.** Lenders must not remove borrowers from concessionary interest rates if they have difficulties meeting their mortgage payments.

## Niche markets

The proposals summarised above will be read across to the niche markets where appropriate, with some limited tailoring to reflect the particular nature of those markets.

### 4. **Who is primarily impacted by your policy/function? Are there any secondary people impacted by it? Any other relevant stakeholders?**

- All home finance providers and administrators.
- All home finance intermediaries.
- All consumers buying home finance products.

### 5. **What evidence (e.g. data, research or consultation) is available to analyse the impact of this policy/function?**

MMR consultations

- DP09/3
- FS10/1
- CP10/2
- PS10/9
- CP10/16
- CP10/28
- CP11/31 (which includes feedback on responses to the previous two consultations as well as new questions)
- This Policy Statement, which includes feedback on responses to the EIA questions in CP11/31

Data

- MMR Data Pack published with DP09/03
- Updated MMR Data Pack published with CP11/31
- Updated MMR Data Pack published with this Policy Statement

## 6. How will this policy/function impact each group?

Protected characteristics	Positive impact	Negative impact	Reason (list findings from data listed in question 8)
	Y = We anticipate our proposals have an impact N = We anticipate our proposals have no impact		
Gender	N	N	<p>Concern has been raised that our proposals may have a negative impact on women, as they make up more of the temporary workforce. This may cause problems for them in establishing regular income to support a mortgage. Lenders may not accept income from part-time or temporary contracts, or women may find it more difficult to provide evidence of sources of income that are acceptable to lenders.</p> <p><b>Our response</b> <i>We are not prescriptive about the type of income or evidence that lenders can accept. Our rules do not prevent lenders accepting income from part-time work or temporary contracts.</i></p>
Race	N	N	No concerns were identified.
Disability	N	N	<p>The following concerns have been raised.</p> <p><b>1. Evidence of income</b> Disabled consumers receiving benefits, or in part-time or irregular work, may find it more difficult to provide evidence of sources of income that are acceptable to lenders.</p> <p><b>Our response</b> <i>In making their affordability assessments, we allow firms to take account of income derived from sources other than employment, which could include benefits, for example. We are not prescriptive about the type of evidence that lenders may accept.</i></p> <p><b>2. Interest-only repayment strategies</b> Disabled borrowers may not be able to demonstrate a repayment strategy for their interest-only mortgage that is acceptable to lenders, if they are relying on the eventual sale of the property (e.g. on death). This is particularly relevant to the home ownership for people with Long-term Disabilities (HOLD) scheme, where lending is typically on this basis.</p>

			<p><b>Our response</b></p> <p><i>We do not prevent lenders accepting the eventual sale of a property as a repayment strategy, provided the consumer is not relying on a speculative strategy for their plan to work, such as property price increases.</i></p> <p><b>3. Access to non-interactive channels</b></p> <p>Some disabled consumers such as the visually impaired may find it difficult to access non-interactive channels such as the internet. There was a concern that by making execution-only sales only available through non-interactive channels, we may be forcing consumers with certain disabilities into taking advice.</p> <p><b>Our response</b></p> <p><i>Lenders have a duty to make reasonable adjustments so that all consumers can access their services. This applies to all products not just mortgages and includes non-interactive channels such as the internet. We understand that it may be more difficult, but not impossible, for disabled people to use these channels.</i></p> <p><b>4. Transitional arrangements</b></p> <p>Disabled consumers requiring alterations to their home may not be able to borrow additional funds because of our transitional arrangements.</p> <p><b>Our response</b></p> <p><i>We considered making an exception for disabled people borrowing funds for essential alterations. However, we are concerned about the practical difficulties in identifying when such an exception would apply. We are also concerned about the potential abuse of such an exception and the detriment to consumers if they are unable to afford the additional lending. Our rules do not prevent lenders from lending additional funds to disabled borrowers, provided the appropriate affordability checks are completed.</i></p> <p><b>5. Professional standards</b></p> <p>A requirement for all intermediaries to obtain a qualification could prove difficult for disabled advisers.</p> <p><b>Our response</b></p> <p><i>Qualification and training providers have a duty under legislation to provide alternative means of obtaining qualifications.</i></p>
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Age	Y	N	<p><b>Positive impacts</b></p> <p>Consumer groups believe the MMR reforms will benefit older borrowers by preventing them from taking unaffordable mortgages into retirement, thereby avoiding financial problems following a drop in income in the future.</p> <p><b>Our response</b></p> <p><i>We agree with this assessment. We want to prevent older consumers carrying unaffordable debt into retirement.</i></p> <p><b>Negative impacts</b></p> <p>The following concerns have been raised:</p> <p><b>1. Responsible lending proposals</b></p> <p>The requirement for lenders to consider future changes in income and expenditure may result in them applying tighter criteria to older borrowers. Equally, a requirement for lenders to assess the repayment strategy for interest-only mortgages may mean some older borrowers cannot obtain a new mortgage or remortgage. This is because lenders may not accept the eventual sale of the property as a repayment strategy. This could push older consumers towards more expensive sources of borrowing.</p> <p>In addition, a requirement to verify income could prevent younger borrowers who do not have an income history from obtaining a mortgage. This is because lenders may set minimum periods on the length of time a consumer must have been in their existing employment, (e.g. six months for employed applicants, two years for self-employed, etc.)</p> <p><b>Our response</b></p> <p><i>Lenders must consider whether the borrower can continue to afford the mortgage following a known change in their income, such as at retirement. Our aim is to prevent unaffordable lending in retirement, not to prevent all lending into retirement.</i></p> <p><i>Our analysis has established that our proposals impact less on first-time buyers (FTBs) than on other groups of consumers. This is because lenders have always taken a more stringent view when underwriting loans to FTBs as they do not have a repayment history. We do not require any fixed minimum periods of employment under the MMR. Lending policy is a commercial matter for firms.</i></p>
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			<p><b>2. Advice</b></p> <p>Requiring advice in all equity release sales may force financially capable consumers to go through a lengthy process that they do not want. Equity release consumers should not be described as 'vulnerable' as it suggests they are less financially capable.</p> <p><b>Our response</b></p> <p><i>We do not regard equity release consumers as less capable. In fact our research suggests the opposite. They are vulnerable, however, to the wider and longer term implications of equity release on which they need appropriate advice.</i></p> <p><i>The industry already recognises the importance of advice and almost all equity release sales are advised due to the code of conduct imposed by the Equity Release Council (formerly SHIP), the trade body of equity release firms.</i></p> <p><b>3. Professional standards</b></p> <p>A requirement for all intermediaries to obtain a qualification could prove difficult for older advisers and for younger people entering the industry.</p> <p><b>Our response</b></p> <p><i>Consumers are entitled to expect anyone selling mortgages to be appropriately qualified, regardless of their age.</i></p>
<b>Sexual orientation</b>	<b>N</b>	<b>N</b>	No concerns were identified.
<b>Faith or belief</b>	<b>N</b>	<b>N</b>	<p>There was a concern that for Islamic Home Purchase Plans removing the requirement for an IDD could have a negative impact. It would mean that Islamic consumers would not receive information on the product's compliance with Sharia Law.</p> <p><b>Our response</b></p> <p><i>Our rules do not prevent firms from using the IDD or any other method of disclosure to inform customers of important information such as compliance with Sharia Law.</i></p>
<b>Gender reassignment</b>	<b>N</b>	<b>N</b>	No concerns were identified.
<b>Marital status</b>	<b>N</b>	<b>N</b>	No concerns were identified.

Pregnancy, maternity and carers	N	N	<p>There were two concerns raised.</p> <p><b>1. Evidence of income</b></p> <p>Pregnant customers or those on maternity leave or taking career breaks may find it more difficult to provide evidence of income that is acceptable to lenders.</p> <p><b>Our response</b></p> <p><i>Lenders are subject to equalities and discrimination legislation and should not have processes that discriminate against customers in this way.</i></p> <p><b>2. Future changes to income</b></p> <p>The requirement to take into account future changes to income and expenditure may conflict with lenders' obligations under equalities legislation, as they would have to ask women about the potential impact of pregnancy and maternity leave on their income.</p> <p><b>Our response</b></p> <p>Our requirements do not conflict with lenders' duties under equalities and discrimination legislation. We have explained in the EIA Annex of the Policy Statement how firms should approach questioning mortgage borrowers about future changes to income in a way that is not discriminatory.</p>
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## 7. Action plan

The following actions apply to all impacts identified in the table above.

1. The MMR implementation team will review firms lending policies as the new rules come into force. Their review will include how lenders implement our rules regarding:
  - evidence of income;
  - known future changes to income; and
  - interest-only repayment strategies.
2. The impacts will be reviewed as part of a post-implementation review, which we will carry out 24 to 60 months after implementation.
3. As we reported in CP11/31, reporting by mortgage firms is being reviewed. Collecting data to help us monitor equalities impacts will be considered in the review, so that such data does not need to be collected manually.

## 8. What steps were considered to regularly monitor the effects of this policy/function on people or the changes proposed and which action will be taken if any negative impacts arise with its implementation?

We will monitor the ongoing impact of our proposals on the protected groups through:

- our Product Sales Data (PSD), which can provide some limited data (for example on age);
- complaints data from the Financial Ombudsman Service (FOS);
- reviews of firms' lending policies by Supervision;
- continued contact with external stakeholders such as the Government Equalities Office (GEO);
- continued contact with industry stakeholders such as the Council of Mortgage Lenders (CML) and Building Societies Association (BSA); and
- a post-implementation review.

Actions in the event of any negative impacts:

- Supervision will assess the impact;
- we will communicate with stakeholders such as FOS, GEO, CML and BSA; and
- we will communicate with firms and consumers to clarify our rules where required.

## 9. Summary agreed with policy/function owner to be given to decision makers

Responses confirm that the changes to our rules do not result in direct discrimination against any of the protected groups. There is clearly some concern that mortgage firms could interpret our rules in such a way that certain protected groups find it more difficult to obtain mortgages.

To protect consumers as much as possible against this we will be checking, through our supervision of the mortgage market, that firms do not introduce lending policies that are discriminatory.

We have established working relationships with a number of stakeholders and will stay in contact with them to monitor the impact of our rule changes as they are implemented. This will also allow us to respond quickly if any negative impacts come to light.

Pregnancy, maternity and carers	N	N	<p>There were two concerns raised.</p> <p><b>1. Evidence of income</b></p> <p>Pregnant customers or those on maternity leave or taking career breaks may find it more difficult to provide evidence of income that is acceptable to lenders.</p> <p><b>Our response</b></p> <p><i>Lenders are subject to equalities and discrimination legislation and should not have processes that discriminate against customers in this way.</i></p> <p><b>2. Future changes to income</b></p> <p>The requirement to take into account future changes to income and expenditure may conflict with lenders' obligations under equalities legislation, as they would have to ask women about the potential impact of pregnancy and maternity leave on their income.</p> <p><b>Our response</b></p> <p>Our requirements do not conflict with lenders' duties under equalities and discrimination legislation. We have explained in the EIA Annex of the Policy Statement how firms should approach questioning mortgage borrowers about future changes to income in a way that is not discriminatory.</p>
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To protect consumers as much as possible against this we will be checking, through our supervision of the mortgage market, that firms do not introduce lending policies that are discriminatory.

We have established working relationships with a number of stakeholders and will stay in contact with them to monitor the impact of our rule changes as they are implemented. This will also allow us to respond quickly if any negative impacts come to light.

We have previously explained that, as part of our future mortgage market work, we will be reviewing the data collected from firms. As part of this review we will be considering data to help us monitor mortgage activity by the protected groups.

**10. Policy/function owner**

Lynda Blackwell

**11. Critical assessor**

Thomas Francis

**12. Date EIA completed**

10 September 2012



## Appendix 1

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# Made rules (legal instrument)



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# Made rules– Mortgage Market Review (Conduct of Business) Instrument 2012

**MORTGAGE MARKET REVIEW (CONDUCT OF BUSINESS) INSTRUMENT 2012****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 149 (Evidential provisions);
  - (3) section 156 (General supplementary powers); and
  - (4) 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. (1) Part 2 of Annex D to this instrument comes into force on 26 October 2012.
- (2) The remainder of this instrument comes into force on 26 April 2014.

**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
Training and Competence sourcebook (TC)	Annex B
Conduct of Business sourcebook (COBS)	Annex C
Mortgages and Home Finance: Conduct of Business sourcebook (MCOB)	Annex D
Supervision manual (SUP)	Annex E
Professional Firms sourcebook (PROF)	Annex F

**Amendments to material outside the Handbook**

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

**Citation**

- F. This instrument may be cited as the Mortgage Market Review (Conduct of Business) Instrument 2012.

By order of the Board  
27 September 2012

## 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 new text is not underlined.

<i>bridging loan</i>	a <i>regulated mortgage contract</i> which has a term of twelve <i>months</i> or less.
<i>credit-impaired customer</i>	a <i>customer</i> who: <ol style="list-style-type: none"> <li>(a) within the last two years has owed overdue payments, in an amount equivalent to three <i>months</i>' payments, on a mortgage or other loan (whether secured or unsecured), except where the amount overdue reached that level because of late payment caused by errors by a bank or other third party; or</li> <li>(b) has been the subject of one or more county court judgments, with a total value greater than £500, within the last three years; or</li> <li>(c) has been subject to an individual voluntary arrangement or bankruptcy order which was in force at any time within the last three years.</li> </ol>
<i>direct deal</i>	a <i>home finance transaction</i> that can only be obtained direct from a <i>home finance provider</i> , and where that <i>home finance provider</i> is not the selling <i>firm</i> .
<i>execution-only sale</i>	<ol style="list-style-type: none"> <li>(a) a <i>home finance transaction</i> entered into by a <i>firm</i> with, or arranged by a <i>firm</i> for, a <i>customer</i>; or</li> <li>(b) a variation of an existing <i>home finance transaction</i> entered into by a <i>firm</i> with, or arranged by a <i>firm</i> for, a <i>customer</i>;</li> </ol> <p>where the <i>firm</i> does not give <i>advice on home finance transactions</i> to that particular <i>customer</i>, or where the <i>customer</i> has rejected such <i>advice</i> given by the <i>firm</i>.</p>
<i>high net worth mortgage customer</i>	a <i>customer</i> with an annual net income of no less than £300,000 or net assets of no less than £3,000,000, or whose obligations are guaranteed by a person with an income or assets of such amount.
<i>high net worth illustration</i>	an <i>illustration</i> for a <i>regulated mortgage contract</i> to a <i>high net</i>

	<i>worth mortgage customer.</i>
<i>high net worth offer document</i>	an <i>offer document</i> for a <i>regulated mortgage contract</i> to a <i>high net worth mortgage customer</i> .
<i>initial contact</i>	the first occasion when a <i>firm</i> is in contact with the <i>customer</i> and may perform any of the following in relation to a <i>home finance transaction</i> : <ul style="list-style-type: none"> <li>(a) <i>advising</i> on the transaction;</li> <li>(b) <i>arranging (bringing about)</i> the transaction; or</li> <li>(c) <i>entering into</i> the transaction, when there is no <i>firm arranging (bringing about)</i> the transaction.</li> </ul>
<i>interest roll-up mortgage</i>	an <i>interest-only mortgage</i> under which neither capital repayments, nor payment of any of the interest accruing under its terms, are required or anticipated until it comes to an end, whether on expiry of the term (if any), discharge of the mortgage or the happening of some other event.
<i>payment shortfall</i>	the outstanding amount to be paid measured against the amount of payments which have become due during the term of a <i>regulated mortgage contract</i> or <i>home purchase plan</i> , including any <i>arrears</i> amount due.
<i>professional customer</i>	a <i>customer</i> who works or has recently worked in the home finance sector for at least one year in a professional position, which requires knowledge of the <i>home finance transactions</i> or home finance services envisaged, and who the <i>firm</i> reasonably believes to be capable of understanding the risks involved in the transaction or transactions contemplated.

Amend the following definitions as shown.

<i>combined initial disclosure document</i>	information about the breadth of advice, <i>scope of advice</i> or <i>scope of basic advice</i> and the nature and costs of the services offered by a <i>firm</i> in relation to <u>either</u> : <ul style="list-style-type: none"> <li>(a) two or more of the following: <ul style="list-style-type: none"> <li>(a i) <i>packaged products</i> or, for <i>basic advice</i>, <i>stakeholder products</i> that are not a <i>group personal pension scheme</i> or a <i>group stakeholder pension scheme</i> (but only if a <i>consultancy charge</i> will be made);</li> <li>(b ii) <i>non-investment insurance contracts</i>;</li> <li>(c iii) <del><i>regulated mortgage contracts</i></del> <u><i>home finance</i></u></li> </ul> </li> </ul>
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transactions (other than ~~lifetime mortgages~~ regulated sale and rent back agreements); or

- ~~(d) home purchase plans;~~
- ~~(e) equity release transactions;~~
- (b) home finance transactions (other than regulated sale and rent back agreements) only;

which contains the keyfacts logo, headings and text in the order shown in, and in accordance with the notes in, COBS 6 Annex 2.

*early repayment charge* (in MCOB and BSOCS) a charge levied by the mortgage lender on the customer in the event that the amount of the loan is repaid in full or in part before a date or event specified in the contract.

*initial disclosure document* information about the *scope of advice* 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 MCOB 4.4.1R(1) and set out in MCOB 4 Annex 1R;~~
- ~~(b) an equity release transaction as required by MCOB 4.4.1R(1) and set out in MCOB 8 Annex 1R;~~
- ~~(e) a home purchase plan as required by MCOB 4.4.1R(1) 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.~~

*repayment mortgage* a regulated mortgage contract under which the customer is obliged to make payments of interest and capital which are designed to repay the mortgage in full over the stated term.

*repayment vehicle strategy* the means by which the customer ~~will~~ intends to repay the outstanding capital due and, where applicable, pay the interest accrued under the regulated mortgage contract, where all or part of that contract is an *interest-only mortgage*.

## Annex B

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

In this Annex, underlining indicates new text.

## 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 (for a mortgage lender or home reversion provider) an activity which would be <u>arranging (bringing about) but for the exclusion in article 28A Regulated Activities Order (Arranging contracts to which the arranger is a party)</u></u>	20	<i>Regulated mortgage contracts for a non-business purpose</i>	Yes
	<u>20 A</u>	<i><u>Regulated mortgage contracts for a business purpose</u></i>	<u>No</u>
	21	<i>Equity release transactions</i>	Yes

Designing scripted questions for <u>non-advised execution-only sales</u>	<u>21 A</u>	<u>Regulated mortgage contracts for a non-business purpose</u>	<u>Yes</u>
	<u>21 B</u>	<u>Regulated mortgage contracts for a business purpose</u>	<u>No</u>
	22	<i>Equity release transactions</i>	Yes
Overseeing <del>non-advised</del> <u>execution-only sales on a day-to-day basis</u>	23	<i>Equity release transactions</i>	Yes
...			

...

Appendix 4E – Appropriate Qualification tables

...

<p><b>Qualification table for: Advising a customer on <u>or arranging (bringing about)</u> a <i>regulated mortgage contract</i> (for a non-business purpose) - Activity number 20 in TC Appendix 1.1.1R; and <u>Designing scripted questions for use in execution-only sales to customers of regulated mortgage contracts</u> for a non-business purpose - Activity number 21A in TC Appendix 1.1.1R</b></p>
...

<p><b>Qualification table for: Advising a customer on <u>or arranging (bringing about)</u> <i>Equity release transactions</i> - Activity number 21 in TC Appendix 1.1.1R</b></p>
...

...

<p><b>Qualification table for : <del>Overseeing non-advised</del> <u>execution-only</u> sales on a day-to-day basis on <i>Equity release transactions</i> – Activity number 23 in TC Appendix 1.1.1R</b></p>
...

**TP 8 Transitional provisions relating to time limits for attaining qualifications**

...		
8.2	R	<p><u>An <i>employee</i> who is carrying on the activities specified in TC Appendix 1 of:</u></p> <p>(1) <u>arranging (bringing about) regulated mortgage contracts or home reversion plans or (for a mortgage lender or home reversion provider) an activity which would be arranging (bringing about) but for the exclusion in article 28A Regulated Activities Order (Arranging contracts to which the arranger is a party) for a non-business purpose; or</u></p> <p>(2) <u>designing scripted questions for execution-only sales of regulated mortgage contracts for a non-business purpose;</u></p> <p><u>as at 26 April 2014 will, for the purposes of TC 2.2A.1R, be regarded as carrying on such activities only with effect from that date; and, in relation to such an <i>employee</i>, a <i>firm</i> need not (in relation to such activities only) comply with TC 2.1.6R until 26 October 2016. TP 8.1 does not apply in respect of such an <i>employee</i>.</u></p>

## Annex C

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

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

## 6.2A Describing advice services

...

6.2A.4 G (1) A *firm* that provides both *independent advice* and *restricted advice* should not hold itself out as acting independently for its business as a whole. ~~However, a *firm* may hold itself out as acting independently in respect of its services for which it provides *independent advice* or *advice which meets other independence requirements for particular investments*. For example, a *firm* that provides *independent advice* on *regulated mortgage contracts* in accordance with *MCOB* but *restricted advice* on *retail investment products* will not be able to hold itself out as an independent financial adviser. However, it would be able to hold itself out as an adviser providing *independent advice* for *regulated mortgage contracts* provided it was made clear in accordance with the *fair, clear and not misleading rule* that it provided *restricted advice* for *retail investment products*.~~

(1A) A *firm* that offers an unlimited range of *regulated mortgage contracts*, or gives *advice* in relation to *contracts of insurance* on the basis of a fair analysis, but offers *restricted advice* on *retail investment products* should not hold itself out as acting independently for its business as a whole, for example by holding itself out as an independent financial adviser. However, it may disclose that it offers an unlimited range for *regulated mortgage contracts* or gives *advice* in relation to *contracts of insurance* on the basis of a fair analysis provided it makes clear in accordance with the *fair, clear and not misleading rule* that it provides *restricted advice* for *retail investment products*.

...

6 Annex 2 **Combined initial disclosure document described in COBS 6.3, ICOBS 4.5, ~~MCOB 4.4.1R(1)~~ and MCOB 4.10.2R(1) 4.4A.20G**

....

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 2 Whose products do we offer? [Note 4] [Note 4A] [Note 6]
 

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### Home Finance Products [Note 13]

#### ~~[Compliance with Islamic law [Note 18]~~

~~Our services are regularly checked by [name(s) of scholar(s)] to ensure compliance with Islamic law. Ask us if you want further information about the role of our scholar(s).]~~

#### [1] ~~[Lifetime] [Mortgages] [Equity Release Products] [and Islamic] [home reversion schemes purchase plans] [Note 13]~~

~~We offer [lifetime] [mortgages] [home reversion plans] [equity release products] from the whole market.~~

~~We [can] [Note 7] only offer [lifetime] [mortgages] [home reversion plans] [equity release products] from a limited number of [lenders / companies].  
Ask us for a list of the [lenders / companies] we offer [lifetime] [mortgages] [home reversion plans] [equity release products] from. [Note 14]~~

~~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 reversion plan] [equity release products]. [Note 11(2)]~~

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

#### [2] ~~[Islamic Home Purchase Plans] [Note 19] [Note 13]~~

~~We offer Islamic home purchase plans from the whole market.~~

~~We [can] [Note 7] only offer Islamic home purchase plans from a limited number of providers.  
Ask us for a list of the providers we offer Islamic home purchase plans from. [Note 14]~~

We ~~[can] [Note 7] only offer [a limited range of the] [a] Islamic home purchase plan [s] from [a single provider] [name of single provider]. [Note 11(1) and (3)][Note 16]~~

~~[or]~~

~~We only offer our own Islamic home purchase plans. [Note 11(2)]~~

Equity release products are either lifetime mortgages or home reversion plans. [Note 5]

We are not limited in the range of [mortgages] [equity release products] [Islamic] [home purchase plans] we will consider for you [Note 7A]

**[Compliance with Islamic law [Note 18]**

Our services are regularly checked by [name(s) of scholar(s)] to ensure compliance with Islamic law. Ask us if you want further information about the role of our scholar(s).]

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3 Which service will we provide you with? **[Note 4] [Note 4A] [Note 6] [Note 6A]**

---

...

**[Home Finance Products] [Note 13]**

~~—— [1] [Mortgages] [Equity Release Products] [Note 13]~~

~~We will advise and make a recommendation for you on [lifetime mortgages] [home reversions] [equity release products] after we have assessed your needs.~~

~~You will not receive advice or a recommendation from us. We may ask some questions to narrow down the selection of [lifetime mortgages] [home reversions] [equity release products] that we will provide details on. You will then need to make your own choice about how to proceed.~~

**[2] [Islamic Home Purchase Plans] [Note 13]**

~~We will advise and make a recommendation for you after we have assessed your needs.~~

~~You will not receive advice or a recommendation from us. We may ask some questions to narrow down the selection of products that we will provide details on. You will then need to make your own choice about how to proceed.~~

<b>4</b>	<b>What will you have to pay us for our services? [Note 4A] [Note 20A]</b>
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...

**[Home Finance Products] [Note 13]****[1] [Mortgages] [Equity Release Products] [Islamic] [Home Purchase Plans] [Note 13]**

- No fee. [We will be paid by commission from the [lender/~~company that buys your home provider~~.] [Note 33]  
A fee of £[ ] payable at the outset and £[ ] payable when you apply for a [lifetime] [mortgage] [home reversion plan] [equity release product] [Islamic] [home purchase plan]. [We will also be paid commission from the [lender/~~company that buys your home provider~~.]]. [Note 33] [Note 34]
- 

You will receive a ~~key facts illustration~~ keyfacts illustration when considering a particular [lifetime] [mortgage] [home reversion plan] [equity release product], which will tell you about any fees relating to it. [Note 13] [Note 13A]

**Refund of fees [Note 32] [Note 13]**

If we charge you a fee, and your [lifetime] [mortgage] [home reversion plan] [Islamic] [home purchase plan] does not go ahead, you will receive: [Note 35]

- A full refund [if the [lender/~~company provider~~] rejects your application]. [Note 36]
- A refund of £ [ ] [if your application falls through]. [Note 36] [Note 37] [Note 38]
- No refund [if you decide not to proceed]. [Note 36]

**[2] [Islamic Home Purchase Plans] [Note 13]**

- No fee. [We will be paid by commission from the provider.] [Note 33]
- A fee of £[ ] payable at the outset and £[ ] payable when you apply for an Islamic home purchase plan. [We will also be paid commission from the provider]. [Note 18]

**Refund of fees [Note 35]**

If we charge you a fee, and your Islamic home purchase plan does not go ahead, you will receive: [Note 32]

- A full refund [if the provider] rejects your application]. [Note 36]
- A refund of £ [ ] [if your application falls through]. [Note 36] [Note 37] [Note 38]
- No refund [if you decide not to proceed]. [Note 36]

...

---

**8 Are we covered by the Financial Services Compensation Scheme (FSCS)?**  
[Note 4A] [Note 39] [Note 55] [Note 56]

---

...

**[Note 59] Message from the Financial Services Authority**

**Think carefully about this information before deciding whether you want to go ahead.**

**If you are at all unsure about which equity release product is right for you, you should ask your adviser to make a recommendation.**

...

**Note 4** – a *firm* should describe the services that it expects to provide to the particular *client*. For services in relation to:

...

- ~~equity release transactions~~ – the *firm* should select a maximum of two boxes within this section. *Firms* should not omit the boxes not selected.
- home finance transactions (other than regulated sale and rent back agreements) – where the *firm* will be providing services to a *consumer* by way of a *distance contract*, it should include in Section 3 a statement that explains whether or not the *consumer* will receive *advice* as part of the services. It should insert the appropriate heading above the statement in accordance with Note 13 (1).

**Note 4A** - If a *firm* is not offering all product types it should omit the headings and text relating to the product types it is not offering. For example, if it is completing the relevant sections of this template in relation to insurance and home finance products but not investment products, it should omit the heading “Investment” and the corresponding text.

**Note 5** – a *firm* should include this sentence if, and only if, it offers *equity release transactions*.

...

**Note 6A** – If the *combined initial disclosure document* is used only in relation to *home finance transactions* (except where Section 3 is required to be used for *home finance transactions* as the *firm* is providing services by way of a *distance contract*: see Note 4), the *firm* should delete this heading and re-number the later sections accordingly.

**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*; ~~or insurer; lender; home purchase provider or home reversion provider~~ is selling its own products.

**Note 7A** - This sentence must only be used where there are no limitations in the product range that a *firm* will be providing to the *customer*. Otherwise, the *firm* must insert alternative text that describes in simple, clear terms the limits on its product range for the relevant market. If the *firm* is not considering products from a comprehensive range across the market and has not listed here the name of every lender/provider it offers products from, the text used must offer a list of these lenders/providers. Where the *firm* offers *equity release products*, it must state if it offers *home reversion plans* but not *lifetime mortgages*, or vice versa. The *firm* must also state that it will not consider *direct deals*, where that is the case. Depending on the *firm*’s precise circumstances, the following examples may be appropriate:

- “We offer a comprehensive range of [mortgages] [equity release products] [Islamic] [home purchase plans] from across the market, but not deals that you can only obtain by going direct to a [lender/provider].”
- “We only offer products from [number] [lenders/providers]. We can provide you with a list of these.”
- “We only offer some, but not all, of the [mortgages] [equity release products] [Islamic] [home purchase plans] from [number] [lenders/providers]. We can provide you with a list of these.”
- “We only offer the [mortgages] [equity release products] [Islamic] [home purchase plans] from [name of lender(s)/provider(s)].”
- “We only offer some, but not all, of the [mortgages] [equity release products] [Islamic] [home purchase plans] from [name of lender(s)/provider(s)].”
- “We only offer lifetime mortgages from [name of lender(s)] and home reversion plans from [name of provider(s)].”
- “We only offer [lifetime mortgages/home reversion plans] but not [lifetime mortgages/home reversion plans]. We only offer [lifetime mortgages/home reversion plans] from [name of provider] and we only offer some, but not all, of their products.”
- “We only sell bridging finance products from [name of lender(s)]. We do not offer products from across the mortgage market.”

...

**Note 11** – if the *firm* selects this box, it will be offering the products of one provider for a particular product type. It should therefore follow the format specified in (1) below except when offering its own products, in which case it should follow (2) instead. In the case of *non-investment insurance contracts*, where the *firm* is providing a service in relation to different types of insurance, this box covers the situation where it is offering a particular type of insurance from a single *insurance undertaking*.

- (1) Insert the name of the provider, namely the *product provider* for *packaged products*, and 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 policy from [name of *lender* *insurance undertaking*]”. ~~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.~~
- (2) If the *firm* is a *product provider* offering only its own products, or is part of a *product provider* offering only the products sold under that part’s trading name, it should use this alternative text.
- ~~(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 12** – ~~if the *firm* does not give *personal recommendations* advise or give personalised information on, both types of *equity release transactions*, then it should indicate to the *client* the sector that the *firm* does not cover. However, if the *firm*’s scope of service does not include *equity release transactions*, the last box (“We do not offer [lifetime mortgages] [home reversion plans]”), should be omitted.~~

**Note 13** – in describing the services and products provided, *firms* should omit the text in brackets that do not apply and ensure that they describe accurately their activities with respect of the services and products that they offer, as follows:

- (1) Headings and sub-headings:
  - a. If the *firm* offers ~~both~~ a combination of *regulated mortgage contracts* and, *home purchase plans* and *equity release products*, it should include the heading “Home Finance Products” in the *combined initial disclosure document* and describe the *regulated mortgage contracts*, ~~and *home purchase plans* and *equity release transactions*~~ (as applicable) that it offers under ~~two~~ separate sub-headings. The sub-headings (“Mortgages”, ~~and “Home Purchase Plans”~~ and

“Equity Release Products”) should be numbered accordingly. If the *firm* only offers one of these ~~two~~ three products, then the heading “Home Finance Products” should be omitted and the heading will read “Mortgages”, or “Home Purchase Plans” or “Equity Release Products”, as appropriate.

- b. If the *firm* offers *equity release transactions*, then the appropriate heading ~~“Home Finance Products” should be omitted and the~~ or sub-heading will read is “Equity Release Products” (even if the *firm* offers ~~*equity release transactions from only one sector*~~) only lifetime mortgages or only home reversion plans.

...

(2) Describing the products:

- a. If a *firm* gives ~~*personal recommendations*~~ or gives personalised information *advice on, or arranges execution-only sales in,* lifetime mortgages, it should change “mortgage” to “lifetime mortgage”
- b. If a *firm* gives ~~*personal recommendations*~~ or gives personalised information *advice on, or arranges execution-only sales in,* home reversion plans, it should use the text in brackets relating to home reversion plans.
- c. If the *firm* gives ~~*personal recommendations*~~ or gives personalised information *advice on, or arranges execution-only sales in,* products from both equity release market sectors, then it should use the term ‘equity release products’ when referring to them collectively.

(3) Describing the provider: If a *firm* gives ~~*personal recommendations*~~ or gives personalised information *advice on, or arranges execution-only sales in,* *home purchase plans* or *home reversion plans*, it should change “mortgage” to “product” and “lender” to “company” or “provider”, as appropriate.

(4) Home purchase plans: A *firm* that carries on *home purchase activities* may add the word “Islamic” to “home purchase plan(s)” if it holds out one or more *home purchase plans* within its product range as compliant with Islamic law. If “Islamic” is included, it should be included consistently throughout the document. However, a *firm* may omit the word “Islamic” in sections 5 and 8 even if it uses it elsewhere throughout the document. A *firm* that wishes to hold itself, its products or services out as compliant with religious or philosophical belief other than Islamic law may include an appropriate description in place of the references to “Islamic” and “Islamic law”.

(5) A *firm* offering services in relation to loans for business purposes must use a description of its services which make that clear.

**Note 13A** – A *firm* must not include this paragraph if the only services to which the combined initial disclosure document relates are activities relating to *home purchase plans*. A *firm* may include a similar explanation regarding the financial information statement if the services they offer include activities relating to *home purchase plans*.

**Note 14** – for services provided in relation to *home 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 finance transactions* from in the previous line, so long as the *firm* offers all of the products generally available from each.

...

**Note 16** – if the *firm* does not select this box, it should alter the wording to say “a single group of companies” for *packaged products*; and “a single insurer” for *non-investment insurance contracts*; ~~“a single lender” for *regulated mortgage contracts* or *lifetime mortgages* and “a single company” (or “a single provider”) for *home purchase plans* and *home reversion plans*.~~ For example: “We only offer the products from a single group of companies” should replace the text in the specimen *combined initial disclosure document*.

...

**Note 18** – This subsection is ~~optional unless~~ may (at the *firm*'s option) be used if, and only if, the *firm* holds itself, its ~~*regulated mortgage contract* or *home purchase plan*~~ products or services out as compliant with Islamic law ~~in the *combined initial disclosure document*~~. If a *firm* includes this section it should describe it as Section 2 and renumber subsequent sections accordingly.

A *firm* that wishes to hold itself, its ~~*regulated mortgage contract* or *home purchase plan*~~ products or services out as compliant with religious or philosophical beliefs other than Islamic law ~~in the *combined initial disclosure document*~~ may also use the subsection in accordance with this note and modify the wording in the section to the extent appropriate.

**Note 19** – ~~A *firm* that carries on *home purchase activities* may omit the word “Islamic” from “Islamic home purchase plan(s)” if one or more *home purchase plans* within its scope of service is not held out as compliant with Islamic law. If “Islamic” is omitted, it should be omitted consistently throughout the document. However, a *firm* may omit the word “Islamic” in sections 5 and 8 without having to omit it throughout the document. A *firm* that wishes to hold itself, its products or services out as compliant with religious or philosophical belief other than Islamic law in the *combined disclosure document* may make appropriate amendments to references to “Islamic” and “Islamic law”.~~

...

**Note 34** – insert a plain language description of when any *fees* are payable for services relating to *home finance transactions*, and the amount ~~This description could include, for example, a cash amount, a percentage of the loan or reversion amount or the amount per hour, as appropriate. However, where a cash amount is not disclosed, one or more examples of the cash amount should be included.~~ If a *firm* offers more than one pricing option in relation to *equity release transactions*, it should specify the pricing policy for each of them. For example, “A fee of £[XX] payable at the outset and £[YY] when you apply for a lifetime mortgage and £[ZZ] when you apply for a home reversion plan”. If a *firm* does not charge a *fee*, the text for the second box should be abbreviated to ‘A fee’. The fee must be described, where possible, as a cash sum, but where this is not possible:

- If the fee is a percentage of another sum which is not yet known (such as the amount to be borrowed), give the percentage and a representative illustrative example which gives an amount as a cash sum.
- If the fee will be one of a range of possible cash fees, provide a description of the fee in terms which include the maximum and minimum possible fees as cash sums, and what factors will determine where in the range the fee will be.
- If the fee will be one of a range of fees that are a percentage of another sum which is not yet known (such as the amount to be borrowed), give the minimum and maximum percentages and a representative illustrative example which gives an amount as a cash sum, and set out what factors will determine where in the range the fee will be.
- If the fee will be based on an hourly rate, but the number of hours to be spent on the *customer's* transaction is unknown, state the hourly rate in cash terms and set out what factors will determine how many hours it takes to provide the *firm's* services.

...

**Note 39** – the *firm* may omit this section for services relating to *packaged products* if the *firm* has, on first contact with the *client*, provided the *client* with its *client agreement* which contains that information. This section may be omitted for services relating to *non-investment insurance contracts* if the information covered by this section is not required by *ICOBS* or is required by *ICOBS* but is provided to the *customer* by some other means. ~~This section may be omitted for services relating to *home finance transactions* in accordance with *MCOB 4.4.1R(3)*.~~ If this section is omitted, the other sections of the *combined initial disclosure document* should be renumbered accordingly.

...

~~**Note 59** – this warning box should be added when the *firm* sells *lifetime mortgages* or *home reversion plans* or both.~~

## Annex D

**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.

**Part 1: Comes into force on 26 April 2014**

**1.2 General application: who? what?**

- 1.2.1 R (1) This sourcebook applies to every *firm* that:
- (a) carries on a *home finance activity* (subject to the business loan and loans to high net worth mortgage customers application provisions); or

...

Firm types and the home finance activities

- 1.2.2 G (1) This sourcebook applies to activities carried out in respect of ~~four types of product:~~ regulated mortgage contracts (which includes lifetime mortgages), equity release transactions, home purchase plans, home reversion plans and regulated sale and rent back agreements...

...

Business loans and loans to high net worth mortgage customers: application of MCOB

- 1.2.3 R In relation to a *regulated mortgage contract* for a business purpose
- (1) *MCOB* applies if the *customer* is not a *large business customer*; and
- (2) if *MCOB* applies, a *firm* must either:
- (a) comply with *MCOB* in full (disregarding the tailored provisions for *regulated mortgage contracts* for a business purpose in the remainder of *MCOB*); or
- (b) comply with *MCOB* in full, but taking account of all those tailored provisions, including *MCOB* 1.2.7R.

- 1.2.3A R In relation to a regulated mortgage contract with a high net worth mortgage customer, a firm must either:

- (a) comply with MCOB in full (disregarding the tailored provisions for *regulated mortgage contracts with high net worth mortgage customers* in the remainder of MCOB); or
- (b) subject to MCOB 1.2.9CR, comply with MCOB in full, but taking account of all those tailored provisions, including MCOB 1.2.7R.

1.2.3B      **R**      Where any provision of MCOB is expressed to apply in respect of a *high net worth mortgage customer*, it applies in respect of joint borrowers (or potential borrowers) if one of them satisfies that definition in his own right.

1.2.4      **G**      ~~For detail of the~~ The tailored provisions applying, see are those in the sections section on ‘business Business loans’ and loans to high net worth mortgage customers: tailored provisions’ set out in each relevant chapter.

1.2.4A      **G**      Certain other provisions of MCOB apply in all cases in respect of *high net worth mortgage customers* or of transactions which are solely for a business purpose. The application of the tailored and other provisions for *high net worth mortgage customers* and transactions for a business purpose are summarised in the table at MCOB 1.2.4BG.

1.2.4B      **G**      **Table of provisions applicable to business loans and high net worth mortgage customers: this table belongs to MCOB 1.2.4AG**

<u>Provisions</u>	<u>Tailored provisions or applicable in all cases?</u>	<u>For business loans only, are the provisions applicable to all business loans, or only where the loan is solely for a business purpose?</u>
<u>Various of the provisions in MCOB 4.7A and MCOB 4.8A</u>	<u>Applicable in all cases</u>	<u>Applicable only where loan is solely for a business purpose</u>
<u>MCOB 4.9</u>	<u>Tailored</u>	<u>Applicable to all business loans</u>
<u>MCOB 5.7</u>	<u>Tailored</u>	<u>Applicable to all business loans</u>
<u>MCOB 6.7</u>	<u>Tailored</u>	<u>Applicable to all business loans</u>
<u>MCOB 7.7</u>	<u>Tailored</u>	<u>Applicable to all business loans</u>

<u>Various of the provisions in MCOB 11.6</u>	<u>Applicable in all cases</u>	<u>Applicable only where loan is solely for a business purpose</u>
<u>MCOB 12.6</u>	<u>Tailored</u>	<u>Applicable to all business loans</u>
<u>MCOB 13.7</u>	<u>Tailored</u>	<u>Applicable to all business loans</u>

- 1.2.5 G (1) ...
- (2) Whether a *regulated mortgage contract* is, or is solely, for a business purpose will be a matter of fact to be determined by a *firm* (in accordance with *MCOB 1.2.9DR* where applicable) depending on the individual circumstances of each case...
- ...
- Business loans and loans to high net worth mortgage customers: additional requirements if tailored route is used
- 1.2.7 R In relation to a *regulated mortgage contract* for a business purpose or with a high net worth mortgage customer, if a *firm* has opted for the tailored route, it must adopt the following modifications to the sourcebook:
- (1) (except in relation to ~~sections 6 and 8 of any initial disclosure document~~ or sections 5 and 8 of any *combined initial disclosure document*) substitute an alternative description of the facility provided under the *regulated mortgage contract* for 'mortgage' where that term is used in any disclosure;
- (2) substitute the term 'illustration' for ~~'key facts'~~ 'keyfacts illustration' when opting to use the tailored business loans or loans to high net worth mortgage customers rules in *MCOB 4.9*, *MCOB 5.7*, *MCOB 6.7* or *MCOB 7.7*; and
- ...
- 1.2.8 G (1) *Firms* are reminded of the requirement in *MCOB 2.2.6R* that any communication should be clear, fair and not misleading when substituting an alternative for the term 'mortgage' in accordance with *MCOB 1.2.7R(1)*.
- (2) Possible alternatives to the term 'mortgage' include, for example, 'secured ~~business~~ overdraft', 'secured loan' or 'secured business credit'.
- 1.2.9 G The disclosure *rules* in *MCOB* place particular emphasis on the description of borrowing. Where the *regulated mortgage contract* is for

a business purpose or with a *high net worth mortgage customer*, a firm should reflect this emphasis in any disclosure by first describing any borrowing before addressing the other facilities provided under the regulated mortgage contract.

...

Provisions for professional customers

1.2.9B      G      Certain provisions of MCOB 4.7A and MCOB 4.8A apply in respect of professional customers. Where they apply, they provide greater flexibility for firms.

Requirement for evidence before treating a loan as being solely for business purposes, or a customer as a high net worth mortgage customer or a professional customer

1.2.9C      R      A firm may not treat a customer as being a high net worth mortgage customer for the purposes of MCOB unless either:

(1) it is aware, from evidence already in its possession as a result of a business relationship between it and the customer, that the customer satisfies the definition of high net worth mortgage customer; or

(2) it has first obtained a written statement which:

(a) confirms that the customer satisfies the definition of high net worth mortgage customer;

(b) specifies the period for which it is valid, which includes the time when the regulated mortgage contract is entered into; and

(c) is signed by a suitably qualified professional adviser of the customer who is not an associate of the firm or of the customer.

1.2.9D      R      A firm must not treat a loan as being solely for a business purpose for the purposes of MCOB unless it has reviewed a business plan provided by the customer which provides credible evidence that that is the case.

1.2.9E      R      A firm must not treat a customer as being a professional customer for the purposes of MCOB unless it has credible evidence that the customer satisfies the definition.

1.2.9F      R      A firm must keep the evidence in MCOB 1.2.9CR(1) and MCOB 1.2.9ER, the business plan in MCOB 1.2.9DR and the written statement in MCOB 1.2.9CR(2) for not less than three years from the date on which it was obtained or, if later, used to satisfy MCOB 1.2.

Authorised professional firms

1.2.10 R *MCOB* does not apply to an *authorised professional firm* with respect to its *non-mainstream regulated activities* except for:

...

(2) ... ~~;~~ and.

(3) ~~initial disclosure requirements but only as regards providing the information contained in section 7 (What to do if you have a complaint) and section 8 (Are we covered by the Financial Services Compensation Scheme?) of an initial disclosure document or combined initial disclosure document (see *MCOB* 4.4 and *MCOB* 4.10).~~ [deleted]

...

**1.3 General application: where?**

...

Distance contracts entered into from an establishment in another EEA State

1.3.4 R ...

(2) The *rules* which do not apply are:

(a) initial disclosure requirements in *MCOB* 4.4 4.4A (in respect of *regulated mortgage contracts*)...

...

(g) *MCOB* 8.3 (Application of rules in *MCOB* 4) to the extent that it applies *MCOB* 4.4 4.4A to *MCOB* 4.6;

...

...

**2.1 Application**

Who?

...

2.1.2 R This table belongs to *MCOB* 2.1.1 R

(1) Category of firm	(2) Applicable section
<i>mortgage lender</i>	whole chapter except <i>MCOB</i> 2.2.6AR, <i>MCOB</i> 2.2.8AR, <i>MCOB</i> 2.2.8BG, <i>MCOB</i> 2.6A.1R to

<i>mortgage administrator</i> <i>mortgage adviser</i> <i>mortgage arranger</i>	<u>2.6A.18G</u> and <i>MCOB 2.8.6G</i>
<i>mortgage administrator</i> <i>mortgage adviser</i> <i>mortgage arranger</i>	As for a <i>mortgage lender</i> , except that <i>MCOB 2.6A.-1R</i> does not apply.
<i>home purchase provider</i>	<i>MCOB 2.1, MCOB 2.2.1G, MCOB 2.2.6R to MCOB 2.2.9G, MCOB 2.5, to MCOB 2.6, MCOB 2.6A.1R to MCOB 2.6A.4G, MCOB 2.6A.7G to MCOB 2.6A.10G, MCOB 2.7.4R to MCOB 2.7.6R, MCOB 2.7A and MCOB 2.8.6G</i>
...	
<i>SRB administrator</i>	<i>MCOB 2.1, MCOB 2.2.1G, MCOB 2.2.2G, MCOB 2.2.3R, MCOB 2.2.6R, MCOB 2.2.7G, MCOB 2.2.8G, MCOB 2.5, to MCOB 2.6, MCOB 2.6A.5BR(5), MCOB 2.6A.8R to MCOB 2.6A.11G, MCOB 2.6A.17AR, MCOB 2.6A.18G, MCOB 2.7.1G to MCOB 2.7.5R, MCOB 2.7A, MCOB 2.8.1G to MCOB 2.8.5G.</i>
...	

...

## 2.2 Communications

...

### Related investment advice

- 2.2.5 G *Firms* are reminded that they should follow the relevant *rules* in *COBS 6* and *COBS 13* relating to advice and disclosure on *investments* if they are *advising the customer* on an *investment* such as an annuity associated with an *equity release transaction* or an *ISA* used as a *repayment vehicle strategy*.

...

## 2.5A The customer's best interests

- 2.5A.1 R A firm must act honestly, fairly and professionally in accordance with the

best interests of its customer.

...

**2.6A Protecting customer's interests: regulated mortgage contracts, home purchase plans, home reversion plans and regulated sale and rent back agreements**

Protecting customer's interests: regulated mortgage contracts

2.6A-1 R A mortgage lender may only include, or rely on, a term in a regulated mortgage contract which permits it to change the rate of interest from a fixed, discounted or other concessionary rate to the firm's standard variable rate in the event of a breach of contract if each of the following conditions is met:

- (1) the breach of contract is material;
- (2) the breach of contract is unrelated to a payment shortfall; and
- (3) that standard variable rate is not an interest rate created especially for customers who are (either at all, or in particular ways) in breach of contract.

...

Protecting customers' interests under regulated sale and rent back agreements: security of tenure

2.6A.5B R (1) When ~~entering into a~~ entering into a regulated sale and rent back agreement, a firm must ensure that, under the terms of the *regulated sale and rent back agreement*:

...

- (2) When ~~entering into a~~ entering into a regulated sale and rent back agreement, a firm must ensure that, under the terms of the *regulated sale and rent back agreement*, if the property is in England and Wales, the terms of the tenancy do not:

...

- (3) When ~~entering into a~~ entering into a regulated sale and rent back agreement, a firm must ensure that, under the terms of the *regulated sale and rent back agreement*, if the property is in Scotland, the terms of the tenancy do not include:

...

- (4) When ~~entering into a~~ entering into a regulated sale and rent back agreement, a firm must ensure that, under the terms of the *regulated sale and rent back agreement*, if the property is in Northern Ireland,

the terms of the tenancy do not include:

...

...

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

...

3.8.6 G Firms should note the additional disclosure requirements in ~~MCOB 4.4.7R~~ (~~Disclosure 4.4A.17R~~ (Additional disclosure where initial contact is by telephone), ~~MCOB 4.4A.18R~~ (Additional disclosure requirements where the services are to be provided to a consumer under a distance contract) 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*.

...

**4.1 Application**

Who?

...

4.1.2 R Table This table belongs to MCOB 4.1.1R

(1) Category of firm	(2) Applicable section
<i>mortgage lender</i>	<u>except in relation to lifetime mortgages: MCOB 4.1 to MCOB 4.4 4.4A, 4.6A, and MCOB 4.8 4.8A in accordance with MCOB 4.1.2A R, to and MCOB 4.9</u>
<i>mortgage adviser</i>	<u>except in relation to lifetime mortgages: whole chapter except MCOB 4.10</u>
<i>mortgage arranger</i>	<u>except in relation to lifetime mortgages: whole chapter except MCOB 4.7 4.7A and MCOB 4.10</u>
<i>home purchase provider</i>	<u>MCOB 4.1, MCOB 4.2 and MCOB 4.10 (except MCOB 4.10.5G to MCOB 4.10.7G). MCOB 4.3, MCOB 4.4 4.4A and MCOB 4.8 4.8A in accordance with MCOB 4.1.2BR and MCOB 4.10</u>

<i>home purchase adviser</i>	<i>MCOB 4.1, MCOB 4.2, MCOB 4.5, MCOB 4.6 and MCOB 4.10.</i> <del><i>MCOB 4.3, MCOB 4.4 4.4A, MCOB 4.7 4.7A and MCOB 4.8 4.8A</i></del> in accordance with <i>MCOB 4.10</i>
<i>home purchase arranger</i>	As for a <i>home purchase adviser</i> except <del><i>MCOB 4.10.5G to MCOB 4.10.7G MCOB 4.10.5AR to MCOB 4.10.9AR, 4.10.13R and MCOB 4.7 4.7A</i></del> do not apply
<del><i>reversion equity release provider</i></del> <del><i>reversion equity release adviser</i></del> <del><i>reversion equity release arranger</i></del>	See <i>MCOB § 8.3</i> for the application of this chapter
...	

4.1.2A R *MCOB 4.8A only applies to a mortgage lender in relation to entering into a regulated mortgage contract where there is no firm which is arranging (bringing about) the regulated mortgage contract to which MCOB 4.8A applies.*

4.1.2B R *MCOB 4.8A only applies to a home purchase provider (as provided in MCOB 4.10.9BR) in relation to entering into a home purchase plan where there is no firm which is arranging (bringing about) the home purchase plan to which MCOB 4.8A applies (as provided in MCOB 4.10.9BR).*

4.1.2C G *MCOB 4.1.2AR and MCOB 4.1.2BR mean that the provisions in MCOB 4.8A on execution-only sales, including the prohibition on entering into them in the circumstances specified in that section, only apply to sales by mortgage lenders or home purchase providers where there is no intermediary firm to which that section applies.*

4.1.2D G *MCOB 4.1.2AR and MCOB 4.1.2BR mean that the situations where MCOB 4.8A applies to a mortgage lender or home purchase provider include where a mortgage intermediary or home purchase intermediary has been involved in arranging a regulated mortgage contract or home purchaser plan but is no longer involved in the transaction.*

What?

4.1.3 R *This chapter applies if a firm in the course of carrying on a home finance activity: enters into, advises on or arranges a home finance transaction or a variation of the terms of a home finance transaction.*

(1) ~~*makes, or anticipates making, a personal recommendation about;*~~  
or

- (2) ~~gives, or anticipates giving, personalised information relating to; the customer~~
- (3) ~~entering into a home finance transaction; or~~
- (4) ~~varying the terms of a home finance transaction entered into by the customer.~~

...

4.1.6 G ~~MCOB 4.1.5 R means that this chapter, MCOB 4, deals with standard regulated mortgage contracts, home purchase plans and regulated sale and rent back agreements only and therefore firms should note that the scope of service rules in this chapter do not apply in respect of equity release transactions. [deleted]~~

...

## 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 ~~nature of the service they may receive from a firm in relation to home finance transactions~~. In particular ~~firms need to make clear to customers the scope~~ range of home finance transactions available from them firms and the basis of their remuneration; and
  - (b) where ~~advice~~ is given, it is suitable for the ~~customer~~. ~~The steps firms need to take to ensure that the customer receives suitable advice will vary depending on the demands and needs of the customer and the type of home finance transaction.;~~
  - (c) the firm provides advice whenever it makes a sale during which there is spoken or other interactive dialogue between the firm and the customer (with exceptions for high net worth mortgage customers and professional customers, and for loans which are solely for a business purpose);
  - (d) when there is no spoken or other interactive dialogue between the firm and the customer during the sale, the firm is able to provide an execution-only service except for certain vulnerable customers (customers for regulated sale and rent back and equity release transactions; customers whose main

purpose is debt consolidation; and *customers* who are using the transaction in order to exercise a statutory “right to buy”) who are given advice in every case;

- (e) *execution-only sales* are only provided where the *customer* has been warned about the implications of proceeding without *advice*, or where the *customer* has rejected *advice* which has been given, and has specifically instructed the *firm* that he wishes to do so; and
- (f) except in the case of *regulated sale and rent back transactions*, *customers* have the right to reject *advice* and proceed on an execution-only basis.

- (3) This chapter also implements certain requirements of the *Distance Marketing Directive* in relation to *distance mortgage mediation contracts* and *distance home purchase mediation contracts*.

...

The existing section 4.3 is deleted in its entirety. The existing text is not struck through.

### **4.3 Scope of service provided** [deleted]

MCOB 4.4 is deleted in its entirety and replaced with a new section MCOB 4.4A. The deleted text is not shown and the new text is not underlined.

### **4.4 Initial disclosure requirements** [deleted]

#### **4.4A Initial disclosure requirements**

Description of a firm’s services in all cases

- 4.4A.1 R Using the methods and at the times specified in this section, a *firm* must provide the *customer* with the following information:
  - (1) whether there are any limitations in the range of products that it will offer to the *customer*, and if so what those are; and
  - (2) the basis on which the *firm* will be remunerated.

Range of products

- 4.4A.2 R (1) The limitations in *MCOB* 4.4A.1R include any limitations on the *regulated mortgage contracts* the *firm* will consider from within the relevant market. A *firm* which is offering services to a *customer* in

respect of more than one type of relevant market must describe its services in relation to each such relevant market.

- (2) For these purposes, there are two relevant markets for *regulated mortgage contracts* (apart from *lifetime mortgages*): one for *regulated mortgage contracts* that are not for a business purpose; and one for *regulated mortgage contracts* that are. A *firm* offering services in relation to loans for a business purpose must make that clear in its disclosure under *MCOB 4.4A.1R(1)*.
  - (3) If a *firm* will not, as part of its services, consider *direct deals*, it need not treat that as a limitation in its product range, but the *firm* must tell the *customer* as part of the disclosure under *MCOB 4.4A.1R(1)* that it will not consider *direct deals*.
- 4.4A.3 G (1) A *firm* that only offers products from one part of a relevant market (for example, just *bridging loans*) should not disclose its service as unlimited.
- (2) When considering whether there are any limitations in its product range across the relevant market, a *firm* need not take account of the existence of exclusive deals which a *mortgage lender* offers to be sold by one or a limited number of *mortgage intermediaries* only (and not generally by *mortgage intermediaries* across the relevant market).
- 4.4A.4 R (1) If a *firm* is not offering to the *customer* products from an unlimited range from across the relevant market, its disclosure on product range in *MCOB 4.4A.1R* must either:
- (a) list the names of all the *mortgage lenders* whose products it is offering; or
  - (b) inform the *customer* of the number of *mortgage lenders* whose products it is offering and that he has the right to request a list of those *mortgage lenders*.
- (2) If a *customer* requests the list in (1), the *firm* must provide it in a *durable medium* as soon as possible following the request and in any event within five *business days*. The list must also indicate whether the *firm* offers all of the products generally available from each *mortgage lender* on the list.
- 4.4A.5 G A *firm* may be able to describe its product range as unlimited even if it offers its *customers* only a selection of the *regulated mortgage contracts* available from the relevant market, or uses ‘panels’. The *firm* would need to ensure that any panel, or selection of products, is sufficiently broad in its composition that it is representative of products from across the market, that it is reviewed regularly, and that its use does not materially disadvantage any *customer*. In such a case, 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.

- 4.4A.6 G The disclosure required by *MCOB* 4.4A.1R(1), *MCOB* 4.4A.2R and *MCOB* 4.4A.4R(1) about limitations in product range and *direct deals* should be expressed in simple, clear terms. A *firm* may wish to consider using a sentence appropriate to the circumstances, along the following lines:
- “We are not limited in the range of mortgages we will consider for you.”
  - “We offer a comprehensive range of mortgages from across the market, but not deals that you can only obtain by going direct to a lender.”
  - “We only offer mortgages from [number] lender(s). We can provide you with a list of these.”
  - “We only offer mortgages from [name of lender(s)].”
  - “We only offer some, but not all, of the mortgages from [number] lender(s). We can provide you with a list of these.”
  - “We only offer some, but not all, of the mortgages from [name of lender(s)].”
  - “We only sell bridging finance products from [name of lender(s)]. We do not offer products from across the mortgage market.”
- 4.4A.7 G (1) *Firms* are reminded that, in the light of the *rules* and *guidance* in *SYSC*, they should have adequate systems and controls in place to ensure that the disclosure they make to a *customer* about their service reflects the service the *customer* is actually offered.
- (2) *Firms* are also reminded that *Principle 7* (Communications with clients) and *MCOB* 2.2.6R (Clear, fair and not misleading communications) are also relevant to how they describe their services, including in any business name they adopt. For example, a *firm* should not call itself an “independent mortgage adviser” unless its product range across the relevant market is unlimited.
- (3) A *firm* that offers a different service for different product types should not disclose that it offers one type of service for its business as a whole. For example, a *firm* that provides independent advice on retail investment products but only offers a limited range of *regulated mortgage contracts* should ensure it discloses to the *customer* that the service is different for the different products.
- (4) There are additional *rules* about complying with *MCOB* 4.4A.1R(1) in relation to *home purchase plans* and *equity release transactions* at

*MCOB* 4.10.3BR and *MCOB* 8.3.2BR.

## Basis of remuneration

- 4.4A.8 R (1) The information about the basis of remuneration required by *MCOB* 4.4A.1R(2) must include all relevant information, including the following details:
- (a) any fees which the *firm* will charge to the *customer*;
  - (b) when any such fees will be payable and, if applicable, reimbursable; and
  - (c) whether the *firm* will receive commission from a third party and, if applicable, any arrangements for offsetting this against any fees charged.
- (2) The details in (1)(a) must be expressed, where possible, as a specific cash sum, but the following *rules* apply where this is not possible:
- (a) If the *firm* will charge a fee that is a percentage of another sum which is not yet known (such as, but not limited to, the amount to be borrowed), the *firm* must provide details of the percentage and a representative illustrative example which gives an amount as a cash sum.
  - (b) If the *firm* will charge one of a range of possible cash fees, the *firm* must provide a description of the fee in terms which include the maximum and minimum possible fees as cash sums, and what factors will determine where in the range the fee will be.
  - (c) If the *firm* will charge one of a range of fees that are a percentage of another sum which is not yet known (such as, but not limited to, the amount to be borrowed), the *firm* must provide details of the minimum and maximum percentages and a representative illustrative example which gives an amount as a cash sum, and set out what factors will determine where in the range the fee will be.
  - (d) If the *firm* will charge an amount based on an hourly rate, but the number of hours to be spent on the *customer's* transaction is unknown, the *firm* must state the hourly rate in cash terms and set out what factors will determine how many hours it takes to provide the *firm's* services.

## Method of providing initial disclosure in all cases

- 4.4A.9 R The information required by *MCOB* 4.4A.1R, *MCOB* 4.4A.2R, *MCOB* 4.4A.4R(1) and *MCOB* 4.4A.8R must be communicated clearly and prominently, and in doing so:

- (1) if the *initial contact* includes spoken interaction, the information must be communicated orally; and
- (2) if the *initial contact* does not include spoken interaction, the messages must appear separately from other messages in the communication.

If the *initial contact* is made by electronic means, the *firm* must ensure that the *customer* cannot progress to the next stage of the sale unless the information has been communicated to the *customer*.

- 4.4A.10 G (1) In order to comply with *MCOB* 4.4A.9R for an internet sale, a *firm* should display the required information on a screen which the *customer* must access as part of the sales process. It would not be sufficient for the information to be accessible only by giving the *customer* the option to click on a link or download a document. The messages could be displayed clearly on one of the initial pages which the *customer* accesses.
- (2) In a postal sale, a *firm* may comply by setting out the messages in a clear covering letter.
- (3) Where the *initial contact* is by email, SMS or instant messaging, the messages could be displayed clearly and prominently early on in the body of the email, SMS or instant messaging.
- (4) For face-to-face and telephone contact, a *firm* should comply by building the messages into the initial oral discussion with the *customer*.
- 4.4A.11 G A *firm* may demonstrate compliance with *MCOB* 4.4A.9R(1) by, for example, undertaking one or more of the following: building a requirement for oral communication of the relevant information into its training of staff as evidenced by its training and compliance manuals; inserting appropriate prompts into paper-based or automated sales systems; and having procedures in place to monitor compliance by staff with that *rule*. What is required in each case will depend on all the circumstances.

#### Timing of initial disclosure in all cases

- 4.4A.12 R The information required by *MCOB* 4.4A.1R, *MCOB* 4.4A.2R, *MCOB* 4.4A.4R(1) and *MCOB* 4.4A.8R must be provided during the course of the *initial contact*.
- 4.4A.13 G (1) In many cases, *MCOB* 4.4A.12R means that information will be 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. The relevant disclosure is only required once this possibility is identified.
- (2) *MCOB* 4.4A.12R does not require a *firm* to provide the information

specified in that *rule* when a *customer* contacts a *firm* simply to arrange to receive services in relation to a *regulated mortgage contract* at a later time, such as when a *customer* books an appointment. In those cases, the initial disclosure should be made when the *firm* first makes contact with the *customer* with a view to actually carrying out the services. 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 is provided in good time (see *MCOB 4.5.3G(1)*).

- 4.4A.14 G *Principle 7* and *MCOB 2.2.6R* also mean that, if initial disclosure has been given but any of the information in it (for example the basis on which the *firm* will be remunerated) subsequently changes, the *firm* should bring this clearly to the *customer's* attention.

Instances where initial disclosure need not be given

- 4.4A.15 R The information requirements in *MCOB 4.4A.1R*, *MCOB 4.4A.2R*, *MCOB 4.4A.4R(1)* and *MCOB 4.4A.8R* do not apply where:
- (1) the information has already been provided by the *firm* and the *firm* has good reason to believe that it is still accurate and appropriate for the *customer*; or
  - (2) the information 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 product range or basis of remuneration described in that information.
- 4.4A.16 G A *mortgage lender* should provide the information in the provisions referred to in *MCOB 4.4A.15R* in a direct sale but need not do so where the sale is through 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 the information as required by this section.

Additional disclosure where initial contact is by telephone

- 4.4A.17 R If the *initial contact* 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 where the services are to be provided to a consumer under a distance contract

- 4.4A.18 R Where a *firm* provides services to a *consumer* by way of a *distance contract*, the *firm* must provide the *consumer* with the following information in a *durable medium* in good time before the *distance contract* has been agreed:
- (1) the information which is required by *MCOB 4.4A.1R* to *MCOB*

4.4A.8R;

- (2) whether or not the *firm* will be providing the *consumer* with *advice*;
- (3) 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*;
- (4) an appropriate statutory status disclosure statement (see *GEN* 4), a statement that the *firm* is on the *FSA Register* and its *FSA* registration number;
- (5) 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;
- (6) the arrangements for payment and for performance;
- (7) 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;
- (8) 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
- (9) any other contractual terms and conditions of the *distance contract*.

4.4A.19 G (1) *MCOB* 4.4A.18R contains the additional disclosure requirements for *firms* providing *mortgage mediation activities* to a *consumer* by way of a *distance contract*. *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*.

- (2) There is *guidance* on *distance contracts* and *consumers* at *MCOB* 1.3.5G and *MCOB* 1.3.6G.

4.4A.20 G If used in accordance with its notes and provided to the *customer* at the correct time, using a *combined initial disclosure document* in a *durable medium* may satisfy the requirements of *MCOB* 4.4A.18R, though *firms* should consider whether it contains all the contractual terms and conditions of the *distance contract*.

Uncertainty whether a mortgage is regulated

4.4A.21 R (1) If at the point that initial disclosure must be made in accordance with *MCOB* 4.4A.1R, *MCOB* 4.4A.2R, *MCOB* 4.4A.4R and *MCOB* 4.4A.8R

a *firm* is uncertain whether the contract will be a *regulated mortgage contract*, the *firm* must:

- (a) make the initial disclosure; 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 must be 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*.

#### Appointed representatives

- 4.4A.22 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* reflects this limited range in any disclosure given to the *customer* under MCOB 4.4A.

#### Record keeping

- 4.4A.23 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.

Amend the following as shown.

#### **4.5 Additional disclosure for distance mortgage mediation contracts, distance home purchase mediation contracts and distance regulated sale and rent back mediation contracts with retail customers**

...

- 4.5.2 R If the ~~initial contact of a kind in MCOB 4.4.1R(1)~~ *initial contact* is with a *consumer* with a view to concluding a *distance mortgage mediation contract*...

After MCOB 4.6 insert the following new section. The text is not underlined.

#### **4.6A Rolling-up of fees or charges into loan**

- 4.6A.1 R A *mortgage lender* may not offer a *regulated mortgage contract* to a *customer* on the basis that fees or charges of any kind (receivable either by the *mortgage lender* or another party) are automatically added to the sum advanced.

- 4.6A.2 R A *firm* must not undertake any action that commits a *customer* to an application for a *regulated mortgage contract* where 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 add the fee or charge to the sum advanced.

MCOB 4.7 is deleted in its entirety and replaced with a new section MCOB 4.7A. The deleted text is not shown and the new text is not underlined.

#### 4.7A Advised sales

- 4.7A.1 G (1) MCOB 4.7A sets out standards to be observed by *firms* when *advising* a particular *customer* on *regulated mortgage contracts*.
- (2) The *rules* at MCOB 4.8A require *firms* which are selling *regulated mortgage contracts* to, or entering into variations of existing *regulated mortgage contracts* with, certain types of vulnerable *customer*, to provide *advice* to them.
- (3) The *rules* at MCOB 4.8A also provide that *advice* must be given wherever the sales process involves spoken or other interactive dialogue (except for *high net worth mortgage customers*, *professional customers* and loans solely for a business purpose). They do not prohibit the giving of pre-contract or preliminary information which does not amount to *advice* to the particular *customer*, but means that *advice* must be given before a *firm enters into* or *arranges a regulated mortgage contract*, or variation of such contract, unless the requirements there are satisfied. *Firms* may wish to refer to *PERG* (particularly *PERG* 4.6) for guidance on the regulatory perimeter in relation to *advising on home finance transactions*.
- (4) The *rules* at MCOB 4.8A provide for an exception which permits certain *execution-only sales* which do not involve additional borrowing.

#### Suitability

- 4.7A.2 R If a *firm* gives *advice* to a particular *customer* to enter into a *regulated mortgage contract*, or to vary an existing *regulated mortgage contract*, it must take reasonable steps to ensure that the *regulated mortgage contract* is, or after the variation will be, suitable for that *customer*.
- 4.7A.3 R In MCOB 4.7A, a reference to *advice* to enter into a *regulated mortgage contract* is to be read as including *advice* to vary an existing *regulated mortgage contract*.
- 4.7A.4 G (1) A *firm* should take reasonable steps to obtain from a *customer* all information likely to be relevant for the purposes of MCOB 4.7A.

- (2) For the purposes of *MCOB 4.7A.2R*, if for any reason a *customer* rejects (in whole or in part) *advice* given by a *firm*, the *firm* is not precluded from advising him to enter into a different *regulated mortgage contract* (in accordance with the requirements of *MCOB 4.7A*) provided the *firm* has taken reasonable steps to ensure that that different contract is suitable for the *customer*.

4.7A.5 R For the purposes of *MCOB 4.7A.2R*:

- (1) a *regulated mortgage contract* will not be suitable for a *customer* unless the *regulated mortgage contract* is appropriate to the needs and circumstances of the *customer*;
- (2) a *firm* must base its determination of whether a *regulated mortgage contract* is appropriate to a *customer's* needs and circumstances on the facts disclosed by the *customer* and other relevant facts about the *customer* of which the *firm* is or should reasonably be aware;
- (3) no *advice* must be given to a *customer* to enter into a *regulated mortgage contract* if there is no *regulated mortgage contract* which is suitable from the product range offered by the *firm*; and
- (4) if a *mortgage lender* is dealing with an existing *customer* with a *payment shortfall* and has concluded that there is no suitable replacement *regulated mortgage contract*, the *firm* must nonetheless have regard to *MCOB 13.3*.

4.7A.6 R When a *firm* assesses whether the *regulated mortgage contract* is appropriate to the needs and circumstances of the *customer* for the purposes of *MCOB 4.7A.5R(1)*, the factors it must consider include the following, insofar as relevant:

- (1) whether the *customer's* requirements appear to be within the *mortgage lender's* known eligibility criteria for the *regulated mortgage contract*;
- (2) whether it is appropriate for the *customer* to have an *interest-only mortgage*, a *repayment mortgage*, or a combination of the two;
- (3) whether it is appropriate for the *customer* to take out a *regulated mortgage contract* for a particular term;
- (4) whether it is appropriate for the *customer* to have stability in the amount of required payments, especially having regard to the impact on the *customer* of significant interest rate changes in the future;
- (5) whether it is appropriate for the *customer* to have their payments minimised at the outset;
- (6) whether it is appropriate for the *customer* to make early

repayments;

- (7) whether it is appropriate for the *customer* to have any other features of a *regulated mortgage contract*;
- (8) whether the *regulated mortgage contract* is appropriate, based on the information provided by the *customer* as to his credit history; and
- (9) whether it is appropriate for the *customer* to pay any fees or charges in relation to the *regulated mortgage contract* up front, rather than adding them to the sum advanced (see also *MCOB 4.6A.2R*).

4.7A.7 G *Firms* are reminded that the list in *MCOB 4.7A.6R* is not exhaustive. For certain *customers* there may be additional considerations to explore beyond those described in that rule; for example, in the case of a business loan or a *regulated mortgage contract* for a *high net worth mortgage customer*.

4.7A.8 G Examples of criteria in *MCOB 4.7A.6R(1)* are: the expected affordability criteria of the *mortgage lender*; and whether the *mortgage lender* will lend in respect of properties of a non-standard construction.

#### Interest-only

4.7A.9 R In relation to *MCOB 4.7A.6R(2)*, where a *firm* has identified an *interest-only mortgage* as appropriate for a *customer*, the *firm* must ensure that the *customer* is aware that he will have to demonstrate to the *mortgage lender* that he will have in place a clearly understood and credible *repayment strategy*, in order for the *mortgage lender* to be able to satisfy *MCOB 11.6.41R(1)*.

4.7A.10 G *MCOB 4.7A.9R* does not require a *firm* to *advise* the *customer* on a credible *repayment strategy* or assess the adequacy of a *customer's* existing *repayment strategy*.

#### Bridging loans

4.7A.11 R When a *firm* assesses whether a *bridging loan* is appropriate to the needs and circumstances of the *customer* for the purposes of *MCOB 4.7A.5R(1)*, the factors it must consider include, in addition to the factors listed at *MCOB 4.7A.6R*:

- (1) whether it is appropriate for the *customer* to make regular payments; and
- (2) whether it is appropriate for the *customer* to access finance quickly.

4.7A.12 R Where a *firm* has identified a *bridging loan* as appropriate for a *customer*, the *firm* must ensure that the *customer* is aware that he will have to demonstrate to the *mortgage lender* that he has a clearly understood and credible *repayment strategy* in place.

- 4.7A.13 R Where a *firm* is considering giving *advice* to a *customer* to enter into a *bridging loan*, the reasonable steps in *MCOB* 4.7A.2R include considering why it is not appropriate for the *customer* to take out a *regulated mortgage contract* which is not a *bridging loan*.
- 4.7A.14 E If a *firm* advises a *customer* to enter into a *regulated mortgage contract* with a term of a particular length so that *MCOB* 4.7A.11R to *MCOB* 4.7A.13R do not apply because the *regulated mortgage contract* does not fall within the definition of a *bridging loan*, that advice may be relied on as tending to show contravention of *MCOB* 2.5A.1R (The customer's best interests).

## Debt consolidation

- 4.7A.15 R When a *firm* advises a *customer* in relation to entering into a *regulated mortgage contract* where the main purpose for doing so is the consolidation of existing debts by the *customer*, in addition to the factors at *MCOB* 4.7A.6R, it must also take account of the following, where relevant, in assessing whether the *regulated mortgage contract* is suitable for the *customer*:
- (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 appropriate for the *customer* to negotiate an arrangement with his creditors rather than to take out a *regulated mortgage contract*.
- 4.7A.16 E An attempt by the *firm* to misdescribe the *customer's* purpose or to encourage the *customer* to tailor the amount he wishes to borrow so that *MCOB* 4.7A.15R does not apply may be relied on as tending to show contravention of *MCOB* 2.5A.1R (The customer's best interests).

## Further advances

- 4.7A.17 R Where the *customer* is looking to increase the borrowing secured on the property which is the subject of an existing *regulated mortgage contract*, unless the *firm* knows that the existing lender will not make a further advance to the *customer*, the *firm* must inform the *customer*, either orally or in writing, that it may be possible, and more appropriate, to do so rather than to enter into a *regulated mortgage contract* with another lender.
- 4.7A.18 G *Firms* are not under any obligation to explore whether a further advance with the existing lender is, in fact, more appropriate for the *customer*.

## Other considerations when advising

- 4.7A.19 R When *advising a customer* on the suitability of a *regulated mortgage contract*, a *firm* must explain to the *customer* that the assessment of whether the *regulated mortgage contract* is appropriate to his needs and circumstances is based only on the *customer's* current circumstances and any reasonably foreseeable changes to those.
- 4.7A.20 G Different considerations apply when giving *advice* to a *customer* with a *payment shortfall*. For example, the circumstances of the *customer* may mean that, viewed as a new transaction, a *customer* should not be advised to enter into a *regulated mortgage contract*. In those cases, a *firm* may still be able to give *advice* to that *customer* where the *regulated mortgage contract* concerned is, in the circumstances, a more suitable one than the *customer's* existing *regulated mortgage contract*.
- 4.7A.21 G In complying with *MCOB 4.7A.5R(1)* 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* may be lower, or both).
- 4.7A.22 G *MCOB 4.7A.5R(3)* means that where the *advice* is not provided on an unlimited range of products from across the relevant market, the assessment of suitability should not be limited to the types of *regulated mortgage contracts* which the *firm* offers. 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. This means, for example, that a *firm* dealing solely in the credit-impaired market should not recommend one of these *regulated mortgage contracts* if approached for *advice* by a *customer* who is not a *credit-impaired customer*.
- 4.7A.23 G A *firm* may generally rely on any information provided by the *customer* for the purposes of *MCOB 4.7A.5R(1)* unless, taking a common sense view of this information, it has reason to doubt it.

#### Rejected advice

- 4.7A.24 R If a *customer* has rejected the *advice* given by a *firm* and instead wishes to enter into a different *regulated mortgage contract* as an *execution-only sale*, the *firm* may *enter into* or *arrange* that contract as an *execution-only sale* provided the requirements in *MCOB 4.8A.14R* are satisfied.

#### Record keeping

- 4.7A.25 R (1) A *firm* must make and retain a record:
- (a) of the *customer* information, including that relating to the *customer's* needs and circumstances, that it has obtained for the purposes of *MCOB 4.7A*;
  - (b) that explains why the *firm* has concluded that any *advice* given to a *customer* complies with *MCOB 4.7A.2R* and satisfies the suitability requirement in *MCOB 4.7A.5(1)R*; and
  - (c) of the *customer's* positive choice in *MCOB 4.6A.2R* (Rolling up of fees or charges into loan) where applicable.
- (2) The records in (1) must be retained for a minimum of three years from the date on which the *advice* was given or, in the case of (1) (d), the making of the choice.

*MCOB 4.8* is deleted in its entirety and replaced with a new section *MCOB 4.8A*. The deleted text is not shown and the new text is not underlined.

#### **4.8A Execution-only sales**

Scope and application of this section

- 4.8A.1 G This section sets out the conditions which must be satisfied for a *firm* to enter into or vary a *regulated mortgage contract* with a *customer*, or arrange such a transaction for a *customer*, without giving *advice*, or where the *advice* given by the *firm* has been rejected. As explained in *MCOB 4.7A.1G*, it does not prohibit the giving of pre-contract or preliminary information which does not amount to *advice* to the particular *customer*. If a *firm* intends (where permitted under this section) to operate a business model under which it will not give *advice* to particular *customers*, it may wish to refer to *PERG* (particularly *PERG 4.6*) for guidance on the regulatory perimeter in relation to the *regulated activities* which constitute *advising on home finance transactions*.
- 4.8A.2 G Subject to certain limited exceptions, where the *rules* in *MCOB 4.8A* apply to a *firm* they restrict *execution-only sales* (which term is defined to include variations of existing contracts) to cases where:
- (1) there is no spoken or other interactive dialogue between the *firm* and the *customer* during the sale; or
  - (2) if there is spoken or other interactive dialogue between the *firm* and the *customer* during the sale:
    - (a) the *customer* is a *high net worth mortgage customer*; or

- (b) the *customer* is a *professional customer*; or
- (c) the loan is solely for a business purpose;

and in each case the *customer* has positively elected to proceed with an *execution-only sale* and (in the case of a *professional customer*) identified the product he wishes to purchase; or

- (3) the *customer* has rejected *advice*, identified the product he wishes to purchase and positively elected to proceed with an *execution-only sale*.

In each case certain requirements must be satisfied.

- 4.8A.3 G Interactive dialogue includes SMS, mobile instant messaging, email and communication via social media sites; this list is not exhaustive. Where a sale is carried out entirely on the internet, a *firm* merely permitting the *customer* to input details about the matters specified in *MCOB* 4.8A.14R(1), (2) or (3) in order to select from the *firm's* product range the *regulated mortgage contract* he wishes to purchase, or the variation he wishes to enter into, would not be engaging in interactive dialogue. *Firms* are reminded that, if this process steers the *customer* towards any one or more of the products offered by it, so as to constitute *advice*, the requirements of *MCOB* 4.7A will apply.

The customer's best interests

- 4.8A.4 G *Firms* are reminded that *MCOB* 2.5A.1R (The customer's best interests) applies in all cases, including in relation to *execution-only sales*.
- 4.8A.5 R A *firm* must not encourage a *customer* to opt out of receiving *advice* on *regulated mortgage contracts* from, or reject *advice* given by, it or any *associate*.
- 4.8A.6 G *Firms* are not prohibited from *entering into* or *arranging execution-only sales* for *regulated mortgage contracts* for *customers* to whom they have provided product information (where otherwise permitted under this section), but *MCOB* 2.5A.1R and *MCOB* 4.8A.5R (The customer's best interests) mean the information they provide should not steer the *customer* to elect to enter into an *execution-only sale*.

Cases where execution-only sales are not permitted

- 4.8A.7 R A *firm* must not enter into or arrange an *execution-only sale* for a *regulated mortgage contract* if:
- (1) the *customer* is intending to use it to exercise a statutory "right to buy" the *customer's* home; or
  - (2) the main purpose of the *customer's* entering into it is to raise funds for debt consolidation; or

- (3) there is spoken or other interactive dialogue between the *firm* and the *customer* at any point during the sale.

4.8A.8 E An attempt by the *firm* either to:

- (1) misdescribe the *customer's* purpose or characteristics; or  
 (2) encourage the *customer* to tailor the amount he wishes to borrow;

so that *MCOB* 4.8A.7R does not apply may be relied on as tending to show contravention of *MCOB* 2.5A.1R (The customer's best interests).

Exceptions: high net worth mortgage customers, professional customers and loans solely for a business purpose.

4.8A.9 R (1) *MCOB* 4.8A.7R does not apply where the *customer* is a *high net worth mortgage customer*.

- (2) *MCOB* 4.8A.7R(3) does not apply where the *customer* is a *professional customer* or the loan is solely for a business purpose.

Exception: rate switches and other variations

4.8A.10 R (1) *MCOB* 4.8A.7R does not apply in the case of a variation of a *regulated mortgage contract*, provided that:

- (a) the variation would not involve the *customer* taking on additional borrowing beyond the amount currently outstanding under the existing *regulated mortgage contract*, other than to finance any product fee or arrangement fee for the proposed new or varied contract; and

- (b) where the variation will (in whole or part) change from one interest rate to another, the *firm* has presented to the *customer*, using only a non-interactive channel, all products offered by it for which the *customer* is eligible, whether or not the *customer* then selects from those products using an interactive channel.

- (2) The reference to a variation in (1) (and in all other provisions which cross-refer to this *rule*) must be read as including any new *regulated mortgage contract* which would replace an existing *regulated mortgage contract* between the *customer* (or, where there are joint borrowers, at least one of them) and the *firm* (either as the original *mortgage lender* or as the transferee of the existing contract).

4.8A.11 G (1) The variation in *MCOB* 4.8A.10R might involve: a transfer to a different property ("porting"); the addition or removal of a borrower for joint mortgages; an extension of the term; a change in payment method; or consent to let the property. This list is not exhaustive.

- (2) Examples of rate changes in *MCOB* 4.8A.10R(1)(b) are: a transfer

from a variable rate to a fixed rate; and a transfer from one fixed rate to another fixed rate.

- (3) *Firms* are reminded that, if their presentation in *MCOB* 4.8A.10R(1)(b) has (either explicitly or implicitly) steered the *customer* towards any one or more of the products offered by them such as to constitute *advice*, the requirements of *MCOB* 4.7A will apply.

Exception: rejected advice

- 4.8A.12 R *MCOB* 4.8A.7R does not apply where the *customer* has rejected *advice* given by a *firm* and instead wishes to enter into a different *regulated mortgage contract* as an *execution-only sale* (see *MCOB* 4.8A.14R).

Execution-only sales: guidance

- 4.8A.13 G (1) If a *firm* wishes to be able to apply the exception in *MCOB* 4.8A.9R for a *high net worth mortgage customer*, it should first consider the provision in *MCOB* 1.2.9CR (Requirement for evidence before treating a loan as being solely for business purposes, or a customer as a high net worth mortgage customer or a professional customer).
- (2) Where a *firm's* business model is such that it does not offer *advice on regulated mortgage contracts* to particular *customers*, it should ensure that it does not *enter into* or *arrange regulated mortgage contracts* for *customers* in breach of *MCOB* 4.8A.7R. Such a *firm* may wish to use filtering questions which the *customer* is required to answer before he is able to proceed, in order to establish whether any of the exceptions to *MCOB* 4.8A.7R apply.

Requirements for execution-only sales

- 4.8A.14 R A *firm* must not *enter into* or *arrange* an *execution-only sale* for a *regulated mortgage contract* unless, except as provided in *MCOB* 4.8A.15R:
- (1) for a new *regulated mortgage contract* not falling within *MCOB* 4.8A.10R, the *customer* has identified the *regulated mortgage contract* he wishes to purchase, specifying to the *firm* at least the following information:
- (a) the name of the *mortgage lender*;
- (b) the rate of interest;
- (c) the interest rate type (that is, whether fixed, variable or some other type);
- (d) the price or value of the property on which the *regulated mortgage contract* would be secured (estimated where

- necessary);
- (e) the length of the term required by the *customer*;
  - (f) the sum the *customer* wishes to borrow; and
  - (g) whether the *customer* wants an *interest-only mortgage* or a *repayment mortgage*;
- (2) for a contract variation not falling within *MCOB* 4.8A.10R (but permitted by *MCOB* 4.8A.7R), the *customer* has specified at least the following information, where applicable to the variation he wishes to enter into:
- (a) the price or value of the property;
  - (b) the length of term required (or confirmation that this should remain unchanged); and
  - (c) the amount the *customer* wishes to borrow;
- (3) for a contract variation falling within *MCOB* 4.8A.10R, the *customer* has specified the variation he wishes to enter into;
- (4) the *customer* has been informed, clearly and prominently and in a *durable medium* (after providing the information in (1), (2), or (3), where that is required):
- (a) in any case falling within *MCOB* 4A.7A.24 R (Rejected advice) where the *firm* has advised the *customer* that the *regulated mortgage contract* (or variation) is unsuitable for the *customer*, that that is the case; or
  - (b) in any other case, that in the provision of its services for the *execution-only sale* the *firm* is not required to assess the suitability of that *regulated mortgage contract* (or variation);

and in either case that the *customer* will not benefit from the protection of the rules (in *MCOB* 4.7A) on assessing suitability. In any case where there is spoken dialogue between the *firm* and the *customer* at any point during the sale, the *firm* must also provide this information orally; and

- (5) once the *customer* has been provided with the information in (4), in any case where there is spoken or other interactive dialogue between the *firm* and the *customer* at any point during the sale, he has confirmed, in writing, to the *firm* that he is aware of the consequences of losing the protections of the *rules* on assessing suitability and is making a positive election to proceed with an *execution-only sale*. The written confirmation must be in the same document as the information in *durable medium* in (4), which must be separate from any other information or contractual

documentation.

- 4.8A.15 R The requirements in *MCOB* 4.8A.14R(1) to (3) do not apply if the *customer* is a *high net worth mortgage customer* or entering into the *regulated mortgage contract* solely for a business purpose.
- 4.8A.16 G Where the information in *MCOB* 4.8A.14R(4) is given by electronic means, the *firm* should ensure that the *customer* cannot progress to the next stage of the sale unless the information has been communicated to the *customer*.

#### Managing execution-only sales

- 4.8A.17 R A *firm* which intends to transact *execution-only sales* in *regulated mortgage contracts* must have in place and operate in accordance with a clearly defined policy which:
- (1) sets out the amount of business the *firm* reasonably expects to transact by way of *execution-only sales* and the steps to be taken by the *firm* if that business exceeds the expected levels; and
  - (2) sets out its processes and procedures for ensuring compliance with the *rules* in *MCOB* 4.8A; in particular:
    - (a) how it will ensure in every case that, before proceeding with an *execution-only sale* it has obtained (where required) a voluntary and informed positive election from the *customer* in order to comply with *MCOB* 4.8A.14R(5);
    - (b) how it will ensure in every case that it acts in compliance with *MCOB* 2.5A.1R and *MCOB* 4.8A.5R (The customer's best interests), including not encouraging a *customer* to enter into a *regulated mortgage contract* (or variation) as an *execution-only sale*; and
    - (c) how it will identify whether a *customer* meets the definition of *high net worth mortgage customer* or *professional customer*, if it will offer *execution-only sales* to those *customers*; and
  - (3) includes the arrangements for monitoring and auditing compliance with the policy, processes and procedures.

#### Record keeping

- 4.8A.18 R (1) Whenever a *firm* enters into or arranges an *execution-only sale* for a *regulated mortgage contract*, it must make and maintain a record of:
- (a) the information provided by the *customer* which satisfies *MCOB* 4.8A.14R(1), (2) or (3);

- (b) the information in *durable medium* in MCOB 4.8A.14R(4);
  - (c) (where applicable) the confirmation by the *customer* in MCOB 4.8A.14R(5); and
  - (d) any *advice* from the *firm* which the *customer* rejected, including the reasons why it was rejected, before deciding to enter into an *execution-only sale*.
- (2) The record in (1) must be retained for a minimum of three years from the date on which the *regulated mortgage contract* was *entered into* or *arranged* (or the variation was entered into or arranged).
  - (3) A *firm* must keep an adequate and up-to-date record of the policy in MCOB 4.8A.17R, where such policy is required by that *rule*. When the policy is changed, a record of the previous policy must be retained for one year from the date of change.

#### Forbearance

- 4.8A.19 R MCOB 4.8A does not apply to any variation which is made solely for the purposes of forbearance where the *customer* has a *payment shortfall*, or in order to avoid a *payment shortfall*.

Amend the following as shown.

#### **4.9 Business loans and loans to high net worth mortgage customers: tailored provisions**

- 4.9.1 R ~~For the purposes of the rules in MCOB there is one market in regulated mortgage contracts for a business purpose. Within this market, a firm should describe its scope of service in accordance with MCOB 4.3.1R. [deleted]~~
- 4.9.1A G Firms are reminded that in accordance with MCOB 1.2.3R and MCOB 1.2.3AR, they should either comply in full with MCOB, but in doing so may opt to take account of or comply with all tailored provisions in MCOB that relate to business loans or loans to high net worth mortgage customers, as the case may be. Therefore, a firm may only follow the tailored provisions in MCOB 4.9 in relation to one of these sectors if it also follows all other tailored provisions in MCOB that relate to that sector. In either case, the rest of MCOB applies in full.
- 4.9.2 G ~~Where a personal recommendation or personalised information is provided in connection with a regulated mortgage contract for a business purpose it is recognised that there may be additional considerations beyond those described in MCOB 4.7.11E as part of the assessment of whether the regulated mortgage contract is appropriate to the needs and circumstances~~

of the *customer*. [deleted]

#### Initial disclosure

- 4.9.3 G ~~As explained in *MCOB 4.4.3G(1)* the requirement to provide an initial disclosure document is only triggered where the *firm* has identified the possibility that it will be giving personalised information or *advice* to a *customer* on a *regulated mortgage contract* for a business purpose. [deleted]~~
- 4.9.4 G (1) *Firms* are reminded that *MCOB 1.2.7R* enables them to substitute an alternative for 'mortgage' in the initial disclosure document in relation to a *regulated mortgage contract* for a business purpose or a *high net worth mortgage customer* (except in relation to sections 6 and 8 of any *initial disclosure document* or sections 5 and 8 of any *combined initial disclosure document*).
- (2) *MCOB 1.2.7R* also means that a *firm* ~~must~~ should amend any *combined initial disclosure document* in relation to a *regulated mortgage contract* for a business purpose or a *high net worth mortgage customer* so that the final sentence of prescribed text in section 4 states: 'You will receive an illustration which will tell you about any fees relating to a particular [term used by the firm to describe the borrowing, for example "mortgage secured overdraft"]'.
- (3) Where the initial disclosure ~~document~~ in relation to a *regulated mortgage contract* for a business purpose or a *high net worth mortgage customer* makes reference to the permitted business of a *firm* (for example, sections 6 5 and 8 of the ~~initial disclosure document~~ *combined initial disclosure document* may refer to a *firm* *advising on or arranging regulated mortgage contracts*) a *firm* can add text explaining the relevance of these descriptions. One approach may be to add an additional sentence such as: 'Secured overdrafts are referred to here as "mortgages" because they involve a charge being taken over your property'.

#### Non-advised sales

- 4.9.5 R ~~*MCOB 4.8.1R* does not apply in relation to a *regulated mortgage contract* for a business purpose. [deleted]~~

...

### 4.10 Home purchase plans: sales standards

#### Scope of service provided

- 4.10.1 R ~~A *firm* must comply with the scope of service requirements at *MCOB 4.3.1R* and *MCOB 4.3.2R* (Providing services within and beyond scope), *MCOB 4.3.4A R* and *4.3.4AR* (Whole of market and *MCOB 4.3.10R* (Appointed representatives)). [deleted]~~

## Initial disclosure requirements

- 4.10.2 R (1) ~~A firm must, on first making contact with a customer when it anticipates giving personalised information or advice on entering into a new home purchase plan, ensure that the customer is, or has been, provided with an appropriate initial disclosure document or combined initial disclosure document in a durable medium.~~
- (2) ~~If the initial contact in (1) is by telephone, a firm must:~~
- (a) ~~(if the call is with a view to concluding a distance home purchase mediation contract) give the following information before proceeding further:~~
- (i) ~~the name of the firm and (if initiated by the firm) the commercial purpose of the call;~~
- (ii) ~~the scope of the service provided by the firm; and~~
- (iii) ~~whether or not the firm will provide the customer with advice on those home purchase plans within its scope; and~~
- (b) ~~Ensure that the customer is, or has been, provided with such a document in a durable medium as soon as is practicable.~~
- (3) ~~A firm must not use a combined initial disclosure document in relation to a combination of home purchase plans and equity release transactions. [deleted]~~
- 4.10.3 G ~~In accordance with Principle 7, where a firm is likely to provide services in relation to both regulated mortgage contracts and home purchase plans, it should provide a combined initial disclosure document rather than two separate initial disclosure documents. [deleted]~~
- 4.10.3A R A firm must comply with the rules in MCOB 4.4A as if the references in those rules to regulated mortgage contracts and mortgage lenders were to, respectively, home purchase plans and home purchase providers.
- 4.10.3B R For the purposes of MCOB 4.4A.2R(1) there is one relevant market for home purchase plans.
- 4.10.4 G ~~The guidance on initial disclosure requirements at MCOB 4.4.2G to MCOB 4.4.4G in MCOB 4.4A may be relevant; in this context, that guidance should be read using home purchase plan terminology instead of the equivalent regulated mortgage contract terminology, where appropriate.~~

**Additional requirements for distance home purchase mediation contracts with retail customers**

[Note: The rules regarding additional disclosure requirements for, and

cancellation of, *distance home purchase mediation contracts* are set out in *MCOB 4.5* and *MCOB 4.6* respectively.]

Advised sales: suitability

- 4.10.5 G ~~In accordance with *Principle 9*, a firm should take reasonable steps to obtain from a *customer* all information likely to be relevant to ensuring the suitability of its advice. [deleted]~~
- 4.10.5A R If a firm gives advice to a particular customer to enter into a home purchase plan, or to vary an existing home purchase plan, it must take reasonable steps to ensure that the home purchase plan is, or after the variation will be, suitable for that customer.
- 4.10.5B R In MCOB 4.10, a reference to advice to enter into a home purchase plan is to be read as including advice to vary an existing home purchase plan.
- 4.10.5C G A firm should take reasonable steps to obtain from a customer all information likely to be relevant for the purposes of MCOB 4.10.5AR to MCOB 4.10.9AR.
- 4.10.5D R For the purposes of MCOB 4.10.5AR:
- (1) a home purchase plan will not be suitable for a customer unless the home purchase plan is appropriate to the needs and circumstances of the customer;
  - (2) a firm must base its determination of whether a home purchase plan is appropriate to a customer's needs and circumstances on the facts disclosed by the customer and other relevant facts about the customer of which the firm is or should reasonably be aware;
  - (3) no advice must be given to a customer to enter into a home purchase plan if there is no home purchase plan which is suitable from the product range offered by the firm;
  - (4) if a home purchase provider is dealing with an existing customer in arrears, with a payment shortfall or otherwise in breach of their home purchase plan and has concluded that there is no suitable replacement home purchase plan, the firm must nonetheless have regard to MCOB 13.3; and
  - (5) the reasonable steps in that rule include considering why it is not appropriate for the customer to take out a regulated mortgage contract.
- 4.10.6 R ~~A firm, before making a personal recommendation on a home purchase plan, must take reasonable steps to ensure that it is:~~
- (1) affordable;

- (2) ~~appropriate to the *customer's* needs and circumstances; and~~
- (3) ~~the most suitable of those *home purchase plans* that the *firm* has available to it within the scope of the service provided to the *customer*.  
[deleted]~~

4.10.6A G *MCOB 4.10.5DR(3) has the effect that a firm cannot recommend the 'least worst' home purchase plan where the firm does not have access to home purchase plan products appropriate to the customer's needs and circumstances.*

4.10.7 G ~~The guidance on suitability at *MCOB 4.7.8G* to *MCOB 4.7.10G* and *MCOB 4.7.16G* may be relevant. *Firms may wish to consider the following provisions:*~~

- (1) *the rule at *MCOB 4.7A.6R* on the customer's needs and circumstances, as if it were guidance and to the extent applicable to home purchase plans; and*
- (2) *the guidance at *MCOB 4.7A.1G(2)*, *MCOB 4.7A.21G* and *MCOB 4.7A.23G* (Other considerations when advising);*

*in each case using home purchase plan terminology instead of the equivalent regulated mortgage contract terminology, where appropriate.*

#### Non-advised sales

4.10.8 R ~~If a *firm* arranges a *home purchase plan* or a variation to an existing *home purchase plan* without giving a *personal recommendation*, it must ensure that the questions it asks about the *customer's* needs and circumstances are scripted in advance. [deleted]~~

4.10.9 G ~~The guidance on non-advised sales at *MCOB 4.8.2G* and on scripted questions at *MCOB 4.8.5G* and *MCOB 4.8.6G* may be relevant. [deleted]~~

#### Rejected recommendations

4.10.9A R *If a customer has rejected the advice given by a firm and instead requested an execution-only sale of a home purchase plan, the firm may enter into or arrange that execution-only sale provided the requirements in *MCOB 4.8A.14R* (as applied in relation to home purchase plans by *MCOB 4.10.9BR* and modified for home purchase plans by *MCOB 4.10.9DR*) are satisfied.*

#### Execution-only sales

4.10.9B R *MCOB 4.8A* applies to a *firm* as if the references in that section to *regulated mortgage contracts* and *mortgage lenders* were to, respectively, *home purchase plans* and *home purchase providers*, but *MCOB 4.8A.14R(1)* and *(2)* are modified in relation to *home purchase plans* as set out in *MCOB 4.10.9DR*.

4.10.9C G As provided in MCOB 4.1.2BR, MCOB 4.8A only applies to home purchase providers in relation to entering into home purchase plans where there is no firm which is arranging the transaction and to which MCOB 4.8A applies.

4.10.9D R For home purchase plans, the following items of information replace those set out in MCOB 4.8A.14R(1) and (2):

- (1) the name of the home purchase provider;
- (2) the length of the term required by the customer; and
- (3) the sum required from the home purchase provider.

#### Risks and features statement and tariff of charges

4.10.10 R A firm must, before ~~making a personal recommendation to~~ advising a customer of, ~~or when a customer requests or selects,~~ to enter into, or entering into or arranging a home purchase plan as an execution-only sale, ensure that the customer is, or has been, provided with an appropriate risks and features statement about that plan.

...

#### Record keeping

4.10.13 R (1) A firm must make and retain a record:

- (a) of the customer information, including that relating to the customer's needs and circumstances that it has obtained for the purposes of MCOB 4.10.5DR;
- (b) that explains why the firm has concluded that any advice given to a customer complies with MCOB 4.10.5AR and satisfies the suitability requirement in MCOB 4.10.5DR(1); and
- (c) of any advice which the customer has rejected, including the reasons why it was rejected and details of the home purchase plan which the customer has proceeded with as an execution-only sale.

(2) The records in (1) must be retained for a minimum of three years from the date on which the advice was given.

4.10.14 G Firms should note the record-keeping requirements in MCOB 4.8A in relation to execution-only sales which are imposed in relation to home purchase plans by MCOB 4.10.9BR.

## **4.11 Sale and rent back: advising and selling standards**

## Initial disclosure requirements

- 4.11.1 R (1) ~~A regulated sale and rent back firm, on first making contact with a potential SRB agreement seller for whom it might reasonably be expected to carry on any regulated sale and rent back activity, must make the following disclosures to him a customer, both orally and in writing, during the initial contact:~~

...

Affordability and appropriateness Advised sales

- 4.11.3 R ~~A regulated sale and rent back firm must not permit a potential SRB agreement seller to become contractually committed to enter into a regulated sale and rent back agreement unless it has reasonable grounds to be satisfied that: a firm with permission to advise on regulated sale and rent back agreements has advised the particular customer to enter into it.~~
- (1) ~~the customer can afford the payments he will be liable to make under the agreement; and~~
- (2) ~~the proposed regulated sale and rent back agreement is appropriate to the needs, objectives and circumstances of the customer.~~

Suitability

- 4.11.3A R A firm must take reasonable steps to ensure that it does not advise a particular customer to enter into a regulated sale and rent back agreement unless the regulated sale and rent back agreement is suitable for that customer.
- 4.11.3B G A firm should take reasonable steps to obtain from a customer all information likely to be relevant for the purposes of MCOB 4.11.3AR.
- 4.11.3C R For the purposes of MCOB 4.11.3AR:
- (1) a regulated sale and rent back agreement will not be suitable unless, having regard to the facts disclosed by the customer and other relevant facts about the customer of which the firm is or should reasonably be aware, the firm concludes on reasonable grounds that:
- (a) the customer can afford the payments he will be liable to make under it; and
- (b) the proposed regulated sale and rent back agreement is appropriate to the needs and circumstances of the customer;
- (2) a firm must base its determination of whether a customer can afford the payments he will be liable to make under a regulated sale and rent back agreement, and whether it is appropriate to his needs and circumstances, on the facts disclosed by the customer and other

relevant facts about the *customer* of which the *firm* is or should reasonably be aware;

- (3) no advice must be given to a *customer* to enter into a *regulated sale and rent back agreement* if there is no *regulated sale and rent back agreement* which is suitable from within the product range offered by the *firm*.

- 4.11.4 E (1) In assessing whether a *customer* can afford to enter into a particular *regulated sale and rent back agreement*, a *firm* should use the following information:
- (a) the rental payments that will be due under the tenancy agreement which confers the right of the *customer* (or trust beneficiary or related party) to continue residing in the property, stress tested to take account of possible future rental increases during the fixed term of the tenancy agreement by reference to the circumstances in which the agreement permits increases or changes to the initial rent;
  - (b) adequate information, obtained from the *customer* to establish his average income and expenditure calculated on a monthly basis, and any other resources that he has available, and verified by the *firm* using evidence provided by the *customer*;
  - (c) the *customer's* net disposable income, which a *firm* should establish using the information referred to in (b);
  - (d) the *customer's* entitlement to means-tested benefits and housing benefits; and
  - (e) the effect of any likely future change to the *customer's* income, expenditure or resources during the period of the *regulated sale and rent back agreement*.
- (2) The *firm* should explain to the *customer* that it will base its assessment on whether he can afford to enter into the particular *regulated sale and rent back agreement* on the information he provides to the *firm* about his income, expenditure and resources.
- (3) In assessing affordability under (1) the *firm*:
- (a) must not rely to a material extent on the capital of, or income from, any lump sum the *customer* receives which represents the net sale proceeds of the property; and
  - (b) must disregard any discount or any future sum that may be payable to the *customer* under the terms of the *regulated sale and rent back agreement*.
- (4) Contravention of (1), (2) or (3) may be relied upon as tending to show

contravention of *MCOB 4.11.3CR(1)(a)*.

4.11.4A     R     In assessing whether the *regulated sale and rent back agreement* is appropriate to the needs and circumstances of the *customer* for the purposes of *MCOB 4.11.3C R(1) (b)*, as a minimum requirement a *firm* must consider the following list of factors:

- (1) whether it is appropriate for the *customer* to sell his property for a price less than its value (as determined by the valuation which is required by *MCOB 6.9.2R*, including where applicable a valuation obtained by the *SRB agreement seller* as described in *MCOB 6.9.2R (4)*) (where this is proposed under the *regulated sale and rent back agreement*);
- (2) whether it is appropriate for the *customer* because he is in financial difficulty;
- (3) whether all other options have been explored and eliminated, including the *customer* speaking to his *home finance provider* and other creditors, getting debt advice, releasing the equity by other means and checking whether he is eligible for government or local authority help;
- (4) whether it would be more appropriate for the *customer* to sell his home on the open market;
- (5) whether the benefits to the *customer* in entering into the proposed *regulated sale and rent back agreement* outweigh any adverse effects it may have for him, including on his entitlement to means-tested benefits and housing benefits;
- (6) the feasibility of the *customer* raising funds by alternative methods other than by a sale of his property; and
- (7) if the *customer* is not under threat of repossession, why it is appropriate for the *customer* to take out a *regulated sale and rent back agreement* rather than to use an alternative method of finance.

4.11.4B     E     The following may be relied on as tending to show contravention of *MCOB 2.5A.1R* (The customer's best interests):

- (1) an attempt by the *firm* to misdescribe the *customer's* reasons for considering a *regulated sale and rent back agreement*; or
- (2) an attempt to encourage a *customer* to enter into a *regulated sale and rent back agreement* involving a sale price for his property which is less than its value (as determined by the valuation which is required by *MCOB 6.9.2R*, including where applicable a valuation obtained by the *SRB agreement seller* as described in *MCOB 6.9.2R(4)*) if he is not under threat of repossession.

4.11.4C G Firms are reminded that the list in MCOB 4.11.4AR is not exhaustive. For certain customers there may be additional considerations to explore beyond those described in that rule.

4.11.5 E (1) ~~In assessing whether a particular regulated sale and rent back agreement is appropriate to the needs, objectives and circumstances of a potential SRB agreement seller, a firm should have due regard to the following:~~

(a) ~~whether the benefits to the customer in entering into the proposed regulated sale and rent back agreement outweigh any adverse effects it may have for him, including on his entitlement to means tested benefits and housing benefits; and~~

(b) ~~the feasibility of the customer raising funds by alternative methods other than by a sale of his property.~~

(2) ~~Contravention of (1) may be relied upon as tending to show contravention of MCOB 4.11.3R(2). [deleted]~~

...

4.11.7 G

...

(2) The firm should consider whether a customer ~~in arrears~~ with a payment shortfall under his regulated mortgage contract or home purchase plan has contacted his mortgage lender or home purchase provider to discuss possible forbearance options that may be available. Other possible alternative methods of raising funds will include the availability of local authority or other government rescue schemes that may apply in the customer's circumstances.

...

#### Record keeping

4.11.8 R (1) A firm must make and retain a record of the customer information that has been provided to it, including that relating to:

(a) the customer's income, expenditure and other resources that it has obtained from him for the purpose of assessing affordability, together with the stress testing of the rental payments;

(b) the customer's needs and individual circumstances that it has obtained from him for the purpose of assessing appropriateness; and

(c) the customer's entitlement to means-tested benefits and housing benefits, including any evidence provided by the customer, that

it has obtained from him for the affordability and appropriateness assessment;

and which explains why the *firm* concluded that the regulated sale and rent back agreement was suitable for the customer could afford, and why it was appropriate for him, and why it advised him to enter into the proposed regulated sale and rent back agreement it.

- (2) The record in (1) must be retained for a minimum of five years from the date on which the assessment of ~~affordability and appropriateness suitability~~ was made, or one year after the end of the fixed term of the tenancy agreement under the *regulated sale and rent back agreement*, if later.

#### Reliance on another firm

- 4.11.9 R A *firm* need not comply with the requirements imposed on a *regulated sale and rent back firm* in this section to the extent that it is satisfied on reasonable grounds that another *firm*, with the appropriate permission to do so, has already done so.
- 4.11.10 G The effect of *MCOB* 4.11.9R is that a *SRB agreement provider* is expected to ~~carry out its own assessments of affordability and appropriateness~~ advise in relation to a particular *regulated sale and rent back agreement*, unless it is reasonable for it to rely on another *firm* with permission to advise on regulated sale and rent back agreements, to have done so in relation to a particular transaction.

The following Annex is deleted in its entirety. The deleted text is not struck through.

#### **4 Annex 1R Initial disclosure document** [deleted]

Amend the following as shown.

### **5.1 Application**

...

What?

- 5.1.3 R (1) This chapter applies if a *firm*:
- (a) ~~makes a personal recommendation to~~ advises a particular customer to enter into, or arranges an execution-only sale in, a home finance transaction; or
- (b) provides information to a *customer* that is specific to the

amount to be provided on a particular *home finance transaction*, including information provided in response to a request from a *customer*; or

- (c) provides the means for a *customer* to make an application to it;

in connection with entering into, or agreeing to enter into, a *home finance transaction* provided by a *home finance provider*, other than an *equity release transaction* or a variation to an existing *home finance transaction*.

...

## 5.2 Purpose

5.2.1 G ...

- (2) The purpose of *MCOB 5* is to ensure that, before a *customer* submits an application for a particular *home finance transaction*, he is supplied with information that makes clear:
- (a) (in relation to a *regulated mortgage contract*) its features, any *linked deposits*, any *linked borrowing* and any *tied products*; and
- (b) the price that the *customer* will be required to pay under that *home finance transaction*, to enable the *customer* to assess whether it is affordable to him make a well-informed purchasing decision.

...

## 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 the information must be clear, fair and not misleading in accordance with Principle 7 and MCOB 2.2.6R; and must be given in accordance with MCOB 2.5A.1R (The customer's best interests).
- 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 5.4.13R 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 5.4.13R(2) or MCOB 5.4.13R(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.~~
- (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    (1)    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 4.7A.2R*, it must give, clearly and prominently, the following information:
- (a)    the same information on the *firm's* product range as is required by *MCOB 4.4A.1R(1)*, *MCOB 4.4A.2R* and *MCOB 4.4A.4R(1)*; and
- (b)    that the *customer* has the right to request an *illustration* for any *regulated mortgage contract* which the *firm* is able to offer the *customer*.
- (2)    A *firm* need not give the information in (1) if it has previously given that information in compliance with this *rule* within the last ten *business days*.

Message to be given when customer requests an execution-only sale

- 5.4.18B    R    (1)    Whenever, as part of an *execution-only sale* (or potential *execution-only sale*), a *customer* provides a *firm* with the information in *MCOB 4.8A.14R(1)*, (2) or (3) the *firm* must inform the *customer*, clearly and prominently, that the *customer* has the right to request an *illustration* for any *regulated mortgage contract* which the *firm* is able to offer the *customer*.
- (2)    Whenever, as part of an *execution-only sale* (or potential *execution-only sale*), a *high net worth mortgage customer* or *customer* who would be entering into a *regulated mortgage contract* solely for a business purpose is provided with information specific to the amount that the *customer* wants to borrow on a particular *regulated mortgage contract*, the *firm* must inform the *customer*, clearly and prominently, that the *customer* has the right to request an *illustration* for any *regulated mortgage contract* which the *firm* is able to offer the *customer*.
- (3)    A *firm* need not give the information in (1) and (2) if it has previously given that information in compliance with this *rule* within the last ten *business days*.

Guidance relevant to messages given to customer

- 5.4.18C    G    (1)    In order to demonstrate compliance with *MCOB 5.4.18AR(1)*, a *firm* may wish to consider, for example, doing one or more of the following: give the messages to the *customer* in a durable medium; build the requirements into the *firm's* training of staff, as evidenced by its training and compliance manuals; insert appropriate prompts into paper-based or automated sales systems; have procedures in place to monitor compliance by its staff with that *rule*. What is required in

each case will depend on all the circumstances.

- (2) 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 obligations in MCOB 5.4.18AR(1)(b) and MCOB 5.4.18BR. A firm may, however, satisfy those obligations 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.

...

Tied products

...

- 5.4.24 G The rules on the content of an *illustration* at MCOB 5.6 (Content of illustrations) mean that if the *regulated mortgage contract* requires the *customer* to take out a *tied product*, the *illustration* must include an accurate quotation or a reasonable estimate of the payments the *customer* would need to make for the *tied product* (see MCOB 5.6.52R(2) ~~on where the *tied product* is a repayment vehicle strategy that is a *tied product* and MCOB 5.6.74R ~~on insurance that is a~~ where the *tied product* is insurance)...~~

...

## 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) ~~A~~ 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~~ *advises* the particular *customer* in relation to enter into one or more that *regulated mortgage contracts*, in which case an *illustration* must be provided at the point the ~~recommendation~~ advice is made given (and ~~illustrations for all recommended *regulated mortgage contracts* must be provided~~), unless the *advice* is given by telephone, in which case the *firm* must provide an *illustration* within 5 business days; or

- (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* for that regulated mortgage contract, unless the *firm* is aware that it is unable to offer that regulated mortgage contract to him; or~~
  - (e) ~~as part of an *execution-only sale* (or potential *execution-only sale*) the *customer* has provided the *firm* with the information in MCOB 4.8A.14R(1) to (3) to indicate which regulated mortgage contract or variation he wishes to enter into; or~~
  - (f) ~~as part of an *execution-only sale* (or potential *execution-only sale*), a *high net worth mortgage customer* or a *customer* who is entering into the regulated mortgage contract solely for a business purpose, has indicated his intention to submit an application for that 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 *direct deal*;
  - (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; or
  - (3)    if the *firm* does not wish to do business with the *customer*.
- 5.5.1B    R    If the *firm* chooses not to give an *illustration* in the circumstances set out in MCOB 5.5.1AR(1), where it has given *advice* on a *direct deal*, the *firm* must give the *customer* a written record of the *advice*.
- 5.5.1C    R    If, notwithstanding MCOB 5.5.1AR(1), a *firm* chooses to give an *illustration* in relation to a *direct deal*, it need not comply with MCOB 5.4.2R or MCOB 5.4.3R (Accuracy).
- 5.5.1D    G    In the circumstances in MCOB 5.5.1CR, a *firm* remains subject to MCOB 5.4.1R (Clear, fair and not misleading).
- 5.5.1E    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.

...

- 5.5.4 R A *firm* must not ~~accept fees, commission a valuation, or undertake any other~~ action that commits the *customer* to an application (including accepting product-related 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]~~

...

No preference between repayment and interest only

- 5.5.13 R If the *customer* expresses no preference between a *repayment mortgage* and an *interest only mortgage*, the *firm* must:
- (1) ~~provide an illustration for a repayment mortgage (except where the firm does not provide repayment mortgages, in which case it must provide only an illustration for an interest only mortgage); and~~
  - (2) ~~make the customer aware that it has provided the illustration on this basis. [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:

...

- (7) any of the following information where it affects the availability of the *regulated mortgage contract* that the *customer* has requested information on or affects the information to be included in the *illustration*:

...

- (c) ~~whether the *customer* needs to self-certify his income; [deleted]~~

...

## 5.6 Content of illustrations

...

Content: required information

...

- 5.6.6 R As a minimum the *illustration* must be personalised to reflect the following requirements of the *customer*:

...

- (4) the term of the *regulated mortgage contract* (where the *customer* is unable to suggest a date at which he expects to repay the loan, for example in the case of an open-ended ~~secured bridging loan~~ *bridging loan*, secured overdraft or *mortgage credit card*, then a term of 12 months must be assumed and this assumption stated); and

...

Section 5: "Overall cost of this mortgage"

- 5.6.31 R Under the section heading 'Overall cost of this mortgage' where the *regulated mortgage contract* has an agreed term for repayment and a regular payment plan (that is, it is not a revolving credit agreement such as a secured overdraft or *mortgage credit card*, or a *regulated mortgage contract* where all of the interest rolls up, such as an open-ended ~~bridging loan~~ *bridging loan*):

...

- 5.6.32 R Under the section heading 'Overall cost of this mortgage' where the *regulated mortgage contract* has no agreed term for repayment, (and a 12 month term has been assumed), or no regular payment plan, or both (for example, a revolving credit agreement such as a secured overdraft or *mortgage credit card* or a *regulated mortgage contract* where all the interest rolls up such as an open-ended ~~bridging loan~~ *bridging loan*):

...

- (2) where all the interest on the *regulated mortgage contract* rolls up and is repaid as a lump sum at the end of the *regulated mortgage contract*, for example a ~~secured bridging loan~~ *bridging loan*, then the following text must follow the text in (1): 'It assumes that you pay back the total amount owing as a lump sum at the end of the mortgage term.';

...

...

Section 6: 'What you will need to pay each [insert frequency of payments from MCOB 5.6.40R]'

- 5.6.39 R *MCOB 5.6.40R to MCOB 5.6.57G do not apply to loans without a term or regular payment plan where some or all of the interest rolls up, for example ~~secured bridging loans~~ bridging loans, secured overdrafts or *mortgage credit cards*. In these cases, *MCOB 5.6.134R to MCOB 5.6.138G* apply.*

...

- 5.6.52 R Where all or part of the *regulated mortgage contract* to which the *illustration* relates is an *interest-only mortgage*:

...

- (2) if the *regulated mortgage contract* requires the *customer* to take out a ~~*repayment vehicle*~~ that is a tied product as a *repayment strategy* either through the *mortgage lender* or *mortgage intermediary* then:

...

- (b) include an accurate quotation or a reasonable estimate of the payments the *customer* will need to make for ~~the *repayment vehicle*~~ that tied product; and

...

- (3) if the *illustration* includes a quotation for the payments that would need to be made ~~into the *repayment vehicle*~~ by the *customer* for the *repayment strategy*:

...

- (b) the *illustration* must provide a brief description only of the type of *repayment vehicle strategy* illustrated (full details of the *repayment vehicle strategy* may be provided separately);

...

- (4) if a quotation for the *repayment vehicle strategy* is not provided in the *illustration*, the *illustration* must include a '?' sign in the column for payments alongside the following text...
- (5) unless *MCOB 5.6.55R* applies, if a quotation for the *repayment vehicle strategy* has been included in the *illustration*, Section 6 must be extended to illustrate the monthly cost inclusive of the savings plan and must have the sub-heading 'What you will need to pay each [insert frequency of payments from *MCOB 5.6.40R*] including the cost of a savings plan to

repay the capital' and must include:

...

- (b) the sum of what the *customer* would need to pay in each instalment for the *regulated mortgage contract* and for the *repayment vehicle strategy* in the payments column. For example if payments are made monthly, this would be the amount that the *customer* would need to pay each month for the *regulated mortgage contract* and the *repayment vehicle strategy*...

...

#### Multi-part mortgages

...

5.6.56 R Where *MCOB* 5.6.55R applies and part of the *regulated mortgage contract* is an *interest-only mortgage*:

- (1) if a quotation for the *repayment vehicle strategy* has been included in the *illustration* in accordance with *MCOB* 5.6.52R(3) then *MCOB* 5.6.52R(5) does not apply.

...

...

#### Section 7: 'Are you comfortable with the risks'?

5.6.58 R *MCOB* 5.6.59R to *MCOB* 5.6.65R do not apply to loans without a term or regular repayment plan where some or all of the interest rolls up, for example, ~~secured bridging loans~~ *bridging loans*, secured overdrafts or *mortgage credit cards*. In these cases *MCOB* 5.6.140R to *MCOB* 5.6.145R apply.

5.6.59 R Under the section heading 'Are you comfortable with the risks?':

- (1) under the sub-heading 'What if interest rates go up?' the *illustration* must include the following:

...

(e)

...

- (ii) where a *repayment vehicle strategy* has been included in the *illustration* in accordance with *MCOB* 5.6.52R(3), the payments quoted in (i) must include the cost of the *repayment vehicle strategy* and state that this is the case;

...

...

Alternative requirements for loans without a term or a regular repayment plan  
Section 6: “ What you will need to pay each [insert frequency of payments from  
MCOB 5.6.40R]”

- 5.6.133 R *MCOB 5.6.134R to MCOB 5.6.138G* apply only to loans without a term or regular payment plan where some or all of the interest rolls up, for example ~~secured bridging loans~~ bridging loans, secured overdrafts or *mortgage credit cards*.
- 5.6.134 R The heading for Section 6 of the *illustration* and the heading of the column on the right-hand side of this section must state the frequency with which payments must be made by the *customer*. (For example, if payments were to be made on a monthly basis, the heading for this section would be 'What you will need to pay each month' and the column would be headed 'Monthly payments'). Where no regular payments are required on the *regulated mortgage contract*, for example where all interest is rolled-up on a ~~secured bridging loan~~ bridging loan, then this section must be retained and the frequency of payments assumed must be 'monthly'.
- 5.6.135 R All the payments in Section 6 of the *illustration* must be calculated based on the frequency used for the purposes of the headings in *MCOB 5.6.40R* and must be shown in the column on the right-hand side of this section. If no payments are required, for example on a ~~secured bridging loan~~ bridging loan or secured overdraft, then this column should be marked on the *illustration* as nil.
- 5.6.136 R Section 6 of the *illustration* must contain the following information:

...

- (3) where no payments are required (or no payments are allowed), for example a ~~secured bridging loan~~ bridging loan or secured overdraft, then section 6 of the *illustration* should state if no payments are required or no payments can be made; or

...

Section 7: “Are you comfortable with the risks?”

- 5.6.139 R *MCOB 5.6.140R to MCOB 5.6.145R* apply only to loans without a term or regular payment plan where some or all of the interest rolls up, for example ~~secured bridging loans~~ bridging loans, secured overdrafts or *mortgage credit cards*.

...

## 5.7 **Business loans and loans to high net worth mortgage customers: tailored provisions**

- 5.7.1 R Where the *regulated mortgage contract* is for a business purpose or a high net

worth mortgage customer, a firm may choose to provide a business illustration or high net worth illustration (as applicable) (in compliance with MCOB 5.7.2R) instead of complying with MCOB 5.6.

5.7.1A G Firms are reminded that, in accordance with MCOB 1.2.3R, they should either comply in full with MCOB, but in doing so may opt to take account of ~~or~~ ~~comply with~~ all tailored provisions in MCOB that relate to business loans or loans to high net worth mortgage customers. Therefore, a firm may only follow the tailored provisions in MCOB 5.7 in relation to one of these sectors if it also follows all other tailored provisions in MCOB ~~if it also follows all other tailored provisions in MCOB~~ that relate to that sector. In either case, the rest of MCOB applies in full.

5.7.2 R A business illustration or high net worth illustration provided to a customer must:

...

(4) use font sizes and typefaces consistently throughout the business illustration or high net worth illustration which are sufficiently legible so that the business illustration or high net worth illustration can be easily read by a typical customer;

...

5.7.3 G ...

(3) A firm may also choose to include other information beyond that required by MCOB 5.6. However, when adding additional material a firm should have regard to:

(a) the intended use of the business illustration or high net worth illustration as an aid to comparison by customers; and

(b) the requirement in MCOB 2.2.6R that any communication should be clear, fair and not misleading.

(4) The business illustration or high net worth illustration provided in accordance with MCOB 5.7.2R should be based upon the total borrowing that the firm is willing to provide under the regulated mortgage contract. This means that there is no requirement for a firm to provide a further business illustration or high net worth illustration (or business offer document or high net worth offer document) where a customer redraws against payments made under the regulated mortgage contract, providing this redrawing does not exceed the borrowing described in the original business offer document or high net worth offer document.

(5) MCOB 5.6.6R(4) requires that where the term of the regulated mortgage contract is open-ended, the business illustration or high net worth illustration must be based on an assumed term of 12 months and

that this assumption must be stated. This does not mean that a *firm* is limited in the actual term of the *regulated mortgage contract*. A *firm* is able to include in the *business illustration or high net worth illustration* an explanation that while a 12-month term has been assumed for the purpose of the *business illustration or high net worth illustration*, the *regulated mortgage contract* itself will be open-ended.

- 5.7.4 R Any *business illustration or high net worth illustration* provided by a *firm* must be limited to facilities provided under a *regulated mortgage contract*.
- 5.7.5 R *MCOB 5.6.31R(2)*, *MCOB 5.6.52R(1)* and *MCOB 5.6.52R(4)* prescribe text that should be used to remind a *customer* with an *interest-only mortgage* that there is a need to separately arrange for the repayment of capital. The options for repayment of capital may be different where the *regulated mortgage contract* is for a business purpose or a high net worth mortgage customer, and a *firm* must vary the prescribed wording in the *business illustration or high net worth illustration* to reflect this. One approach may be for the *firm* to revise the wording to reflect how the *customer* has said he will repay the capital.
- 5.7.6 R (1) When providing a *business illustration or high net worth illustration* in accordance with *MCOB 5.7.2R* a *firm* should describe facilities provided under the *regulated mortgage contract* that are not a loan within section 12 (Additional features) of the *business illustration or high net worth illustration*.
- (2) In complying with (1), a *firm* should follow the requirements in *MCOB 5.6.92R - MCOB 5.6.108G* where these are relevant. Where the facility is of a type not considered in *MCOB 5.6.92R - MCOB 5.6.108G* the *firm* should provide in section 12:
- (a) a brief description of the facility involved;
  - (b) the term of the facility if different from the term described elsewhere in the *business illustration or high net worth illustration*; and
  - (c) a summary of any charges, including any *early repayment charges*, which apply to the operation of the facility.
- (3) Full information on any facility described in section 12 must be provided in supplementary materials that accompany the *business illustration or high net worth illustration*.
- 5.7.7 G (1) In accordance with *MCOB 5.7.6R(1)*, where the *regulated mortgage contract* includes a loan, the facilities described in section 12 of the *business illustration or high net worth illustration* should include the existence of, and a simple explanation of, any all monies charge, any contingent liabilities such as guarantees and so on.
- (2) Where the *regulated mortgage contract* includes more than one loan facility (such as a secured loan and a separate secured overdraft

facility) the *business illustration* or *high net worth illustration* should be based upon the primary facility and describe any other loan within section 12.

## 5.8 Home purchase plans

...

Financial information statement: timing

- 5.8.1 R ~~A~~ Except in the circumstances in MCOB 5.8.1AR, a firm dealing directly with a customer must ensure that the customer is, or has been, provided with an appropriate financial information statement for a home purchase plan in a durable medium:
- (1) before the *customer* submits an application for that particular plan to a *home purchase provider*; and
  - (2) without undue delay when any of the following occurs:
    - (a) ~~the firm makes a personal recommendation to~~ advises the particular *customer* to enter into a one or more home purchase plan plans, in which case a financial information statement must be provided at the point the advice is given (and financial information statements for all recommended home purchase plans must be provided), (unless the personal recommendation advice is made given by telephone, in which case a firm must ensure the financial statement is or has been provided as soon as practicable after the telephone call) the firm must provide a financial information statement within five business days; or
    - (b) ~~the firm provides written information that is specific to the amount of finance to be provided on a particular plan; or [deleted]~~
    - (c) ~~the customer requests written information from the firm that is specific to the amount of finance to be provided on a particular plan, unless the firm does not wish to do business with the customer. [deleted]~~
    - (d) the customer requests a financial information statement, unless the firm is aware that it is unable to offer that home purchase plan to him; or
    - (e) as part of an execution-only sale (or potential execution-only sale) the customer has provided the firm with the information in MCOB 4.10.9DR (Execution-only sales) (see MCOB 4.10.9BR and MCOB 4.10.9CR) to indicate which home purchase plan or variation he wishes to enter into.

- (3) A *firm* may comply with (1) and (2) by providing an *offer document* if this can be done as quickly as providing a financial information statement.

5.8.1A R A *firm* need not provide a financial information statement:

- (1) in relation to a *direct deal*; 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; or
- (3) if the *firm* does not wish to do business with the *customer*.

5.8.1B R If the *firm* chooses not to give a financial information statement in the circumstances set out in *MCOB 5.8.1AR*, where it has given *advice* on a *direct deal*, the *firm* must give the *customer* a written record of the *advice*.

...

Financial information statement: format

...

- 5.8.5 R A financial information statement, if not set out in a separate document, must be:
- (1) in a prominent place within the ~~other~~ document and clearly identifiable as key information that the *customer* should read; and
- (2) separate from the other content of the document in which it is included.

...

Message to be given when providing information on home purchase plans

- 5.8.12 R (1) Except in the circumstances in (2), whenever a *firm* provides a *customer* with information specific to the amount of finance to be provided on a particular *home purchase plan* following an assessment of the *customer's* needs and circumstances in order to comply with *MCOB 4.10.5DR*, it must give, clearly and prominently, the following information:
- (a) the same information on the *firm's* product range as is required by *MCOB 4.4.A1R(1)*, *MCOB 4.4A.2R* and *MCOB 4.4A.4R (1)* (as applied in relation to *home purchase plans* by *MCOB 4.10.3AR*); and
- (b) that the *customer* has the right to request a financial information statement for any *home purchase plan* which the *firm* is able to

offer the customer.

- (2) A firm need not give the information in (1) if it has previously given that information in compliance with this rule within the last ten business days.

Message to be given when customer requests an execution-only sale

- 5.8.13 R Whenever, as part of an *execution-only sale* (or potential *execution-only sale*), a customer provides a firm with the information in MCOB 4.10.9DR (Execution-only sales) (see MCOB 4.10.9BR and MCOB 4.10.9CR) the firm must inform the customer, clearly and prominently, unless the firm has previously given this information in compliance with this rule within the last ten business days, that the customer has the right to request a financial information statement for any home purchase plan which the firm is able to offer the customer.

...

## 6.4 Mortgages: content of the offer document

...

Modifications to the illustration

- 6.4.4 R The illustration provided as part of the offer document in accordance with MCOB 6.4.1R(1) must meet the requirements of MCOB 5.6 (Content of illustrations) with the following modifications:

...

- (7) MCOB 5.6.52 R to MCOB 5.6.53 G is replaced by the following:  
Where all or part of the regulated mortgage contract is an interest-only mortgage, the illustration in the offer document must:
- (a) clearly state that the payments on the regulated mortgage contract cover only interest, and not the capital borrowed; and
  - (b) ~~state the repayment vehicle the customer intends to use where the firm knows details of the specific repayment vehicle from the application by the customer; if the firm does not know how the customer intends to repay the capital borrowed, the firm must clearly state that the repayment vehicle is unknown, and must provide the customer with a clear reminder of the need to put suitable arrangements in place; and [deleted]~~
  - (c) include a statement reminding the customer to check regularly the performance of any investment used as a repayment vehicle strategy, to see whether it is likely to be adequate to repay the capital and, where applicable, pay the interest accrued at the end of the term of the regulated mortgage contract;

(7A) The illustration may state the repayment strategy the customer intends to use.

...

Other information contained in the offer

...

6.4.11A R If the illustration provided by the firm to the customer does not state the repayment strategy the customer intends to use, as permitted by MCOB 6.4.4R(7A), that information must be included in the offer document.

...

## 6.7 **Business loans and loans to high net worth mortgage customers: tailored provisions**

6.7.1 R (1) Where the *regulated mortgage contract* is for a business purpose or a high net worth mortgage customer, a firm may choose to provide a customer with a *business offer document* or high net worth offer document (as applicable) instead of the *offer document* referred to in MCOB 6.4.1R.

(2) If a firm provides a customer with a *business offer document* or high net worth offer document in accordance with (1), it must ensure that:

(a) an updated *business illustration* or high net worth illustration (as applicable), as required by MCOB 5.7 (~~Pre-application disclosure for business~~ Business loans and loans to high net worth mortgage customers: tailored provisions), forms part of the *business offer document* or high net worth offer document; and

(b) subject to the tailoring required by MCOB 5.7 (~~Pre-application disclosure for business~~ Business loans and loans to high net worth mortgage customers: tailored provisions), the *business offer document* complies with MCOB 6.4 (~~Mortgages: Content~~ content of the offer document).

6.7.1A G *Firms* are reminded that in accordance with MCOB 1.2.3R and MCOB 1.2.3AR, they should ~~either~~ comply in full with MCOB, but in doing so may opt to take account of or comply with all tailored provisions in MCOB that relate to business loans or loans to high net worth mortgage customers (as applicable). Therefore, a firm may only follow the tailored provisions in MCOB 6.7 in relation to one of these sectors if it also follows all other tailored provisions in MCOB that relate to that sector. In either case, the rest of MCOB applies in full.

6.7.2 G MCOB 6.7.1R(2) means, for example, that the required text in MCOB 6.4.4R(7) should be replaced by text that satisfies the requirements for

*business illustrations or high net worth illustrations* in MCOB 5.7.5R.

- 6.7.3 G A *firm* may supplement the first paragraph of text prescribed in MCOB 6.4.4R(5)(a) to clarify that, while the *regulated mortgage contract* is not binding until the relevant mortgage document has been signed and funds have been released, the *business offer document or high net worth offer document* may form part of a wider set of negotiated facilities and that the *customer* is separately bound by these.

...

## 6.9 Regulated sale and rent back agreements

Process for concluding regulated sale and rent back agreements

- 6.9.1 R A *SRB agreement provider* must not ~~enter into a~~ enter into a regulated sale and rent back agreement unless it follows the process outlined in this section.

Valuation of the property

- 6.9.2 R (1) A *SRB agreement provider* intending to ~~enter into a~~ enter into a specific regulated sale and rent back agreement with a *SRB agreement seller* and before it complies with the other requirements in this section, must ensure that the property is properly valued by a valuer: ...

...

...

## 7.4 Mortgages: disclosure at the start of the contract

Disclosure requirements

- 7.4.1 R (Subject to *MCOB 7.7.5R*) a *firm* that *enters into a regulated mortgage contract* with a *customer* must provide the *customer* with the following information before the *customer* makes the first payment under that *regulated mortgage contract*:

...

- (4) confirmation of whether, in connection with the *regulated mortgage contract*, insurance or *investments* (such as a *repayment ~~vehicle~~ strategy*, term assurance, buildings and contents insurance or payment protection insurance) have been purchased through the *firm*;

...

- (8) if all or part of the *regulated mortgage contract* is an *interest-only mortgage*, a reminder to the *customer* to check that a *repayment ~~vehicle~~ strategy* is in place, if the *repayment ~~vehicle~~ strategy* is not provided by the *firm*;

- (9) what to do if the *customer* falls into ~~arrears~~ a payment shortfall, explaining the benefit of making early contact with the *firm*, providing the address and telephone number of a contact point for the *firm* and drawing the *customer's* attention to the *arrears* charges set out in the *tariff of charges*.

...

## 7.5 Mortgages: statements

...

Annual statement: content

7.5.3 R The statement required by *MCOB 7.5.1R* must contain the following:

(1) except in the case of *mortgage credit cards*, information on the type of *regulated mortgage contract*, including:

...

(b) a prominent reminder, where all of the *regulated mortgage contract* is an *interest-only mortgage*, that:

(i) the *customer's* payments to the *firm* do not include ~~the~~ any costs of ~~any the~~ repayment vehicle strategy (if that is the case); and...

...

(c) a prominent reminder, where only part of the *regulated mortgage contract* is an *interest-only mortgage*, that:

(i) the *customer's* payments to the *firm* do not include ~~the~~ any costs of ~~any the~~ repayment vehicle strategy (if that is the case); and...

...

(4) information at the date the statement is issued on:

...

(e) the cost of redeeming the *regulated mortgage contract* (this must be shown as the sum of *MCOB 7.5.3R(4)(a)* and *MCOB 7.5.3R(4)(d)* plus any *linked borrowing* that cannot be retained (including the outstanding balances) plus any other charges that can be quantified at the date the statement is issued); if additional charges are payable that cannot be quantified at the point that the statement is issued (for example if the *customer* is in ~~arrears~~ arrears) a warning must be included to that effect; and

...

7.5.4 R ~~In the limited circumstances where it would be unlikely for~~ Where payments are not being made for a repayment vehicle to be set up strategy for an interest-only mortgage (for example, for a short term bridging loan bridging loan) *MCOB 7.5.3R(1)(b)(ii)* or *MCOB 7.5.3R(1)(c)(ii)* is replaced with the following: "As all or part of your mortgage is an interest-only mortgage, it assumes that you pay back the total amount borrowed on an interest-only

basis as a lump sum at the end of the mortgage term."

...

Annual statement: additional content for customers in arrears

- 7.5.8 G If a *firm* chooses to use the annual statement to provide a *customer* with a regular written statement in accordance with *MCOB* 13.5.1R (Statements of charges), as described in *MCOB* 13.5.2G(4), it will need to include the actual ~~payment shortfall~~ payment shortfall in the annual statement.

...

## 7.6 Mortgages: event-driven information

...

Further advances

- 7.6.7 R Before a *customer* submits an application to a *firm* for a further advance on an existing *regulated mortgage contract* or for a further advance that is a new *regulated mortgage contract*, if the further advance requires the approval of the *mortgage lender*, the *firm* must provide the *customer* with an illustration that complies with the requirements of *MCOB* 5 (Pre-application disclosure) and *MCOB* 7.6.9R to *MCOB* 7.6.17R for the further advance, unless an illustration has already been provided or the *regulated mortgage contract* is for a business purpose and the *firm* has chosen to comply with the tailored provisions for *regulated mortgage contracts* for a business purpose or loans to high net worth mortgage customers (see *MCOB* 7.7 (Business loans and loans to high net worth mortgage customers: tailored provisions)).

...

- 7.6.9 R The *illustration* provided in accordance with *MCOB* 7.6.7R must:

...

- (4) include a clear statement, where all or part of the *regulated mortgage contract* is an *interest-only mortgage* and the amount paid in each instalment does not include the cost of a *repayment vehicle strategy*, to indicate that these payments do not include the cost of any savings plan or other investment.

...

## 7.7 Business loans and loans to high net worth mortgage customers: tailored provisions

Further advances

- 7.7.1 R (1) Where, in relation to a *regulated mortgage contract* for a business purpose or a high net worth mortgage customer, a *customer* either:

- (a) seeks an immediate increase in the borrowing provided under the *regulated mortgage contract*; or
- (b) overdraws on the borrowing under the *regulated mortgage contract*;

the further advance rules in *MCOB 7.6.7R* to *MCOB 7.6.17R* do not apply.

- (2) Where (1) applies, the *firm* must within five *business days* (for a loan for a business purpose) or in good time before the customer is bound by the regulated mortgage contract (for a high net worth mortgage customer) provide the *customer* with either:
  - (a) a business illustration or high net worth illustration (as applicable) for the new total borrowing; or

...

- 7.7.1A G *Firms* are reminded that in accordance with *MCOB 1.2.3R*, they should ~~either~~ comply in full with *MCOB*, but in doing so may opt to take account of ~~or~~ comply with all tailored provisions in *MCOB* that relate to business loans or loans to high net worth mortgage customers. Therefore, a *firm* may only follow the tailored provisions in *MCOB 7.7* in relation to one of these sectors if it also follows all other tailored provisions in *MCOB* that relate to that sector. In either case, the rest of *MCOB* applies in full.

...

- 7.7.3 R Where a *customer* applies for a further advance that is a *regulated mortgage contract* for a business purpose or a high net worth mortgage customer and *MCOB 7.7.1R* does not apply:
- (1) the business illustration or high net worth illustration must be based upon the total borrowing; and
  - (2) *MCOB 7.6.9R* to *MCOB 7.6.10G* and *MCOB 7.6.12G* do not apply.

#### Arrangements to repay capital

- 7.7.4 R Where *MCOB 7.6.28R(5)* applies, a *firm* may omit the final sentence of the required text where it is aware, in the context of an *interest-only mortgage*, that the *customer's* intention is not to use a savings plan as a *repayment vehicle strategy*.

#### Disclosure

- 7.7.5 R *MCOB 7.4* (Disclosure at the start of the contract) does not apply in relation to a *regulated mortgage contract* that is for a business purpose or a high net worth mortgage customer.

...

**7.8 Home purchase plans**

...

Annual statement – additional content for customers in arrears

7.8.4 G If a *firm* uses the annual statement to provide a *customer* with a written statement relating to *arrears*, it will need to include the actual ~~payment shortfall~~ payment shortfall in the annual statement (see *MCOB* 13.5.2G(4)).

...

**8.1 Application**

Who?

8.1.1 R This chapter applies to a *firm* in a category listed in column (1) of the table in *MCOB* 8.1.2 R in accordance with column (2) of that table.

8.1.2 R This table belongs to *MCOB* 8.1.1R

(1) Category of firm	(2) Applicable section
<i>equity release provider</i>	whole chapter except <i>MCOB</i> 8.5A and <i>MCOB</i> 8.7, <i>MCOB</i> 8.6A in accordance with <i>MCOB</i> 8.1.2AR
<i>equity release adviser</i>	whole chapter except <del><i>MCOB</i> 8.6</del> . <i>MCOB</i> 8.7 does not apply in relation to a <i>lifetime mortgage</i>
<i>equity release arranger</i>	whole chapter except <i>MCOB</i> 8.5A. <i>MCOB</i> 8.7 does not apply in relation to a <i>lifetime mortgage</i>

8.1.2A R *MCOB* 8.6A only applies to an *equity release provider* in relation to entering into an *equity release transaction* where there is no *firm* which is arranging (bringing about) the *equity release transaction* to which *MCOB* 8.6A applies.

8.1.2B G *MCOB* 8.1.2AR means that the situations where *MCOB* 8.6A applies to an *equity release provider* include where an *equity release intermediary* has been involved in arranging (bringing about) an *equity release transaction* but is no longer involved in the transaction.

What?

8.1.3 R (1) This chapter applies to a *firm* which in the course of carrying on an *equity release activity*: enters into, advises on or arranges an *equity release transaction* or a variation of the terms of an *equity release*

transaction.

- (a) ~~makes, or anticipates making, a *personal recommendation* about; or~~
- (b) ~~gives, or anticipates giving, personalised information relating to;~~

~~the *customer*:~~

- (c) ~~entering into an *equity release transaction*; or~~
- (d) ~~varying the terms of an *equity release transaction* entered into by the *customer*.~~

- (2) In respect of *arranging or advising on a home reversion plan* for a *customer* who is acting in his capacity as an *unauthorised reversion provider*, only MCOB 8.1, MCOB 8.2 and MCOB 8.7 apply.

...

- 8.1.5 G ~~If a *firm* is an *authorised professional firm*, MCOB 1.2.10R(3) has the effect that when the *firm* conducts *non-mainstream regulated activities* with a *customer*, MCOB 4.4 (Initial disclosure requirements) (as modified by MCOB 8) applies. The *firm* is only required to provide the initial disclosure information in section 7 (What to do if you have a complaint) and section 8 (Are we covered by the Financial Services Compensation Scheme (FSCS)?) of the *initial disclosure document* or *combined initial disclosure document*.  
[deleted]~~

## 8.2 Purpose

- 8.2.1 G ~~The purpose of this chapter for *equity release transactions* is the same as that for *regulated mortgage contracts* and *home purchase plans* in MCOB 4.  
[deleted]~~
- 8.2.2 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 nature of the service they may receive from a *firm* in relation to *equity release transactions*. In particular *firms* need to make clear to *customers* the range of *equity release transactions* available from them and the basis of the *firm's* remuneration;
  - (b) where *advice* is given, it is suitable for the *customer*;

- (c) customers for equity release transactions receive advice in all cases;
  - (d) subject to certain limited exceptions (which are set out in MCOB 8.6A), execution-only sales are only provided where the customer has rejected advice which has been given, has been warned about the implications of proceeding and has specifically instructed the firm that he wishes to do so.
- (3) This chapter also implements certain requirements of the Distance Marketing Directive in relation to distance mortgage mediation contracts.

### 8.3 Application of rules in MCOB 4

- 8.3.1 R (1) (a) Subject to (c), MCOB 4.1 to MCOB 4.6A and MCOB 4.8 (with the modifications stated in MCOB 8.3.32BR and to MCOB 8.3.4R) apply to a firm where the home finance transaction is a lifetime mortgage.
- (b) MCOB 4.1 to MCOB 4.4A and MCOB 4.8 (with the modifications stated in MCOB 8.3.32BR and to MCOB 8.3.4R) apply to a firm where the home finance transaction is a home reversion plan, except for those provisions that by their nature are only relevant to regulated mortgage contracts.
- (c) MCOB 4.6A applies to a lifetime mortgage only if it is not an interest roll-up mortgage.
- ...
- 8.3.2 R ~~In applying initial disclosure requirements to equity release transactions, the market for equity release transactions should be treated as one single market with two separate sectors. References to the 'whole market' must be read as references to the whole market for equity release transactions. This is unless the firm only gives personalised information or advice to customers on products in one market sector, in which case references to the 'whole market' must be read as references to the whole market for lifetime mortgages or home reversion plans as the case may be. [deleted]~~
- 8.3.2A G ~~The effect of the rules on independence is that a firm that sells lifetime mortgages and home reversion plans from the whole market and enables the customer to pay a fee for the provision of the service, can hold itself out as being 'independent' for the equity release market (see MCOB 4.3.7 R). If the firm offers a service on this basis for only one of these market sectors, then it can only describe itself as 'independent' for that sector. [deleted]~~
- 8.3.2B R For the purposes of MCOB 4.4A.2R(1) there is one relevant market for equity release transactions. Accordingly, a firm offering a customer only

lifetime mortgages or only home reversion plans must include in its disclosure under MCOB 4.4A.1R(1) that it is limited in that regard in the range of products that it can offer to the customer.

8.3.2C G In the light of MCOB 8.3.2BR, a firm may wish to consider using a sentence appropriate to the circumstances, along the following lines:

- “We offer a comprehensive range of equity release products from across the market.”
- “We sell home reversion plans only and not lifetime mortgages, though we will consider all home reversion plans available in the market.”

8.3.3 R Table of modified cross-references to other rules: This table belongs to MCOB 8.3.1R.

Subject	Rule or guidance	Reference in rule or guidance	To be read as a reference to:
<del>Advice or information from the whole market</del>	<del>MCOB 4.3.4R(2)</del>	<del>MCOB 4.7.2R</del>	<del>MCOB 8.5.2R</del>
<del>Initial disclosure requirement (for equity release transactions only)</del>	<del>MCOB 4.4.1R(1)(e) and (3)</del>	<del>MCOB 4 Ann 1R</del>	<del>MCOB 8 Ann 1R</del>
<del>Initial disclosure requirements</del>	<del>MCOB 4.4.3G</del>	<del>MCOB 4</del>	<del>MCOB 4 as modified by MCOB 8</del>
<del>Initial disclosure requirements where initial contact is by telephone (for equity release transactions only)</del>	<del>MCOB 4.4.7R(2)</del>	<del>MCOB 4 Ann 1R</del>	<del>MCOB 8 Ann 1R</del>
<del>Additional disclosure for distance mortgage mediation contracts</del>	<del>MCOB 4.5</del>	<del>MCOB 4</del>	<del>MCOB 4 as modified by MCOB 8</del>
<del>Non advised sales</del>	<del>MCOB 4.8.6G</del>	<del>MCOB 4.7</del>	<del>MCOB 8.5</del>

8.3.4 R Table of rules in MCOB 4 replaced by rules in MCOB 8: This table belongs to MCOB 8.3.1 R.

Subject	Rule(s)	Rule(s) replaced by
Advised sales	MCOB 4.7 <u>A</u>	MCOB 8.5 <u>A</u>



*transaction* which satisfies the requirements of *MCOB* 8.5A.2R, the *firm* must nonetheless have regard to *MCOB* 13.3.

- 8.5A.6 R When a *firm* assesses whether the *equity release transaction* is appropriate to the needs and circumstances of the *customer* for the purposes of *MCOB* 8.5A.5R(1), the factors it must consider include the following:
- (1) whether the benefits to the *customer* outweigh any adverse effect on:
    - (a) the *customer's* entitlement (if any) to means-tested benefits; and
    - (b) the *customer's* tax position (for example the loss of an Age Allowance);
  - (2) alternative methods of raising the required funds such as, in particular:
    - (a) (where relevant) a local authority (or other) grant; or
    - (b) taking a further advance under an existing *regulated mortgage contract* (including a *lifetime mortgage*), or a new *regulated mortgage contract* (including a *lifetime mortgage*) to replace an existing one, or an additional release under an existing *home reversion plan*;
  - (3) whether the *customer's* requirements appear to be within the *equity release provider's* known eligibility criteria for the *equity release transaction*;
  - (4) the *customer's* preferences for his estate (for example, whether the *customer* wishes to be certain of leaving a bequest to his family or others);
  - (5) the *customer's* health and life expectancy;
  - (6) the *customer's* future plans and needs (for example, whether the *customer* is likely to need to raise further funds or is likely to move house);
  - (7) whether the *customer* has a preference or need for stability in the amount of payments (where payments are required) especially having regard to the impact on the *customer* of significant interest rate changes in the future;
  - (8) whether the *customer* has a preference or need for any other features of an *equity release transaction*; and
  - (9) for *lifetime mortgages* only, whether it is more appropriate for the *customer* to pay any fees or charges in relation to the *lifetime mortgage* up front, rather than adding them to the sum advanced (see also *MCOB* 4.6A).
- 8.5A.7 G Examples of eligibility criteria in *MCOB* 8.5A.6R(3) are: the amount that

the *customer* wishes to borrow or to release; the loan-to-value ratio; the age of the *customer*; the value of the property which would be the subject of the *equity release transaction*.

The customer's needs and circumstances: means-tested benefits, customer's tax position and alternative methods of finance

8.5A.8 R In considering the factor at *MCOB* 8.5A.6R(1), where a *firm* has insufficient knowledge of means-tested benefits and tax allowances to reach a conclusion, the *firm* must refer a *customer* to an appropriate source or sources such as the Pension Service, HM Revenue and Customs or Citizens Advice Bureau (or other similar agency) to establish the required information.

8.5A.9 E (1) In considering the factor at *MCOB* 8.5A.6R(2)(a), a *firm* should:

- (a) establish, on the basis of information given by the *customer* about his needs and objectives, whether these appear to be within the general scope of a local authority (or other) grant (for example where the *customer* requires funds for essential repairs to his property); and
- (b) refer a *customer* to an appropriate source such as his local authority or Citizens Advice Bureau (or other similar agency) to identify whether such a grant is available to him.

(2) Compliance with (1) may be relied upon as tending to show compliance with *MCOB* 8.5A.6R(2)(a).

8.5A.10 R If for any reason a *customer*:

- (1) declines to seek further information on means-tested benefits, tax allowances or the scope for local authority (or other) grants; or
- (2) rejects the conclusion of a *firm* that alternative methods of raising the required funds are more suitable;

a *firm* can advise the *customer* (in accordance with the remaining requirements of this chapter) to enter into an *equity release transaction* where there is an *equity release transaction* (or more than one *equity release transaction*) that is appropriate to the needs and circumstances of the *customer*, but must confirm to the *customer*, in a *durable medium*, the basis on which the *advice* has been given.

Debt consolidation

8.5A.11 R In relation to *MCOB* 8.5A.5R(1), when a *firm* advises a *customer* in relation to entering into an *equity release transaction* where the main purpose for doing so is the consolidation of existing debts by the *customer*, it must also take account of the following in assessing whether the *equity release transaction* is suitable for the *customer*:

- (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 enter into an *equity release transaction*.

8.5A.12 E An attempt by the *firm* to misdescribe the *customer's* purpose or to encourage the *customer* to tailor the amount he wishes to borrow so that *MCOB 8.5A.11R* does not apply may be relied on as tending to show contravention of *MCOB 2.5A.1R* (The customer's best interests).

#### Further advances

8.5A.13 R Where the *customer* is looking to increase the borrowing secured on the property which is the subject of an existing *regulated mortgage contract*, a *firm* must inform the *customer* (either orally or in writing) that it may be possible, and more appropriate, for the *customer* to take a further advance with the existing lender rather than entering into an *equity release transaction* with another provider.

8.5A.14 G *MCOB 8.5A.13R* does not mean that *firms* are under any obligation to explore whether a further advance with the existing lender is, in fact, more appropriate for the *customer*.

#### Other considerations when advising

8.5A.15 R When *advising a customer* on the suitability of an *equity release transaction*, a *firm* must explain to the *customer* that the assessment of whether the *equity release transaction* is appropriate to his needs and circumstances is based on the *customer's* current circumstances, which may change in the future.

8.5A.16 G Different considerations apply when dealing with a *customer* with a *payment shortfall*. For example, the circumstances of the *customer* may mean that, viewed as a new transaction, a *customer* should not be advised to enter into an *equity release transaction*. In such cases, a *firm* may still be able to *advise the customer* to enter into an *equity release transaction* where it is more suitable than the *customer's* existing *home finance transaction*.

8.5A.17 G *MCOB 8.5A.5R(3)* means that where the *advice* provided is based on a selection of *equity release transactions* from a single or limited number of providers, the assessment of suitability should not be limited to the types of *equity release transactions* which the *firm* offers. A *firm* cannot recommend the 'least worst' *equity release transaction* where the *firm* does not have access to products appropriate to the *customer's* needs and circumstances. This means, for example, that if a *firm* only has access to

lump sum *equity release transactions* it should not recommend or arrange one of these if approached by a *customer* requiring regular payments.

- 8.5A.18 G *MCOB 8.5A.5R(1)* 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*. *MCOB 8* 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*).

#### Record keeping

- 8.5A.19 R (1) A *firm* must make and retain a record:
- (a) of the *customer* information, including that relating to the *customer's* needs and circumstances and the *customer's* apparent satisfaction of the *equity release provider's* known eligibility criteria, that it has obtained for the purposes of *MCOB 8.5A*;
  - (b) that explains why the *firm* has concluded that any *advice* given to a *customer* complies with *MCOB 8.5A.2R* and satisfies the suitability requirement in *MCOB 8.5A.5R(1)*;
  - (c) of any *advice* which the *customer* has rejected, including the reasons why they were rejected and details of the *equity release transaction* which the *customer* has proceeded with as an *execution-only sale*; and
  - (d) where applicable, of the *customer's* positive choice in *MCOB 4.6A.2R* (Rolling up of fees or charges into loan).
- (2) The records in (1) must be retained for a minimum of three years from the date on which the *advice* was given or, in the case of (1)(d), the making of the choice.

*MCOB 8.6* is deleted in its entirety and replaced with a new section *MCOB 8.6A*. The deleted text is not shown and the new text is not underlined.

### **8.6A Execution-only sales**

#### Scope and application of this section

- 8.6A.1 G (1) *MCOB 8.6A* provides that a *firm* may only *enter into an equity release transaction* with a *customer*, or *arrange* such a transaction for a *customer*, as an *execution-only sale* if the *customer* has rejected *advice*, identified the product he wishes to purchase and positively elected to proceed with an *execution-only sale*.
- (2) The aim of *MCOB 8.6A* is to ensure that, in all sales of *equity release transactions*, there is one *firm* which *advises* the *customer*

on the *equity release transaction* and, where applicable, is responsible for ensuring that the conditions for an *execution-only sale* are satisfied. So, as provided in *MCOB 8.1.2AR*, *MCOB 8.6A* only applies to *equity release providers* in relation to *entering into equity release transactions* where there is no *firm* which is *arranging* the transaction and to which *MCOB 8.6A* applies.

The customer's best interests

- 8.6A.2 G *Firms* are reminded that *MCOB 2.5A.1R* (The customer's best interests) applies in all cases, including in relation to *execution-only sales*.
- 8.6A.3 R A *firm* must not encourage a *customer* to reject *advice* received by him on *equity release transactions*.

The conditions for execution-only sales

- 8.6A.4 R A *firm* must not *enter into* or *arrange* an *execution-only sale* for a *equity release transaction* unless:

- (1) the *customer* has rejected the *advice* given by the *firm* and instead requested an *execution-only sale* of an *equity release transaction*;
- (2) the *customer* has identified which particular *equity release transaction* he wishes to purchase, and specified to the *firm* at least the required additional information (where applicable);
- (3) after providing the required information in (2), the *customer* has been informed, clearly and prominently and in a *durable medium*, and that the *customer* will not benefit from the protection of the rules (in *MCOB 8.5A*) on assessing suitability.
  - (a) in any case where the *firm* has advised the *customer* that the *equity release transaction* is unsuitable for the *customer*, that that is the case; and
  - (b) in any other case, that in the provision of its services for the *execution-only sale* the *firm* is not required to assess the suitability of that *equity release transaction*;

and in either case that the *customer* will not benefit from the protection of the rules (in *MCOB 8.5A*) on assessing suitability. In any case where there is spoken dialogue between the *firm* and the *customer* at any point, the *firm* must also provide this information orally; and

- (4) after the *customer* has been provided with the information in (3), in any case where there is spoken or other interactive dialogue between the *firm* and the *customer* at any point, the *customer* has confirmed in writing to the *firm* that he is aware of the consequences of losing the protections of the rules on assessing suitability and is making a positive election to proceed with an *execution-only sale*. The written

confirmation must be in the same document as the information in *durable medium* in (3), which must be separate from any other information and contractual documentation.

Exception: rate switches and other variations to lifetime mortgages

- 8.6A.5 R (1) The condition in *MCOB* 8.6A.4R(1) does not apply in the case of a variation of a *lifetime mortgage*, provided that:
- (a) the variation would not involve the *customer* taking on additional borrowing beyond the amount currently outstanding under the existing *lifetime mortgage*, other than to finance any product fee or arrangement fee for the proposed new or varied contract; and
  - (b) where the variation will (in whole or part) change from one interest rate to another, the *firm* has presented to the *customer*, using a non-interactive channel, all products offered by it for which the *customer* is eligible, whether or not the *customer* then selects from those products using an interactive channel.
- (2) The reference to a variation in (1) (and in all other provisions which cross-refer to this *rule*) must be read as including any new *lifetime mortgage* which would replace an existing *lifetime mortgage* between the *customer* (or, where there are joint borrowers, at least one of them) and the *firm* (either as the original *equity release provider* or as the transferee of the existing contract).
- 8.6A.6 G (1) The variation in *MCOB* 8.6A.5R might involve the addition or removal of a borrower for joint mortgages or a change in payment method. This list is not exhaustive.
- (2) Examples of rate changes in *MCOB* 8.6A.5R(2) are: a transfer from a variable rate to a fixed rate; and a transfer from one fixed rate to another fixed rate.
- (3) *Firms* are reminded that, if their presentation in *MCOB* 8.6A.5R(1)(b) has (either explicitly or implicitly) steered the *customer* towards any one or more of the products offered by them such as to constitute *advice*, the requirements of *MCOB* 8.5A will apply.
- 8.6A.7 R The required additional information in *MCOB* 8.6A.4R(2) is:
- (1) for a *lifetime mortgage* other than one falling within *MCOB* 8.6A.5R:
    - (a) the name of the *mortgage lender*;
    - (b) the rate of interest;
    - (c) the interest rate type;

- (d) the price or value of the property on which the *lifetime mortgage* would be secured (estimated where necessary); and
  - (e) the sum the *customer* wishes to borrow under it, either immediately or in the future (including the amount of any lump sum, any regular drawdown or flexible facility or any combination of amounts the *customer* wishes to apply for);
- (2) for a *home reversion plan*:
- (a) the name of the *equity release provider*;
  - (b) any initial lump sum required and any lump sum required in the future;
  - (c) the price or value of the property to which the *home reversion plan* would relate (estimated where necessary); and
  - (d) in the case of a *home reversion plan* which is not a full reversion, the amount or percentage of the value of the property that the *customer* wishes to retain.

8.6A.8 G Where the information in *MCOB 8.6A.4R(3)* is given by electronic means, the *firm* should ensure that the *customer* cannot progress to the next stage of the sale unless the information has been communicated to the *customer*.

#### Record keeping

- 8.6A.9 R (1) Whenever a *firm enters into* or *arranges an execution-only sale* for an *equity release transaction*, it must make and maintain a record of:
- (a) the required information provided by the *customer* which satisfies *MCOB 8.6A.4R(2)*;
  - (b) the information in *durable medium* in *MCOB 8.6A.4R(3)*;
  - (c) the confirmation by the *customer* in *MCOB 8.6A.4R(4)* (where applicable); and
  - (d) any *advice* from the *firm* which the *customer* rejected, including the reasons why it was rejected, before deciding to enter into an *execution-only sale*.
- (2) The record in (1) must be retained for a minimum of three years from the date on which the *equity release transactions* was *entered into* or *arranged*.

#### Forbearance

8.6A.10 R The restrictions in *MCOB 8.6A* on entering into *execution-only sales* do not apply to any variation which is made solely for the purposes of forbearance

where the *customer* has a *payment shortfall*, or in order to avoid a *payment shortfall*.

The following Annex is deleted in its entirety. The deleted text is not shown struck through.

**8 Annex 1R: Initial Disclosure Document [deleted]**

Amend the following as shown.

**9.3 Pre-application disclosure**

...

9.3.1 R ...

- (2) The table in *MCOB 9.3.2R* shows how the relevant *rules* and *guidance* in *MCOB 5* must be modified by replacing the cross-references with the relevant cross-references to *rules* and *guidance* in ~~*MCOB 9.3*~~ and ~~*MCOB 9.4*~~ applicable to *equity release transactions*.

...

...

9.3.2 R **Table of modified cross-references to other rules.**

This table belongs to *MCOB 9.3.1R*.

Subject	Rule or guidance	Reference in rule or guidance	To be read as a reference to:
...			
Applying for a <i>lifetime mortgage</i>	<i>MCOB 5.3.2G</i>	<i>MCOB 5.6.26R</i> and <i>MCOB 5.6.27R</i>	<i>MCOB 9.4.26R</i> and <i>MCOB 9.4.27R</i>
<u>Messages to be given when providing information on <i>equity release transactions</i></u>	<u><i>MCOB 5.4.18AR(1)</i></u>  <u><i>MCOB 5.4.18AR(1)(a)</i></u>	<u><i>MCOB 4.7A.2R</i></u>  <u><i>MCOB 4.4A.1R(1)</i></u> , <u><i>MCOB 4.4A.2R</i></u> and	<u><i>MCOB 8.5A.2R</i></u>  <u><i>MCOB 4.4A.1R(1)</i></u> , <u><i>MCOB 4.4A.2R</i></u> and

		<u>MCOB 4.4A.4R(1)</u>	<u>MCOB 4.4A.4R(1)</u> , each as applied by <u>MCOB 8.3.1R</u> in modified form
<u>Messages to be given when customer requests an execution-only sale</u>	<u>MCOB 5.4.18BR(1)</u>	<u>MCOB 4.8A.14R(1) to (3)</u>	<u>MCOB 8.6A.4R(2)</u>
<u>Guidance relevant to messages given to customer</u>	<u>MCOB 5.4.18CG</u>	<u>MCOB 5 Annex 1R</u>	<u>MCOB 9 Annex 1R</u> for a lifetime mortgage; <u>MCOB 9 Annex 2R</u> for a home reversion plan.
<i>Tied products</i>	<i>MCOB 5.4.24G</i>	<i>MCOB 5.6.74R</i>	<i>MCOB 9.4.73R</i> or <i>MCOB 9.4.160R</i>
<u>Provision of illustrations: timing</u>	<u>MCOB 5.5.1R(2)(e)</u>	<u>MCOB 4.8A.14R(1), (2) or (3)</u>	<u>MCOB 8.6A.4R(2)</u>
...			

9.3.3 R **Table of rules in MCOB 5 replaced by rules in MCOB 9: This table belongs to MCOB 9.3.1R**

Subject	Rule(s) or guidance	Rule(s) or guidance replaced by:
...		
<del>Information that is not an illustration</del>	<del>MCOB 5.4.14R</del>	<del>MCOB 9.3.11R</del>
...		

9.3.4 R **Table of rules in MCOB 5 which do not apply to MCOB 9: This table**

belongs to *MCOB 9.3.1R*.

Subject	Rule(s)
<del>Illustrations for repayment mortgages and interest only mortgages</del>	<i>MCOB 5.5.13R</i>
Business loans <u>and loans to high net worth mortgage customers: tailored provisions</u>	<i>MCOB 5.7</i>
...	

...

9.3.11 R ~~Where a *firm* provides a *customer* with information specific to an *equity release transaction* on a screen:~~

- (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 equally prominently on each page on screen: This information does not contain all of the details you need to choose an equity release product . Make sure that you read the separate key facts illustration before you make a decision.~~
- (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]~~

9.3.12 R In meeting a request for ~~written information specific to the *customer's* requirements on an *illustration*~~ in relation to a particular *equity release transaction* (see *MCOB 5.5.1R(2)(e)(d)*), the *firm* must not delay the provision of the *illustration* by requesting information other than:

...

...

## 9.7 Disclosure at the start of the contract: lifetime mortgages

...

Disclosure requirements where interest payments are required

9.7.2 R A *firm* that enters into a *lifetime mortgage* with a *customer* where interest payments are required (whether or not they will be collected by deduction from the income from an annuity or other linked *investment* product) must provide the *customer* with the following information before the *customer* makes the first payment under the contract:

...

- (9) if it is possible for ~~arrears~~ a payment shortfall to occur, what to do if the *customer* ~~falls into arrears~~ has a payment shortfall, explaining the benefit of making early contact with the *firm*, providing the name, address and telephone of a contact point with the *firm*, and drawing the *customer's* attention to the *arrears* charges set out in the tariff of charges;

...

Disclosure requirements where a lump sum payment is made to the customer and interest is rolled up

- 9.7.8 R Where the *lifetime mortgage* provides for a lump sum payment to be made to the *customer*, and all or part of the interest will be rolled up during the life of the mortgage, the *firm* must provide the *customer* with the following information before the *customer* makes the first payment under the contract, or if no payment are required from the *customer*, within seven days of completion of the mortgage:

...

- (2) If payments are required from the customer:

...

(d) what to do if the *customer* ~~falls into arrears~~ has a payment shortfall, explaining the benefit of making early contact with the *firm*, providing the name, address and telephone of a contact point with the *firm*, and drawing the *customer's* attention to the *arrears* charges set out in the tariff of charges;

...

MCOB 11.1, 11.2 and 11.3 are deleted in their entirety and replaced with new sections MCOB 11.4 et seq. The deleted text is not shown and the new text is not underlined.

## **11 Responsible lending, and responsible financing of home purchase plans**

### **11.1 Application [deleted]**

### **11.2 Purpose [deleted]**

### **11.3 Responsible lending, and responsible financing of home purchase plans [deleted]**

### **11.4 Application**

Who?

11.4.1 R This chapter applies to a *firm* in a category listed in column (1) of the table in *MCOB* 11.4.2R in accordance with column (2) of that table.

11.4.2 R This table belongs to *MCOB* 11.4.1R

(1) Category of firm	(2) Applicable section
<i>mortgage lender</i>	Whole chapter
<i>home purchase provider</i>	Whole chapter except <i>MCOB</i> 11.6.1G (2), <i>MCOB</i> 11.6.5R (3) and (4), <i>MCOB</i> 11.6.18R, <i>MCOB</i> 11.6.19G, <i>MCOB</i> 11.6.20R (2) and (9), <i>MCOB</i> 11.6.40G to <i>MCOB</i> 11.6.59G, <i>MCOB</i> 11.6.60R(2)(e), (3) and (4) and <i>MCOB</i> 11.7.3 R

What?

11.4.3 R This chapter applies:

- (1) if a *firm* enters into a regulated mortgage contract or home purchase plan with a customer; or
- (2) if a *firm* varies an existing regulated mortgage contract or home purchase plan; and

throughout the term of any regulated mortgage contract or home purchase plan which a *firm* has entered into.

## 11.5 Purpose

- 11.5.1 G (1) This chapter requires a *firm* to treat *customers* fairly by assessing, before deciding to:
- (a) enter into a regulated mortgage contract or home purchase plan; or
  - (b) vary a regulated mortgage contract or home purchase plan;
- whether the *customer* will be able to repay the sums borrowed and interest (in the case of a regulated mortgage contract) or pay the sums due (in the case of a home purchase plan).
- (2) This chapter aims to ensure that *customers* are not exploited by *firms* that provide finance in circumstances where the *customers* are self-evidently unable to repay (or pay) through income and have no alternative means of repayment (or payment).
  - (3) This chapter sets out some limited exceptions to the requirement to assess the *customer's* ability to repay (or pay), including

transitional arrangements in relation to *customers* with existing *regulated mortgage contracts* or *home purchase plans* which satisfy certain conditions.

- (4) This chapter also applies in relation to extending the term of a *bridging loan*.

## 11.6 Responsible lending and financing

Contents of this section

- 11.6.1 G (1) This section sets out *rules* and *guidance* for lenders and providers under *regulated mortgage contracts* and *home purchase plans*, in relation to the assessment of affordability for the *customer* of these contracts. *Firms* have the option of applying certain of the *rules* and *guidance* on a modified basis in relation to *regulated mortgage contracts* and *home purchase plans* which are solely for a business purpose or are with *high net worth mortgage customers*. This section also contains (at *MCOB* 11.6.41R to *MCOB* 11.6.52G) additional *rules*, with accompanying *guidance*, in relation to *regulated mortgage contracts* which are *interest-only mortgages*. These *rules*:
- (a) restrict the circumstances in which *interest-only mortgages* may be entered into, and impose additional requirements on *mortgage lenders* in those limited cases where they are permitted; and
  - (b) provide for an exception to the requirement to assess affordability in relation to those *interest-only mortgages* which are *interest roll-up mortgages*, and restrict the circumstances in which *interest roll-up mortgages* may be used (see *MCOB* 11.6.57R to *MCOB* 11.6.59G).
- (2) This section also contains (at *MCOB* 11.6.53E to *MCOB* 11.6.54G) special provisions for *mortgage lenders* in relation to *bridging loans*, including some which apply only where the *bridging loan* is an *interest-only mortgage*.

The assessment of affordability

- 11.6.2 R (1) Except as provided in *MCOB* 11.6.3R, *MCOB* 11.6.57R (Interest roll-up mortgages) and *MCOB* 11.7 (Transitional arrangements):
- (a) before *entering into*, or agreeing to vary, a *regulated mortgage contract* or *home purchase plan*, a *firm* must assess whether the *customer* (and any guarantor of the *customer's* obligations under the *regulated mortgage contract* or *home purchase plan*) will be able to pay the

sums due; and

- (b) the *firm* must not enter into the transaction in (a) unless it can demonstrate that the new or varied *regulated mortgage contract* or *home purchase plan* is affordable for the *customer* (and any guarantor).

(2) In *MCOB* 11.6, references to payment of sums due means:

- (a) in the case of a *regulated mortgage contract*, the making of the payments to repay the sums advanced and interest reasonably expected to be accrued under the *regulated mortgage contract*; and
- (b) in the case of a *home purchase plan*, the payment of sums due under the *home purchase plan*;

in each case as they fall due.

(3) In *MCOB* 11.6, references to the *customer* must be read as referring also to any guarantor of the *customer's* obligations under the *regulated mortgage contract*, where the context permits.

11.6.3 R (1) *MCOB* 11.6.2R does not apply to:

- (a) *entering into* a new *regulated mortgage contract* or *home purchase plan* as a replacement for an existing *regulated mortgage contract* or *home purchase plan* between the *customer* and the *firm* (either as the original *mortgage lender* or *home purchase provider* or as the transferee of the existing contract), whether or not the new contract relates to the same property; or
- (b) a variation of an existing *regulated mortgage contract* or *home purchase plan*;

provided the conditions in (2) are satisfied.

(2) The conditions referred to in (1) are that:

- (a) the proposed new or varied *regulated mortgage contract* or *home purchase plan* would not involve the *customer* taking on additional borrowing or (for a *home purchase plan*, increasing the amount of finance provided under the plan) beyond the amount currently outstanding under the existing *regulated mortgage contract* or *home purchase plan*, other than to finance any product fee or arrangement fee for the proposed new or varied contract; and
- (b) there is no change to the terms of the *regulated mortgage contract* or *home purchase plan* which is likely to be

material to affordability.

- (3) *MCOB 11.6.2R* does not apply to a variation to the terms of a *regulated mortgage contract* or *home purchase plan* which is made solely for the purposes of forbearance where the *customer* has a *payment shortfall*, or in order to avoid a *payment shortfall*.
- 11.6.4 E (1) If a *firm* treats any of the following changes as not likely to be material to affordability, this may be relied upon as tending to show contravention of *MCOB 11.6.2R*:
- (a) an extension of the term of the *regulated mortgage contract* or *home purchase plan* which it is reasonable to expect will extend into the *customer's* retirement; or
  - (b) changing from a *repayment mortgage* to an *interest-only mortgage*, or vice versa; or
  - (c) the addition or removal of a *customer*.
- (2) The list in (1) is not exhaustive.
- 11.6.5 R When assessing for the purposes of *MCOB 11.6.2R* whether a *customer* will be able to pay the sums due, a *firm*:
- (1) must not base its assessment of affordability on the equity in the property which is used as security under the *regulated mortgage contract* or is subject to the *home purchase plan*, or take account of an expected increase in property prices;
  - (2) must take full account of:
    - (a) the income of the *customer*, net of income tax and national insurance; and, as a minimum
    - (b) (i) the *customer's* committed expenditure; and
    - (ii) the basic essential expenditure and basic quality-of-living costs of the *customer's* household;
  - (3) (if it is a *mortgage lender*) must assess affordability on the basis of both repayment of capital and payment of interest over the term, except where lending under an *interest-only mortgage* in accordance with *MCOB 11.6.41R(1)*; and
  - (4) (if it is a *mortgage lender*) must take account of the impact of likely future interest rate increases on affordability, as set out in *MCOB 11.6.18R*.
- 11.6.6 R For the purposes of *MCOB 11.6.2R*, a *firm* must not rely on a general declaration of affordability by the *customer* or his representative.

## Income multiples

- 11.6.7 G A *firm* may wish to impose a limit, expressed as a multiple of the *customer's* income, on the amount it is prepared to advance under a *regulated mortgage contract* or *home purchase plan*. Such an approach is not, of itself, inconsistent with *MCOB* 11.6.2R but, in accordance with the *rules* in this section, the *firm* must be able to demonstrate that the loan is affordable, having taken full account of the *customer's* income and expenditure, and (for a *mortgage lender*) the impact of future likely interest rate increases on affordability.

## Income

- 11.6.8 R In taking account of the *customer's* income (in accordance with *MCOB* 11.6.5R(2)(a)) for the purposes of its assessment of whether the *customer* will be able to pay the sums due:
- (1) a *firm* must obtain evidence of the income declared by the *customer* for the purposes of the *customer's* application for the *regulated mortgage contract* or *home purchase plan* (or variation). The evidence, whether document-based or derived through the use of automated systems, must be of a type and for a period which is adequate to support each element of income that the *firm* is taking into account, and subject to appropriate anti-fraud controls; and
  - (2) a *firm* must not accept self-certification of income by the *customer*, and the source of the evidence in (1) must be independent of the *customer*.
- 11.6.9 G In relation to taking account of the *customer's* income for the purposes of its assessment of whether the *customer* will be able to pay the sums due:
- (1) income may be derived from sources other than employment (such as pensions or investments), or from more than one job;
  - (2) the evidence necessary to comply with *MCOB* 11.6.8R will vary according to factors such as the employment status and the nature of the employment of the *customer* (for example, whether he is employed, self-employed, a contractor or retired), his length of employment and, in particular, any elements of income that are not contractually guaranteed. For example: income from overtime working may be evidenced by payslips over a period of time or by checking the level of income regularly paid into a bank account;
  - (3) for a self-employed *customer*, a *firm* may wish to consider using projections of future income, where these form part of a credible business plan;

- (4) a *firm* may use information it already holds about a *customer's* income, for example where the *customer* holds a current account with the *mortgage lender*;
- (5) the source of evidence may be independent of the *customer* even where it is supplied by the *customer*; for example, in the form of payslips, bank statements or tax returns;
- (6) a *firm* may use information provided to it by a *home finance intermediary* or other third party, including electronic sources of information, but the *firm* will retain responsibility for compliance with this chapter; and
- (7) *mortgage lenders* and *home purchase providers* are reminded of their obligations under SYSC 8 in respect of outsourcing where they choose to use a third party to verify income information.

#### Expenditure

- 11.6.10 R For the purposes of a *mortgage lender's* or *home purchase provider's* assessment of whether the *customer* will be able to pay the sums due:
- (1) the committed expenditure of a *customer* in MCOB 11.6.5R(2)(b)(i) is his credit and other contractual commitments which will continue after the *regulated mortgage contract* or *home purchase plan* (or variation) is entered into;
  - (2) the basic essential expenditure of a *customer's* household in MCOB 11.6.5R(2)(b)(ii) comprises expenditure for: housekeeping (food and washing); gas, electricity and other heating; water; telephone; council tax; buildings insurance; ground rent and service charge for leasehold properties; and essential travel (including to work or school); and
  - (3) the basic quality-of-living costs of a *customer's* household in MCOB 11.6.5R(2)(b)(ii) are its expenditure which is hard to reduce and gives a basic quality of life (beyond the absolute essential expenditure in (2)).
- 11.6.11 G (1) Examples of committed expenditure are: credit commitments such as loans and credit cards; hire purchase agreements; child maintenance; alimony; and the cost of a *repayment strategy* where the *customer* has an *interest-only mortgage* (where affordability has not been assessed on a capital and interest basis: see MCOB 11.6.48R (Assessing affordability under an interest-only mortgage)).
- (2) Examples of basic quality-of-living costs (which can be reduced, but only with difficulty) are: clothing; household goods (such as furniture and appliances) and repairs; personal goods (such as toiletries); basic recreation (television, some allowance for basic

recreational activities, some non-essential transport); and childcare.

- 11.6.12 R For the purposes of its assessment of whether the *customer* will be able to pay the sums due:
- (1) a *firm* may generally rely on any evidence of income or information on expenditure provided by the *customer* unless, taking a common sense view, it has reason to doubt the evidence or information;
  - (2) in taking account of the *customer's* committed expenditure, a *firm* must take reasonable steps to obtain details of the *customer's* actual outstanding commitments; and
  - (3) in taking account of the basic essential expenditure and basic quality-of-living costs of a *customer's* household, a *firm* may obtain details of the actual expenditure. Alternatively, it may use statistical data or other modelled data appropriate to the composition of the *customer's* household, including the *customer*, dependent children and other dependents living in the household. If it uses statistical or other modelled data a *firm* must apply realistic assumptions to determine the level of expenditure of the *customer's* household.
- 11.6.13 G (1) Examples of evidence of income in *MCOB* 11.6.12R(1) are payslips and bank statements.
- (2) If a *firm* obtains details of the *customer's* credit commitments from the *customer*, it should corroborate the information, for example by making a credit reference agency search or checking credit card or bank statements.
  - (3) Where the *customer's* credit or contractual commitments are due to end shortly after the *regulated mortgage contract* or *home purchase plan* (or variation) has been entered into, a *firm* should take a common sense approach to deciding whether to include those commitments in its assessment of whether the *customer* will be able to pay the sums due, according to such factors as the remaining term of the commitment and the magnitude of payments required under it.

#### Future changes to income and expenditure

- 11.6.14 R If a *firm* is, or should reasonably be aware from information obtained during the application process, that there will, or are likely to, be future changes to the income and expenditure of the *customer* during the term of the *regulated mortgage contract* or *home purchase plan*, the *firm* must take them into account when assessing whether the *customer* will be able to pay the sums due for the purposes of *MCOB* 11.6.2R.

- 11.6.15 G (1) Examples of future changes to income and expenditure in *MCOB 11.6.14R* are: reductions in income that may come about following the *customer's* retirement; where it is known that the *customer* is being made redundant; or where the *firm* is aware of another loan commitment that will become due during the term of the *regulated mortgage contract* or *home purchase plan*, such as an equity loan to assist in property purchase.
- (2) If the term of a *regulated mortgage contract* or *home purchase plan* would extend beyond the date on which the *customer* expects to retire (or, where that date is not known, the state pension age), a *firm* should take a prudent and proportionate approach to assessing the *customer's* income beyond that date. The degree of scrutiny to be adopted may vary according to the period of time remaining to retirement when the assessment is made. The closer the *customer* is to retiring, the more robust the evidence of the level of income in retirement should be. For example, where retirement is many years in the future, it may be sufficient merely to confirm the existence of some pension provision for the *customer* by requesting evidence such as a pension statement; where the *customer* is close to retirement, the more robust steps may involve considering expected pension income from a pension statement. In accordance with *MCOB 11.6.12R(1)*, a *firm* should take a common sense view when assessing any information provided by the *customer* on his expected retirement date.
- (3) Where an additional loan commitment is expected to become due during the term of the *regulated mortgage contract* or *home purchase plan*, the *mortgage lender* should assess whether the *regulated mortgage contract* or *home purchase plan* will remain affordable when the loan commitment becomes due, unless there is an appropriate repayment strategy in place to repay that loan, such as through the sale of the property which is the subject of the *regulated mortgage contract* or *home purchase plan*.

#### Debt consolidation and credit-impaired customers

- 11.6.16 R (1) This *rule* applies where:
- (a) a purpose of a *regulated mortgage contract* or *home purchase plan* (or variation) is debt consolidation; and
- (b) the *customer* is a *credit-impaired customer*.
- (2) Subject to (3), where each of the conditions in (1) is satisfied and, if the debts which are to be repaid using the sums raised by the *regulated mortgage contract* or *home purchase plan* (or variation) were not repaid, the transaction would not be affordable for the *customer*, the *firm* must take reasonable steps to ensure that, on completion of the transaction, those debts are actually repaid.

- (3) The requirement in (2) does not apply if the *firm* has assumed that the *customer's* existing debts which are to be repaid using the sums raised by the *regulated mortgage contract* or *home purchase plan* (or variation) will not in fact be repaid and, accordingly, include them as committed expenditure in the affordability assessment for the *customer*.

- 11.6.17 G The requirement in *MCOB* 11.6.16R(2) for reasonable steps may be satisfied by the *mortgage lender's*, or *home purchase provider's*, repaying the committed expenditure directly to the creditors concerned as a condition of granting the *regulated mortgage contract* or *home purchase plan*.

Considering the effect of future interest rate rises

- 11.6.18 R (1) Under *MCOB* 11.6.5R(4), in taking account of likely future interest rate increases for the purposes of its assessment of whether the *customer* will be able to pay the sums due, a *mortgage lender* must consider the likely future interest rates over a minimum period of five years from the expected start of the term of the *regulated mortgage contract* (or variation), unless the interest rate under the *regulated mortgage contract* is fixed for a period of five years or more from that time, or for the duration of the *regulated mortgage contract* (or variation), if less than five years.
- (2) A *mortgage lender* must be able to justify the basis it uses for determining likely future interest rates for the purposes of this *rule* by reference to market expectations.
- (3) For the purposes of this *rule*, even if the basis used by the *mortgage lender* in (2) indicates that interest rates are likely to fall, or to rise by less than 1%, during the first five years of the *regulated mortgage contract* (or variation), a *mortgage lender* must assume that interest rates will rise by a minimum of 1% over that period.

- 11.6.19 G In relation to *MCOB* 11.6.18R(2):
- (1) an example of market expectations is the forward sterling rate published on the Bank of England website. A *mortgage lender* should not use its own forecast; and
- (2) a *mortgage lender* should not link its determination to market expectations without considering the likely effect of rate changes in accordance with the market expectations on the specific *regulated mortgage contract* in question.

Responsible lending or financing policy

- 11.6.20 R A *firm* must put in place, and operate in accordance with, a written policy (which may be contained in more than one document), approved by its *governing body*, setting out the factors it will take into account in

assessing a *customer's* ability to pay the sums due. The policy must address the following matters:

- (1) how income and expenditure is to be assessed, including (except as provided in *MCOB* 11.6.32R(1) and *MCOB* 11.6.39R(1)):
  - (a) details of the types of income which are acceptable;
  - (b) the proportion of different income streams which is acceptable;
  - (c) how variations in income over time, of which the *firm* is aware, are to be considered;
  - (d) what is acceptable evidence of income (including the time period to be covered by the evidence); and
  - (e) how committed expenditure, basic essential expenditure and basic quality-of-living costs are taken into account when assessing affordability;
- (2) how future interest rates are taken into account when assessing affordability;
- (3) the calculations used to determine whether the *regulated mortgage contract* or *home purchase plan* is affordable;
- (4) how the *mortgage lender's* or *home purchase provider's* anti-fraud controls are incorporated into affordability assessments;
- (5) how the *mortgage lender's* or *home purchase provider's* method of calculating the size of the advance for each *customer*, based on a consideration of the *customer's* income and expenditure, is to be monitored, including the timing of reviews and key performance indicators to be used (see *MCOB* 11.6.22R (Monitoring));
- (6) the actions to be taken if the *mortgage lender's* or *home purchase provider's* calculation method, referred to in (5), does not perform as expected;
- (7) how regular audits of compliance with the *mortgage lender's* or *home purchase provider's* responsible lending or financing policy established in accordance with this *rule* are to be undertaken (as required by *MCOB* 11.6.24R);
- (8) how the record keeping requirements in *MCOB* 11.6.60R are to be met;
- (9) (if applicable) the matters required by *MCOB* 11.6.50R (Interest-only policy); and
- (10) (if applicable) how the *firm* will apply the *rules* in *MCOB* 11.7

(Transitional arrangements) so as to permit exceptions to its procedures for affordability assessments, to include arrangements for use of management information to monitor its application of those exceptions.

- 11.6.21 G Examples of different income streams in *MCOB* 11.6.20R(1)(b) are: income derived from sources other than employment; income from more than one job; and elements of income that are not contractually guaranteed.

#### Monitoring

- 11.6.22 R A *firm* must put in place, and be able to demonstrate that it has, robust systems and controls (including the use of management information and key performance indicators) to monitor the effectiveness of its affordability assessments, including in preventing payment difficulties.
- 11.6.23 G Except as provided in *MCOB* 11.6.32R(2) and *MCOB* 11.6.39R(2), the monitoring in *MCOB* 11.6.22R should:
- (1) include use of management information, key performance indicators and root cause analysis to review and (where appropriate) adjust and improve the *mortgage lender's* or *home purchase provider's* method of calculating the size of the advance for each *customer*, based on a consideration of the *customer's* income and expenditure; and
  - (2) take place on a regular basis. However, a *firm* should put in place key performance indicators that trigger more frequent reviews; for example, if the incidence of *customers* being in *arrears*, or of early *arrears*, is higher than expected.
- 11.6.24 R A *firm* must ensure that its compliance with the responsible lending or financing policy required by *MCOB* 11.6.20R is reviewed at least once per calendar year:
- (1) in any case where the *firm* has an internal audit function or outsourced equivalent, by that function; and
  - (2) in any other case, by the *firm's* internal compliance function or an outsourced equivalent.

#### Alternative provisions for loans which are solely for a business purpose

- 11.6.25 R Where a *regulated mortgage contract* is solely for a business purpose, a *firm* may opt to apply *MCOB* 11.6.26R to *MCOB* 11.6.31R in place of *MCOB* 11.6.5R to *MCOB* 11.6.19G.
- 11.6.26 R When assessing for the purposes of *MCOB* 11.6.2R whether a *customer* will be able to pay the sums due, a *firm*:

- (1) must not base its assessment of affordability on the equity in the property which is used as security under the *regulated mortgage contract*, or take account of an expected increase in property prices;
- (2) must:
  - (a) where the repayments will be made from the resources of the *customer*:
    - (i) take full account of the income, net of income tax and national insurance, or net assets (or both) of the *customer*; and the *customer's* committed expenditure; and
    - (ii) take account, in general terms as a minimum, of the basic essential expenditure and basic quality-of-living costs of the *customer's* household; and
  - (b) where the repayments will be made from the financial resources of the business, take full account of the strength of those resources;
- (3) in a case falling within (2)(b), if the *customer* is relying on the business for his personal income, must as a minimum consider in general terms whether the business can support the *customer's* basic essential expenditure and basic quality-of-living costs;
- (4) must assess affordability on the basis of both repayment of capital and payment of interest over the term, except where lending under an *interest-only mortgage* in accordance with *MCOB* 11.6.41R(1); and
- (5) must take account of the impact of likely future interest rate increases on affordability.

11.6.27 R For the purposes of *MCOB* 11.6.2R, a *firm* must not rely on a general declaration of affordability by the *customer* or his representative.

11.6.28 R In taking account (in accordance with *MCOB* 11.6.26R(2)) of the *customer's* income or net assets (or both) and the resources of the business for the purposes of its assessment of whether the *customer* will be able to pay the sums due:

- (1) a *firm* must obtain evidence of the income or net assets (or both) of the *customer* and the resources of the business, as declared by the *customer* for the purpose of the *customer's* application for the *regulated mortgage contract* (or variation); and
- (2) a *firm* must not accept self-certification of income by the *customer*, and the source of the evidence in (1) must be

independent of the *customer*.

- 11.6.29 R In *MCOB* 11.6.26R, for the purposes of taking full account of committed expenditure and taking account in general terms of basic essential expenditure and basic quality-of-living costs, the meaning of those phrases is as set out in *MCOB* 11.6.10R.
- 11.6.30 G The information which a *firm* should consider when taking account, for the purposes of *MCOB* 11.6.26(2)(b), of the strength of the financial resources of the business will vary according to the characteristics of the business, but may include factors such as the cash flow, assets and liabilities of the business.
- 11.6.31 R If a *firm* is, or should reasonably be aware from information obtained during the application process, that there will, or are likely to, be future changes to the income and expenditure of the *customer*, or the resources of the business, during the term of the *regulated mortgage contract*, the *firm* must take them into account when assessing whether the *customer* will be able to pay the sums due for the purposes of *MCOB* 11.6.2R.
- 11.6.32 R Where a *firm* chooses, in accordance with *MCOB* 11.6.25R, to apply the provisions of *MCOB* 11.6.26R to *MCOB* 11.6.31R in place of *MCOB* 11.6.5R to *MCOB* 11.6.19G:
- (1) its policy in *MCOB* 11.6.20R(1) need not address each of the matters prescribed in sub-paragraphs (a) to (e) of that *rule*;
  - (2) *MCOB* 11.6.23G does not apply; and
  - (3) in each case the record-keeping requirements in *MCOB* 11.6.60R(2)(a) to (d) apply only to the extent relevant, but the record in *MCOB* 11.6.60R(1) must also include, to the extent relevant:
    - (a) the *customer's* assets and the evidence relied on to assess them; and
    - (b) the details considered in relation to the resources of the business.

Alternative provisions for loans with high net worth mortgage customers

- 11.6.33 R Where a *regulated mortgage contract* is for a *high net worth mortgage customer*, a *firm* may opt to apply *MCOB* 11.6.34R to *MCOB* 11.6.38R in place of *MCOB* 11.6.5R to *MCOB* 11.6.19G.
- 11.6.34 R When assessing for the purposes of *MCOB* 11.6.2R whether a *customer* will be able to pay the sums due, a *firm*:
- (1) must not base its assessment of affordability on the equity in the property which is used as security under the *regulated mortgage*

*contract*, or take account of an expected increase in property prices;

- (2) must:
  - (a) take full account of the income, net of income tax and national insurance, or net assets (or both) of the *customer*; and the *customer's* committed expenditure; and
  - (b) take account, in general terms as a minimum, of the basic essential expenditure and basic quality-of-living costs of the *customer's* household;
- (3) must assess affordability on the basis of both repayment of capital and payment of interest over the term, except where lending under an *interest-only mortgage* in accordance with *MCOB* 11.6.41R(1); and
- (4) must take account of the impact of likely future interest rate increases on affordability.

- 11.6.35 R For the purposes of *MCOB* 11.6.2R, a *firm* must not rely on a general declaration of affordability by the *customer* or his representative.
- 11.6.36 R In taking account of the *customer's* income or net assets (or both) (in accordance with *MCOB* 11.6.34R(2)(a)) for the purposes of its assessment of whether the *customer* will be able to pay the sums due:
- (1) a *firm* must obtain evidence of the income or net assets (or both) declared by the *customer* for the purpose of the *customer's* application for the *regulated mortgage contract* (or variation); and
  - (2) a *firm* must not accept self-certification of income by the *customer*, and the source of the evidence in (1) must be independent of the *customer*.
- 11.6.37 R In *MCOB* 11.6.34R, for the purposes of taking full account of committed expenditure and taking account in general terms of basic essential expenditure and basic quality-of-living costs, the meaning of those phrases is as set out in *MCOB* 11.6.10R.
- 11.6.38 R If a *firm* is, or should reasonably be, aware from information obtained during the application process, that there will, or are likely to, be future changes to the income and expenditure of the *customer* during the term of the *regulated mortgage contract*, the *firm* must take them into account when assessing whether the *customer* will be able to pay the sums due for the purposes of *MCOB* 11.6.2R.
- 11.6.39 R Where a *firm* chooses, in accordance with *MCOB* 11.6.33R, to apply the provisions of *MCOB* 11.6.34R to *MCOB* 11.6.38R in place of *MCOB* 11.6.5R to *MCOB* 11.6.19G:

- (1) its policy in *MCOB* 11.6.20R(1) need not address each of the matters prescribed in sub-paragraphs (a) to (e) of that *rule*;
- (2) *MCOB* 11.6.23G does not apply; and
- (3) in each case the record-keeping requirements in *MCOB* 11.6.60R(2)(a) to (d) apply only to the extent relevant, but the record in *MCOB* 11.6.60R(1) must also include, to the extent relevant, the *customer's* assets and the evidence relied on to assess them.

#### Interest-only mortgages

- 11.6.40 G The rules in this part (*MCOB* 11.6.41R to *MCOB* 11.6.49R) provide that *interest-only mortgages* may be *entered into* by mortgage lenders in limited circumstances.

#### Entering into interest-only mortgages

- 11.6.41 R (1) A mortgage lender may only enter into an *interest-only mortgage*, or switch a *repayment mortgage* onto an interest-only basis for all or part of its term, if:
- (a) it has evidence that the *customer* will have in place a clearly understood and credible *repayment strategy*; and
  - (b) as far as it is reasonably able to assess at that time, the *repayment strategy* has the potential to repay the capital borrowed and any interest reasonably expected to be accrued under the *interest-only mortgage*.
- (2) In *MCOB* 11.6, a reference to an *interest-only mortgage* is to be read as including any *regulated mortgage contract* which includes an interest-only period or where part of the sum is advanced on an interest-only basis.
- (3) A mortgage lender must not accept speculative *repayment strategies* for the purposes of (1).
- 11.6.42 G *Firms* are reminded that:
- (1) *interest-only mortgages* include those where some, but not all, interest is payable at the end of the term. Accordingly, the requirement in *MCOB* 11.6.41R(1)(b) applies equally to such *interest-only mortgages* as it does to those where all of the interest is accrued until the end of the term; and
  - (2) a *lifetime mortgage* is a type of *interest-only mortgage*, as full repayment of capital and interest is not required over the term. Accordingly, the requirements in the *Handbook* (including in *MCOB* 11.6 and *MCOB* 11.7) which apply to *interest-only*

*mortgages* apply to *lifetime mortgages*, unless specifically disapplied. Depending always on its terms, a *lifetime mortgage* may also be an *interest roll-up mortgage*, as noted in *MCOB* 11.6.59G.

- 11.6.43 R *MCOB* 11.6.41R(1) does not prevent a *mortgage lender*, when appropriate, from making a temporary concession, by which he accepts payment of interest only, with a *customer* who is in *arrears* or has a *payment shortfall*, or is at risk of *arrears* or a *payment shortfall*, on a *regulated mortgage contract*.
- 11.6.44 G *Firms* are reminded that whether it is appropriate to take the action contemplated by *MCOB* 11.6.43R will depend on all the circumstances of the particular case and must be considered having regard to, among other things, *Principle 6* and the *rules* in *MCOB* 13.
- 11.6.45 G The following are examples of *repayment strategies* that may, subject to the circumstances of the *customer*, be acceptable for the purposes of *MCOB* 11.6.41R(1):
- (1) regular deposits into a savings or investment product;
  - (2) the periodic repayment of capital from irregular sources of income (such as bonuses or some sources of income from self-employment); and
  - (3) the sale of assets such as another property or other land owned by the *customer*.
- 11.6.46 E Acceptance by a *mortgage lender* of any of the following *repayment strategies* for the purposes of *MCOB* 11.6.41R(1) may be relied upon as tending to show contravention of that *rule*:
- (1) an expectation that the value of the property which is the subject of the *regulated mortgage contract* will increase over its term sufficiently to enable the *customer* to sell the property to repay the capital borrowed and, where applicable, pay the interest accrued under the *interest-only mortgage*;
  - (2) an intention on the part of the *customer* to utilise an expected, but uncertain, inheritance to repay the capital borrowed and, where applicable, pay the interest accrued under the *interest-only mortgage*; and
  - (3) the sale of the property which is the subject of the *regulated mortgage contract*, where that is the *customer's* main residence and the *mortgage lender* does not consider whether the property will have the potential to:
    - (a) provide sufficient funds for the *customer* to repay the capital borrowed and, where applicable, the interest accrued under the *interest-only mortgage*; and

- (b) allow the *customer* to purchase a cheaper property to reside in or execute any other associated strategy.

The above list is not exhaustive.

- 11.6.47 G In complying with *MCOB* 11.6.41R(1), where a *customer's repayment strategy* is the sale of the property which is the subject of the *regulated mortgage contract*, a *mortgage lender* may wish to consider, as part of its assessment of that *repayment strategy*, factors such as the equity in the property when considered in relation to the level of property prices in the relevant area at the time of the consideration or, for a *lifetime mortgage*, the borrower's life expectancy.

Assessing affordability under an interest-only mortgage

- 11.6.48 R For the purposes of *MCOB* 11.6.2R, where a *mortgage lender* is lending under an *interest-only mortgage* in accordance with *MCOB* 11.6.41R(1), it may assess affordability on the basis of payment of interest only over the term (plus repayment of such capital as may be due to be repaid over the term). If it does so, it must consider as part of the *customer's* committed expenditure under *MCOB* 11.6.5R(2)(b)(i) (or the equivalent alternative provision for transactions with *high net worth mortgage customers* or solely for business purposes) the cost to the *customer* of the *repayment strategy*.

Review during the term of interest-only mortgages

- 11.6.49 R (1) This *rule* applies in relation to all *interest-only mortgages* which a *mortgage lender enters into* on or after 26 April 2014 except:
- (a) *lifetime mortgages*;
  - (b) *bridging loans*; and
  - (c) any other case where the repayment of capital borrowed and, if applicable, interest accrued, is certain.
- (2) Except as set out in (3), a *mortgage lender* must carry out a review (as a minimum, once) during the term of the mortgage, in which contact is made with the *customer*, to check that the *customer's repayment strategy* is still in place, and that it is still reasonable to expect that the *repayment strategy* has the potential to repay the capital borrowed and, where applicable, pay the interest reasonably expected to be accrued under the *interest-only mortgage*. The review must be carried out at a stage of the term when, if the *repayment strategy* is not in place, or not adequate, there is likely to be sufficient time prior to the end of the term for the *customer* to take appropriate steps to remedy the situation.
- (3) The review in (2) is not required in any case where, despite reasonable efforts to contact the *customer*, the *mortgage lender* has

been unable to do so.

- (4) Following the review in (1), where appropriate the *mortgage lender* must take reasonable steps to discuss with the *customer* what may be done to address the situation.

#### Interest-only policy

- 11.6.50 R A *mortgage lender* which enters into *interest-only mortgages* (unless they are only *lifetime mortgages*) must include in the policy which is required by *MCOB* 11.6.20R (Responsible lending and financing policy) a policy on *interest-only mortgages*, setting out its processes and procedures for ensuring compliance with *MCOB* 11.6.41R(1) and for safeguarding the interests of *customers* during the term of *interest-only mortgages*. This policy must include:
- (1) details of the *mortgage lender's* plans for lending by way of *interest-only mortgages*, including its planned volumes of lending on that basis over a specified period, and provision for reviewing the actual volumes of lending on that basis, including the timing and method of review;
  - (2) specification of the types of *repayment strategy* which will be considered acceptable, and the evidential requirements and other controls which will be applied to ensure that only such types will be accepted, including the controls to be applied where the *repayment strategy* is the sale of the property which is the subject of the *regulated mortgage contract*;
  - (3) the procedures for checking the existence and adequacy of the *repayment strategy* in line with the policy, including questions to be asked of the *customer*;
  - (4) the arrangements for monitoring and auditing compliance with the policy, processes and procedures (see *MCOB* 11.6.22R and *MCOB* 11.6.24R (Monitoring)); and
  - (5) the process for the review required by *MCOB* 11.6.49R which, as a minimum:
    - (a) prescribes the timing of the review;
    - (b) prescribes the content of the review, including the questions to be asked of the *customer* and the actions to be taken if the *customer* proves difficult to contact or otherwise does not co-operate with the review;
    - (c) sets out how it is to be decided whether the *customer's repayment strategy* meets the criteria in *MCOB* 11.6.49R(2); and

- (d) sets out the actions which will be appropriate to be considered during the discussions in *MCOB 11.6.49R(2)*, depending on the circumstances of the *customer*.
- 11.6.51 G (1) The controls in *MCOB 11.6.50R(2)* may include, where appropriate: maximum loan to value limits; minimum equity requirements; regional factors such as property prices; or other eligibility requirements.
- (2) The policy and procedures for safeguarding the interests of a *customer* under an *interest-only mortgage* should not permit the *mortgage lender* to change the *interest-only mortgage* to a *repayment mortgage*, extend the term or otherwise change the features of the *interest-only mortgage* unless to do so is compatible with the duties of the *mortgage lender* under *Principle 6* and any other applicable *rules* and regulations, including those relating to *arrears* or *payment shortfall*. A *mortgage lender* should also have regard to the *Unfair Terms Regulations* when drafting the provisions of *regulated mortgage contracts* in relation to changes to their features.
- 11.6.52 G *MCOB 11.6.50R* sets out requirements for *mortgage lenders* to have appropriate procedures for managing *interest-only mortgages* in order to safeguard the interests of *customers*. *Firms* are reminded of the *rules* and *guidance* in *SYSC* (notably *SYSC 7.1*) relating to systems and controls for the management of risks to which *firms* themselves are exposed. *Firms* will need to consider whether their systems and controls are adequate in relation to the management of risks arising from *interest-only mortgages*.

#### Assessing the customer's repayment strategy for bridging loans

- 11.6.53 E For a *bridging loan* which is an *interest-only mortgage*, acceptance by a *mortgage lender* as a *repayment strategy* for the purposes of *MCOB 11.6.41R(1)* of an expectation that, by entering into the *bridging loan*, the *customer's* credit status will be sufficiently improved to enable him to refinance to a longer-term *regulated mortgage contract* (except where the *mortgage lender* has evidence of a guaranteed offer for such a longer-term contract) may be relied upon as tending to show contravention of that *rule*.
- 11.6.54 G For a *bridging loan* which is an *interest-only mortgage*, in complying with *MCOB 11.6.41R(1)*:
- (1) where the *customer's repayment strategy* is the sale of his existing home, the *mortgage lender* may wish to consider asking for it to be supported by an independent valuation of that property, as a condition of accepting that *repayment strategy*; and
- (2) where the *customer's repayment strategy* is the replacement of the *bridging loan* with a mainstream *regulated mortgage contract*, the *mortgage lender* should not accept that *repayment strategy* unless

it is reasonably satisfied that a mainstream *mortgage lender* will be willing to enter into a *regulated mortgage contract* with the *customer*. A *firm* may wish to consider requesting evidence of a guaranteed offer or agreement in principle that will be in place once the existing term of the *bridging loan* has expired, or obtain the necessary income and expenditure information, in order to be so satisfied.

#### Extending the term of a bridging loan

- 11.6.55 R Except in relation to a secured overdraft which is solely for a business purpose or is with a *high net worth mortgage customer*:
- (1) when considering extending the term of a *bridging loan*, a *mortgage lender* must comply with *MCOB* 11.6.2R as if the *bridging loan* were a new loan;
  - (2) where *MCOB* 11.6.2R does not apply in relation to extending the term of a *bridging loan* (because the *bridging loan* is an *interest roll-up mortgage*, and therefore *MCOB* 11.6.57R applies), the *mortgage lender* must consider with the *customer*, before he commits himself to extend the term, the impact of the extension on the *customer's* remaining equity in the property which is the subject of the *bridging loan*; and
  - (3) a *firm* must not agree to extend the term of a *bridging loan* unless the *customer* has made a positive choice to do so.
- 11.6.56 G *Firms* are reminded that, when extending the term of a *bridging loan* to which *MCOB* 11.6.55R does not apply, in accordance with *MCOB* 2.5A.1R, they must act honestly, fairly and professionally in accordance with the best interests of their *customer*.

#### Interest roll-up mortgages

- 11.6.57 R The requirements in *MCOB* 11.6.2R (and any *Handbook* provisions applicable only to that *rule*) do not apply in relation to an *interest roll-up mortgage*.
- 11.6.58 R A *mortgage lender* may not enter into an *interest roll-up mortgage*, or vary an existing *regulated mortgage contract* so that it becomes an *interest roll-up mortgage*, unless it is:
- (1) a *lifetime mortgage*; or
  - (2) a *bridging loan*; or
  - (3) a loan to a *high net worth mortgage customer*; or
  - (4) a loan solely for business purposes.

- 11.6.59 G *Firms* are reminded that an *interest roll-up mortgage* is a type of *interest-only mortgage*, where no payments of interest or capital are required or anticipated until the mortgage comes to an end. Depending always on their terms, it is possible to structure the types of product set out in *MCOB* 11.6.58R(1) to (4) as an *interest roll-up mortgage*. Where that is the case, *MCOB* 11.6.2R will not apply in relation to them, but *MCOB* 11.6.40G to *MCOB* 11.6.52G will apply to all *interest roll-up mortgages*, to the extent they are permitted by *MCOB* 11.6.58R.

## Record-keeping

- 11.6.60 R (1) A *firm* must make, in paper or electronic form, an adequate record of the steps it takes to comply with the *rules* in this chapter in relation to each *customer*.
- (2) The record in (1) must include the information taken into account in each affordability assessment, so that it is possible to understand from the record the basis of the *mortgage lender's* or *home purchase provider's* lending or financing decision, including (except as provided in *MCOB* 11.6.32R(3) and *MCOB* 11.6.39R(3)):
- (a) the *customer's* income, including, where relevant, a breakdown of the different income types;
  - (b) the *customer's* committed expenditure;
  - (c) the basic essential expenditure and basic quality-of-living costs of the *customer's* household (whether actual expenditure for that household or assumed expenditure from statistical or other modelled data, including information to show why the assumed data is appropriate to that *customer's* household);
  - (d) the evidence relied on to assess income and expenditure;
  - (e) the rate or assumptions used to test affordability against likely future interest rate rises;
  - (f) the repayment type and term of the *regulated mortgage contract*, or the term of the *home purchase plan*; and
  - (g) the calculation used to determine whether the *regulated mortgage contract, home purchase plan* is (or, where applicable, following the variation, remains) affordable for the *customer*.
- (3) In relation to *interest-only mortgages*, the record in (1) must include:
- (a) the reasons for each decision to offer an *interest-only*

*mortgage to a customer;*

- (b) the evidence of the *customer's repayment strategy* and, where applicable, its cost;
  - (c) details of the *firm's* attempts to contact the *customer* where required by *MCOB* 11.6.49R; and
  - (d) the outcome of each review required by *MCOB* 11.6.49R (whether conducted once during the term of the *interest-only mortgage* or more frequently).
- (4) In relation to the extension of the term of a *bridging loan* which falls within *MCOB* 11.6.55R, the record in (1) must include:
- (a) the *customer's* positive choice to extend the term;
  - (b) the reasons for the decision to extend the term; and
  - (c) the evidence of the *customer's repayment strategy* and its cost.
- (5) A *firm* must retain the records required by (1) to (4) for the term of the *regulated mortgage contract* or *home purchase plan*.
- (6) Where a *firm* enters into or varies a *regulated mortgage contract* or *home purchase plan* under *MCOB* 11.7 (Transitional arrangements), it must keep, for the term of the contract or plan, a record of:
- (a) the outstanding balance on the existing contract or plan;
  - (b) the cost of the repairs or maintenance work to the property, where relevant;
  - (c) any product fee or arrangement fee financed by any additional borrowing taken on under the contract or increase in the amount of finance provided under the plan; and
  - (d) the rationale for each decision made to enter into or vary a *regulated mortgage contract* or *home purchase plan* under *MCOB* 11.7 (Transitional arrangements), including why the *firm* considered it to be in the *customer's* best interests.
- (7) A *firm* must make, and keep up to date, an adequate record of the policy required by *MCOB* 11.6.20R. When the policy is changed, a record of the previous policy must be retained for so long as any *regulated mortgage contract* or *home purchase plan* to which it was applicable remains outstanding.

11.6.61 G For the purposes of *MCOB* 11.6.60R(2)(c) and (g), if it is not practicable

for the *firm* to record on the *customer's* file full details of the calculation method applied, it should record clearly which version of that method was applied in order that the file can be reviewed in conjunction with the applicable version of the method, so that it is possible to reconstruct the lending decision.

## 11.7 Transitional arrangements

- 11.7.1 R When considering *entering into* or varying a *regulated mortgage contract* or *home purchase plan*, a *firm* need not apply the rules in *MCOB* 11.6.2R to *MCOB* 11.6.18R inclusive (as modified by *MCOB* 11.6.25R to *MCOB* 11.6.31R and *MCOB* 11.6.33 to *MCOB* 11.6.38R, where applicable) if it has established, acting reasonably, that the following conditions are satisfied:
- (1) the *customer* has:
    - (a) an existing *regulated mortgage contract* (whether or not *entered into* on or after 31 October 2004) or *home purchase plan* (whether or not *entered into* on or after 6 April 2007) which was in existence prior to 26 April 2014; or
    - (b) an existing *regulated mortgage contract* or *home purchase plan* which was entered into in reliance on, and in compliance with, *MCOB* 11.7;
  - (2) subject to *MCOB* 11.7.2R, the proposed *regulated mortgage contract* or *home purchase plan*, or variation, would not involve the *customer* taking on additional borrowing (or, for a *home purchase plan*, increasing the amount of finance provided under the plan) beyond the amount currently outstanding under the existing *regulated mortgage contract* or *home purchase plan*, other than to finance any product fee or arrangement fee for the proposed new or varied contract;
  - (3) the proposed transaction would be in the *customer's* best interests; and
  - (4) the *customer* has not, after 26 April 2014 increased the size of the advance under the existing *regulated mortgage contract* or *home purchase plan* other than to finance any relevant product fee or arrangement fee in relation to, or the cost of essential repairs or maintenance to the property which is the subject of, that *regulated mortgage contract* or *home purchase plan*.
- 11.7.2 R The condition in *MCOB* 11.7.1R(2) does not apply if each of the following conditions is satisfied:
- (1) the *firm* is the *mortgage lender* or *home purchase provider* under

- the existing *regulated mortgage contract* or *home purchase plan* in *MCOB 11.7.1R(1)*;
- (2) the value of the property which is the subject of the *regulated mortgage contract* or *home purchase plan* is at risk if repairs or maintenance work to the property are not carried out;
  - (3) the funds generated by the additional borrowing or increase in finance provided are to be used to carry out the repairs or maintenance work; and
  - (4) the *firm* has obtained credible evidence which demonstrates that the additional borrowing or increase in finance are no more than the cost of the repairs or maintenance work.
- 11.7.3 R (1) When considering *entering into* or varying an *interest-only mortgage*, a *mortgage lender* need not apply the rules in *MCOB 11.6.41R(1)*, *MCOB 11.6.49R*, *MCOB 11.6.50R* and *MCOB 11.6.60R(3)* if the conditions in *MCOB 11.7.1R* are satisfied, and if it has established, acting reasonably, that the existing *regulated mortgage contract* in *MCOB 11.7.1R(1)* is an *interest-only mortgage*.
- (2) Where only part of the sum advanced under the existing *regulated mortgage contract* is on an interest-only basis, (1) applies, but only to that part.
- 11.7.4 G In accordance with its obligation under *Principle 6* to treat its *customers* fairly, a *firm* should not treat a *customer* with whom it enters into or varies a *regulated mortgage contract* or *home purchase plan* pursuant to this section 11.7 less favourably than it would treat other *customers* with similar characteristics, for example by offering less favourable interest rates or other terms.
- 11.7.5 G *Firms* should note the record-keeping requirements at *MCOB 11.6.60R(6)* which apply when *regulated mortgage contracts* and *home purchase plans* are *entered into* or varied under this section.

Amend the following as shown.

## 12.1 Application

...

What?

...

- 12.1.4 R The ~~arrears~~ *payment shortfall* charges and excessive charges requirements in this chapter will continue to apply to a *firm* after a *regulated mortgage contract* has come to an end following the sale of a *repossessed* property.

The excessive charges requirements will continue to apply to a *firm* after a *home reversion plan* has ended. References in this chapter to ‘customer’ will include references to a former *customer* as appropriate.

- 12.1.5 G The *FSA* will expect a *firm* to ensure that charges made to a *customer* arising from the sale of a *repossessed* property and charges arising in relation to a *sale shortfall* are not excessive and are subject to the same considerations as apply with respect to ~~arrears~~ payment shortfall charges under this chapter.

...

#### 12.4 **Arrears Payment shortfall charges: regulated mortgage contracts**

- 12.4.1 R (1) A *firm* must ensure that any *regulated mortgage contract* that it enters into does not impose, and cannot be used to impose, a charge or charges for ~~arrears~~ a payment shortfall on a *customer* ~~except where that~~ unless the *firm* is able objectively to justify that the charge is equal to or lower than a reasonable estimate calculation of the cost of the additional administration required as a result of the *customer* being in arrears having a payment shortfall.
- (2) ~~Paragraph (1) does not prevent a *firm* from entering into a regulated mortgage contract with a *customer* under which the *firm* may change the rate of interest charged to the *customer* from a fixed or discounted rate of interest to the *firm*'s standard variable rate if the *customer* goes into arrears, providing that this standard variable rate is not a rate created especially for *customers* in arrears.~~ [deleted]
- 12.4.1A E The imposition of a charge for ~~arrears~~ a payment shortfall on a *customer* who is adhering to an arrangement under which the *customer* and the *firm* agree that the *customer* will make payments of a set amount per month (or other agreed period) on agreed dates may be relied upon as tending to show contravention of *MCOB* 12.4.1R(1).
- 12.4.1B R When a *customer* has a ~~payment shortfall~~ payment shortfall in respect of a *regulated mortgage contract*, a *firm* must ensure that any payments received from the *customer* are allocated first towards paying off the balance of the ~~shortfall~~ payment shortfall (excluding any interest or charges on that balance).
- 12.4.2 G For each type of payment shortfall charge (for example, a monthly arrears management charge), ~~A~~ a *firm* may calculate the same level of ~~arrears charges~~ additional administration costs and payment shortfall charges for all *regulated mortgage contracts* where the *customer* is in ~~arrears~~ payment shortfall, rather than performing a calculation on the basis of the individual *regulated mortgage contract* with the particular *customer*.

- 12.4.3 G *Firms* are also subject to requirements on information provision and standards relating to *arrears* and *repossessions* (see *MCOB 13* (Arrears and repossessions)).
- 12.4.4 R In calculating the cost of the additional administration required as a result of a customer having a payment shortfall, a firm must not take into account:
- (1) the following types of costs:
    - (a) funding or capital;
    - (b) general bank charges that are not incurred as a result of a customer having a payment shortfall;
    - (c) unrecovered fees;
    - (d) advertising costs; and
    - (e) regulatory fines;
  - (2) the costs of preparing financial reports for the firm unless there is an objectively justifiable reason to do so and the costs relate solely to the analysis and management of accounts in payment shortfall;
  - (3) executive staff costs unless there is an objectively justifiable reason to do so and the costs relate to the day-to-day management of customers in payment shortfall.
- 12.4.5 R In MCOB 12.4, 'executive staff' means the staff or business owners responsible for the management of the firm's business.
- 12.4.6 G
- (1) For some firms, their executive staff will be the executive board members.
  - (2) Executive staff costs relating to company strategy, including payment shortfall strategy, should not be included as costs relating to the day-to-day management of customers in payment shortfall.
  - (3) General financial reporting costs, including all legal and regulatory reporting costs, should not be included as costs relating solely to the analysis and management of accounts in payment shortfall.
- 12.4.7 G In calculating the cost of the additional administration required as a result of a customer having a payment shortfall, the firm:
- (1) may, where appropriate, take into account the following types of costs:
    - (a) providing information or documents;

- (b) non-executive staff costs;
- (c) premises costs;
- (d) human resources costs; and
- (e) information technology costs;

- (2) should consider the extent to which the cost of the additional administration is shared with the rest of its business; and
- (3) should, where a type of cost is absent from the lists in (1) and at MCOB 12.4.4R(1), before taking it into account, consider whether it is appropriate to do so.

12.4.8     R     A firm must not impose a charge for a payment shortfall that is calculated as a proportion of the outstanding loan.

...

## **12.6     Business loans and loans to high net worth mortgage customers: tailored provisions**

12.6.1     G     *Firms are reminded that, in relation to a regulated mortgage contract which is solely for a business purpose or is with a high net worth mortgage customer in circumstances where MCOB 7.7.1R applies, if there is a new early repayment charge or a change to the existing early repayment charge, MCOB 7.7.1R(2) requires a firm to notify the customer within five business days of the maximum amount payable as an early repayment charge.*

12.6.2     G     *Firms are also reminded that in accordance with MCOB 1.2.3R, they should either comply in full with MCOB, but in doing so may opt to take account of or comply with all tailored provisions in MCOB that relate to business loans solely for a business purpose or loans to high net worth mortgage customers.*

...

## **13        Arrears, payment shortfalls and repossessions: regulated mortgage contracts and home purchase plans**

### **13.1     Application**

...

What?

...

13.1.5     G     The FSA expects a firm to treat a sale shortfall in the same way that it

treats a ~~payment shortfall~~ payment shortfall.

...

### 13.3 Dealing fairly with customers ~~in arrears~~ with a payment shortfall: policy and procedures

...

- 13.3.1 R (1) A *firm* must deal fairly with any *customer* who:
- (a) ~~is in arrears~~ has a *payment shortfall* on a regulated mortgage contract or home purchase plan;

...

...

- 13.3.1A R (1) Where a *customer* has a *payment shortfall* in relation to a *regulated mortgage contract* or *home purchase plan*, a *firm* must not attempt to process more than two direct debit requests in any one calendar month.
- (2) Where a *firm's* direct debit request, in respect of a *customer* who has a *payment shortfall* on a *regulated mortgage contract* or *home purchase plan*, has been refused, on at least one occasion in each of two consecutive months, due to insufficient funds, the *firm* must:
- (a) consider whether the method of payment remains suitable for the *customer*;
- (b) make reasonable efforts to contact the *customer* to discuss whether the method of payment remains suitable for the *customer*; and
- (c) not pass on any costs to the *customer* which were incurred as a consequence of presenting direct debit requests during this period of consideration.

- 13.3.1B G *MCOB* 13.3.1AR(2)(c) does not prevent a *firm* from attempting to process up to two direct debit requests in any one calendar month provided the *firm* has made reasonable efforts to contact the *customer* and the *customer* has failed to respond.

...

- 13.3.2A R 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~~ *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~~ payment shortfall or *sale shortfall*;
- (3) allow a reasonable time over which the ~~payment shortfall~~ 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*;

...

...

13.3.4A R In complying with *MCOB* 13.3.2AR(6):

- (1) a *firm* must consider whether, given the individual circumstances of the *customer*, it is appropriate to do one of more of the following in relation to the *regulated mortgage contract* or *home purchase plan* with the agreement of the *customer*:

...

- (d) treat the ~~payment shortfall~~ payment shortfall as if it was part of the original amount provided (but a *firm* must not automatically capitalise a ~~payment shortfall~~ payment shortfall where the impact would be material); or

...

...

13.3.4AA R In *MCOB* 13.3.4AR, the impact of a capitalisation would be material if, either on its own or taken together with previous automatic capitalisations, it increased:

- (1) the interest payable over the term of the *regulated mortgage contract* by £50 or more; or
- (2) the contractual monthly repayment amount under the *regulated mortgage contract* by £1 or more.

13.3.4B R ...

...

13.3.4D G In the *FSA*'s view, in order to comply with *Principle 6*, *firms* should not agree to capitalise a ~~payment shortfall~~ payment shortfall save where no other option is realistically available to assist the *customer*.

...

- 13.3.6 G In relation to adopting a reasonable approach to the time over which the ~~payment shortfall~~ payment shortfall or sale shortfall should be repaid, the FSA takes the view that the determination of a reasonable payment period will depend upon the individual circumstances. In appropriate cases this will mean that repayments are arranged over the remaining term.

...

Record keeping: ~~arrears~~ payment shortfalls and repossessions

- 13.3.9 R (1) A mortgage lender or administrator must make and retain an adequate record of its dealings with a customer whose account ~~is in arrears~~ has a payment shortfall or ~~who has~~ a sale shortfall, which will enable the firm to show its compliance with this chapter. That record must include a recording of all telephone conversations between the firm and the customer which discuss ~~the sums due~~ any amount in arrears or any amount subject to payment shortfall charges.
- (2) A mortgage lender or administrator must retain the record required by (1) for three years from the date of the dealing.

- 13.3.10 G The record referred to in MCOB 13.3.9R should contain, or provide reference to, matters such as:
- (1) the date of first communication with the customer, after the account was identified as ~~being in arrears~~ having a payment shortfall;
  - (2) in relation to correspondence issued to a customer ~~in arrears~~ with a payment shortfall, the name and contact number of the employee dealing with that correspondence, where known;
  - (3) the basis for issuing tailored information in accordance with MCOB 13.7.1R in relation to a loan solely for a business purpose;
  - (4) information relating to any new payment arrangements proposed;
  - (5) the date of issue of any legal documents;
  - (6) the arrangements made for sale after the repossession (whether legal or voluntary); ~~and~~
  - (7) the date of any communication summarising the customer's outstanding debt after sale of the *repossessed* property; and
  - (8) the date and time of each call for the purposes of MCOB 13.3.9R(1).

...

#### 13.4 Arrears: provision of information to the customer of a regulated mortgage contract

13.4.1 R If a *customer* falls into *arrears* on a *regulated mortgage contract*, a *firm* must as soon as possible, and in any event within 15 *business days* of becoming aware of that fact, provide the *customer* with the following in a *durable medium*:

...

(3) the total sum of the ~~payment shortfall~~ payment shortfall;

(4) the charges incurred as a result of the ~~payment shortfall~~ payment shortfall;

...

(6) an indication of the nature (and where possible the level) of charges the *customer* is likely to incur unless the ~~payment shortfall~~ payment shortfall is cleared.

...

13.4.3 G (1) ...

(2) Where a *firm* provides the information in *MCOB* 13.4.1R when a ~~payment shortfall~~ payment shortfall occurs but before the *customer's* account falls into *arrears*, it need not repeat the provision of the information in *MCOB* 13.4.1R when the *customer's* account falls into *arrears*.

Customer in arrears within the past 12 months

13.4.4 R If a *customer's* account has previously fallen into *arrears* within the past 12 months (and at that time the *customer* received the disclosure required by *MCOB* 13.4.1R), the *arrears* have been cleared and the *customer's* account falls into *arrears* on a subsequent occasion a *firm* must either:

(1) ...

(2) provide, as soon as possible, and in any event within 15 *business days* of becoming aware of the further *arrears*, a statement, in a *durable medium*, of the payments due, the actual ~~payment shortfall~~ payment shortfall, any charges incurred and the total outstanding debt excluding any charges that may be added on redemption, together with information as to the consequences, including *repossession*, if the ~~payment shortfall~~ payment shortfall is not cleared.

...

**13.5 Dealing with a customer in arrears or with a sale shortfall on a regulated mortgage contract**

## Statement of charges

- 13.5.1 R Where an account is in *arrears*, and the ~~payment shortfall~~ payment shortfall or *sale shortfall* is attracting charges, a *firm* must provide the *customer* with a regular written statement (at least once a quarter) of the payments due, the actual ~~payment shortfall~~ payment shortfall, the charges incurred and the debt.
- 13.5.2 G ...
- (3) ~~If an account in *arrears* is subject to a payment plan agreed between a *firm* and a *customer*, and the account is operating in accordance with that plan, the *firm* will still need to send the *customer* a written statement if the payment shortfall or *sale shortfall* is attracting charges.~~ [deleted]
- (4) Information provided should cover the period since the last statement. *Firms* may use the annual statement to comply with *MCOB* 13.5.1R, in which case the annual statement will need to be supplemented to include the actual ~~payment shortfall~~ payment shortfall.

...

### 13.7 **Business loans and loans to high net worth mortgage customers: tailored provisions**

- 13.7.1 R Where the *regulated mortgage contract* is for a business purpose or is with a high net worth mortgage customer, a *firm* may as an alternative to *MCOB* 13.4.1R(1) provide the following information in a *durable medium* instead of the *Money Advice Service* information sheet "Problems paying your mortgage":
- (1) details of the consequences if the ~~payment shortfall~~ payment shortfall is not cleared;
- (2) a description of the options available to the *customer* for clearing the ~~payment shortfall~~ payment shortfall; and
- (3) (in the case only of loans for a business purpose) details of sources of fee-free advice for business *customers*.
- 13.7.2 G *Firms* are reminded that in accordance with *MCOB* 1.2.3R, they should ~~either~~ comply in full with *MCOB*, but in doing so may opt to take account of or comply with all tailored provisions in *MCOB* that relate to ~~business loans~~ solely for a business purpose or loans to high net worth mortgage customers. Therefore, a *firm* may only follow the relevant tailored provisions in *MCOB* 13.7, if it also follows all other relevant tailored provisions in *MCOB*. In either case, the rest of *MCOB* applies in full.

...

**Schedule 1 Record keeping requirements**

...

Sch 1.3 G

<b>Handbook reference</b>	<b>Subject of record</b>	<b>Contents of record</b>	<b>When record must be made</b>	<b>Retention period</b>
<u>MCOB 1.2.9CR(1)</u>	<u>A high net worth mortgage customer</u>	Evidence of satisfaction of definition of <u>high net worth mortgage customer</u>	<u>When it is used or obtained</u>	Three years from when obtained or, if later, used
<u>MCOB 1.2.9CR(2)</u>	<u>A high net worth mortgage customer</u>	Written statement confirming the <u>customer is a high net worth mortgage customer</u>	<u>When it is used or obtained</u>	Three years from when obtained or, if later, used
<u>MCOB 1.2.9DR</u>	<u>A loan solely for a business purpose</u>	<u>Business plan</u>	<u>When it is used or obtained</u>	Three years from when obtained or, if later, used
<u>MCOB 1.2.9ER</u>	<u>A professional customer</u>	Evidence of satisfaction of definition of <u>professional customer</u>	<u>When it is used or obtained</u>	Three years from when obtained or, if later, used
...				
<u>MCOB 4.4A.23G</u>	<u>Disclosures</u>	<u>Appropriate records of disclosures required by section 4.4A</u>	<u>When disclosure made</u>	<u>As required by SYSC 9</u>
<u>MCOB 4.7.17R (1)(a)</u>	<u>Suitability</u>	Details of the customer information obtained, including the <u>customer's needs and circumstances, for the purpose of assessing the suitability of a regulated mortgage contract</u>	<u>When the personal recommendation is made</u>	Three years
<u>MCOB 4.7.17R (1)(b)</u>	<u>Suitability</u>	An explanation of the reasons why the <u>firm believes the personal recommendation complies with the suitability</u>	<u>When the personal recommendation is made</u>	Three years

		requirements in <i>MCOB 4.7.4 R(1)</i>		
<i>MCOB 4.7.17R (1)(b)</i>	Suitability	An explanation of the reasons why a <i>personal recommendation</i> has been made on a basis other than that described in <i>MCOB 4.7.13E(1)</i>	When the <i>personal recommendation</i> is made	Three years
<i>MCOB 4.8.7R</i>	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
<i>MCOB 4.6.11R</i>	Notice of cancellation	A record of the fact that notice has been given (including the original notice instructions and a copy of any receipt of notice issued)	When the <i>firm</i> first becomes aware that notice has been served	Three years
<i>MCOB 4.7A.25R (1)(a)</i>	<u>Suitability of regulated mortgage contracts</u>	<u>Customer information obtained for the purposes of assessing suitability of a regulated mortgage contract</u>	<u>When advice given</u>	<u>Three years</u>
<i>MCOB 4.7A.25R (1)(b)</i>	<u>Suitability of regulated mortgage contracts</u>	<u>An explanation of why the firm has concluded its advice is suitable</u>	<u>When advice given</u>	<u>Three years</u>
<i>MCOB 4.7A.25R (1)(c)</i>	<u>Rolling-up of fees or charges into loan</u>	<u>The customer's positive choice to add fees or charges to the sum advanced</u>	<u>When choice made</u>	<u>Three years</u>
<i>MCOB 4.8A.18R (1)(a)</i>	<u>Execution-only sales of regulated mortgage contracts</u>	<u>Information provided by the customer about the regulated mortgage contract he wishes to purchase.</u>	<u>The date a regulated mortgage contract was entered into or arranged</u>	<u>Three years</u>
<i>MCOB 4.8A.18R (1)(b)</i>	<u>Execution-only sales of regulated mortgage</u>	<u>The warning to the customer in a durable medium regarding his lack of protection of</u>	<u>The date a regulated mortgage contract was entered into or</u>	<u>Three years</u>

	<u>contracts</u>	<u>the rules on assessing suitability</u>	<u>arranged</u>	
<u>MCOB 4.8A.18R (1)(c)</u>	<u>Execution-only sales of regulated mortgage contracts</u>	<u>The customer's confirmation of his positive election to proceed with an execution-only sale</u>	<u>The date a regulated mortgage contract was entered into or arranged</u>	<u>Three years</u>
<u>MCOB 4.8A.18R (1)(d)</u>	<u>Execution-only sales of regulated mortgage contracts</u>	<u>Details of advice rejected.</u>	<u>The date a regulated mortgage contract was entered into or arranged</u>	<u>Three years</u>
<u>MCOB 4.8A.18R (3)</u>	<u>Execution-only sales of regulated mortgage contracts</u>	<u>The firm's policy for managing execution-only sales</u>	<u>When the policy is made</u>	<u>One year from when the policy is changed</u>
<u>MCOB 4.10.9BR</u>	<u>Execution-only sales of home purchase plans</u>	<u>Information provided by the customer about the home purchase plan he wishes to purchase; the warning to the customer in a durable medium regarding his lack of protection of the rules on assessing suitability; the customer's confirmation of his positive election to proceed with an execution-only sale.</u>  <u>The firm's policy for managing execution-only sales</u>	<u>The date a home purchase plan was entered into or arranged</u>  <u>When the policy is made</u>	<u>Three years</u>  <u>One year from when the policy is changed</u>
<u>MCOB 4.10.13R(1) (a)</u>	<u>Suitability of home purchase plans</u>	<u>Customer information obtained for the purposes of assessing suitability of a home purchase plan</u>	<u>When advice given</u>	<u>Three years</u>
<u>MCOB 4.10.13R(1) (b)</u>	<u>Suitability of home purchase plans</u>	<u>An explanation of why the firm has concluded its advice is suitable</u>	<u>When advice given</u>	<u>Three years</u>
<u>MCOB 4.10.13R(1) (c)</u>	<u>Advice on home purchase plans</u>	<u>Any advice rejected, including the reasons rejected and details of any home purchase plan the customer has</u>	<u>When advice given</u>	<u>Three years</u>

		<u>proceeded with as an execution-only sale</u>		
...				
<i>MCOB</i> 4.11.8R	<i>Customer</i> information on which an assessment of the <u>affordability and appropriateness suitability and basis of advice</u> for a <i>regulated sale and rent back agreement</i> was based	<i>Customer</i> information on his income, expenditure, resources, needs, objectives and individual circumstances	The date on which the <i>firm</i> <del>reached a conclusion on affordability and appropriateness</del> <u>assessed suitability</u>	Five years, or one year after the end of the fixed term of the tenancy agreement, if later
...				
<i>MCOB</i> 8.5.22R(1) (a)	Suitability	Details of the customer information obtained, including the <i>customer's</i> needs and circumstances, for the purpose of assessing the suitability of a <i>equity release transaction</i>	When the <i>personal recommendation</i> is made	Three years
<i>MCOB</i> 8.5.22R(1) (b)	Suitability	An explanation of the reasons why the <i>firm</i> believes the <i>personal recommendation</i> complies with suitability requirements in <i>MCOB</i> 8.5.4R(1)	When the <i>personal recommendation</i> is made	Three years
<i>MCOB</i> 8.5.22R(1) (b)	Suitability	An explanation of the reasons why a <i>personal recommendation</i> has been made on a basis other than that described in <i>MCOB</i> 8.5.17E(1)	When the <i>personal recommendation</i> is made	Three years
<i>MCOB</i> 8.3.1R(1)	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
<i>MCOB</i> 8.3.1R(1)	Notice of cancellation	A record of the fact that notice has been given (including the original notice instructions and a copy of any receipt of notice issued)	When the <i>firm</i> first becomes aware that notice has been served	Three years
<i>MCOB</i> 8.5A.19R (1)(a)	<u>Suitability of equity release transactions</u>	<u>Customer information obtained for the purposes of assessing suitability of an equity release transaction</u>	<u>When advice given</u>	<u>Three years</u>
<i>MCOB</i> 8.5A.19R (1)(b)	<u>Suitability of equity release transactions</u>	<u>An explanation of why the firm has concluded its advice is suitable</u>	<u>When advice given</u>	<u>Three years</u>
<i>MCOB</i> 8.5A.19R (1)(c)	<u>Advice on equity release transactions</u>	<u>Any advice rejected, including the reasons rejected and details of any regulated mortgage contract the customer has proceeded with as an execution-only sale</u>	<u>When advice given</u>	<u>Three years</u>
<i>MCOB</i> 8.5A.19R (1)(d)	<u>Rolling-up of fees or charges into loan</u>	<u>The customer's positive choice to add fees or charges to the sum advanced</u>	<u>When choice made</u>	<u>Three years</u>
<i>MCOB</i> 8.6A.9R	<u>Execution-only sales of equity release transactions</u>	<u>Information provided by the customer about the equity release transaction he wishes to purchase; the warning to the customer in a durable medium regarding his lack of protection of the rules on assessing suitability; the customer's confirmation of his positive election to proceed with an execution-only sale; any advice from the firm which the customer rejected,</u>	<u>The date a home purchase plan was entered into or arranged</u>	<u>Three years</u>

		<u>including the reasons why it was rejected.</u>		
...				
<i>MCOB</i> 11.3.1R(2)	Ability of the <i>customer</i> to repay advance	Evidence to demonstrate that the <i>firm</i> has taken into account the <i>customer's</i> ability to repay	When the assessment of the <i>customer's</i> ability to repay is made	One year from the date on which the <i>regulated mortgage contract</i> is entered into, or the further advance provided
<i>MCOB</i> 11.3.4R(2)	Responsible lending policy	A record of the <i>firm's</i> written policy setting out the factors the <i>firm</i> will take into account in assessing the <i>customer's</i> ability to repay	The date on which the policy is set	One year from the date on which the policy is replaced
<i>MCOB</i> <u>11.6.60R(1) to (4)</u>	<u>Responsible lending and financing</u>	<u>Steps taken to comply with rules including: information taken into account in each affordability assessment; in relation to <i>interest-only mortgages</i>, the reasons for the offer decision, evidence relating to the <i>customer's</i> repayment strategy, details of the <i>firm's</i> attempts to contact the <i>customer</i> and the outcome of each mid-term review; information relating to the extension of the term of <i>bridging loans</i> which are neither with a <i>high net worth mortgage customer</i> nor or a secured overdraft solely for a business purpose</u>	<u>When <i>regulated mortgage contract</i> or <i>home purchase plan</i> (or variation) is entered into, or the mid-term review takes place</u>	<u>The term of the contract or plan</u>
<i>MCOB</i> 11.6.60R(6) (a)	<u>Transitional arrangements</u>	<u>The outstanding balance on the existing contract</u>	<u>When new contract or variation is entered into</u>	<u>For the term of the <i>regulated</i></u>

				<u>mortgage contract or home purchase plan</u>
<u>MCOB 11.6.60R(6)(b)</u>	<u>Transitional arrangements</u>	<u>The cost of repairs or maintenance work to the property</u>	<u>When new contract or variation is entered into</u>	<u>For the term of the regulated mortgage contract or home purchase plan</u>
<u>MCOB 11.6.60R(6)(c)</u>	<u>Transitional arrangements</u>	<u>Any product fee or arrangement fee financed by any additional borrowing or increase in finance</u>	<u>When new contract or variation is entered into</u>	<u>For the term of the regulated mortgage contract or home purchase plan</u>
<u>MCOB 11.6.60R(6)(d)</u>	<u>Transitional arrangements</u>	<u>The rationale for each decision to enter into or vary a contract under MCOB 11.7</u>	<u>When new contract or variation is entered into</u>	<u>For the term of the regulated mortgage contract or home purchase plan</u>
<u>MCOB 11.6.60R(7)</u>	<u>Responsible lending and financing policy</u>	<u>The firm's policy, setting out the factors it will take into account in assessing a customer's ability to pay the sums due</u>	<u>When the policy is made</u>	<u>For so long as any regulated mortgage contract or home purchase plan to which it was applicable remains outstanding.</u>
<u>MCOB 13.3.9R</u>	<u>Dealings with customers <del>in arrears</del> with a payment shortfall, or with a mortgage sale shortfall <del>debt</del></u>	<u>Details of all dealings with the customer (including a recording of all telephone conversations which discuss any arrears or any amount subject to payment shortfall charges); information relating to any repayment plan; date of issue of any legal</u>	<u>The date of the dealing</u>	<u>Three years from the date on which the record is made</u>

		proceedings; arrangements made for sale of a <i>repossessed</i> property; and the basis of any tailored information where the loan is for a business purpose.		

**Part 2: Comes into force on 26 October 2012**

**11.8 Customers unable to change regulated mortgage contract, home purchase plan or provider**

11.8.1 E Where a *customer* is unable to:

- (1) enter into a new *regulated mortgage contract* or *home purchase plan* or vary the terms of an existing *regulated mortgage contract* or *home purchase plan* with the existing *mortgage lender* or *home purchase provider*; or
- (2) enter into a new *regulated mortgage contract* or *home purchase plan* with a new *mortgage lender* or *home purchase provider*;

the existing *mortgage lender* or *home purchase provider* should not (for example, by offering less favourable interest rates or other terms) take advantage of the *customer's* situation or treat the *customer* any less favourably than it would treat other *customers* with similar characteristics. To do so may be relied on as tending to show contravention of *Principle 6* (Customers' interests).

## Annex E

## Amendments to the Supervision manual (SUP)

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

## 16 Annex 18BG

**NOTES FOR COMPLETION OF  
THE RETAIL MEDIATION ACTIVITIES RETURN ('RMAR')**

...

**Section G: Training & Competence ('T&C')**

...

**Section G: guide for completion of individual fields**

...	
What types of advice were provided?	For each type of advice, the <i>firm</i> should indicate whether or not staff have provided advice on that basis / business type. <u>In relation to their <i>home finance mediation activities</i>, firms are not required by MCOB 4.4A to use a label to describe the service they provide to customers. In filling out this section they should simply answer 'no' for each category relating to their <i>home finance mediation activities</i>.</u>
...	
Independent (whole of market plus option of fee-only)	To hold itself out as acting independently, a <i>firm</i> carrying on <i>home finance mediation activity</i> must consider products from across the whole of the market, and offer its clients the opportunity to pay by fee ( <del>MCOB 4.3.7R</del> ).
...	

## Annex F

### Amendments to the Professional Firms sourcebook (PROF)

In this Annex, striking through indicates deleted text.

#### 5.3 Reference to other sourcebooks or manuals

...

Mortgages: Conduct of business sourcebook

...

5.3.8 *MCOB* 1.2.10R provides that *MCOB* does not apply to an *authorised professional firm* with respect to its *non-mainstream regulated activities* except for *MCOB* 2.2 (Clear, fair and not misleading communication); and *MCOB* 3 (Financial promotion) ~~and to a limited extent *MCOB* 4.4 (Initial disclosure requirements).~~

## Annex G

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

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

#### 4.4 What is a regulated mortgage contract?

...

Type of lending

- 4.4.11 G The definition of *regulated mortgage contract* also covers a variety of types of product. Apart from the normal mortgage loan for the purchase of property, the definition also includes other types of secured loan, such as secured overdraft facility, a ~~secured bridging loan~~ bridging loan, a secured credit card facility and *regulated lifetime mortgage contracts* under which the borrower (usually an older person) takes out a loan where repayment of the capital (and in some cases the interest) is not required until the property is sold, usually on the death of the borrower.



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Made rules – Prudential sourcebook  
for Mortgage and Home Finance  
Firms, and Insurance Intermediaries  
(Non-Bank Lenders)  
Instrument 2012

**PRUDENTIAL SOURCEBOOK FOR MORTGAGE AND HOME FINANCE FIRMS,  
AND INSURANCE INTERMEDIARIES (NON-BANK LENDERS)  
INSTRUMENT 2012**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of:
- (1) the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
    - (a) section 138 (General rule-making power);
    - (b) section 156 (General supplementary powers);
    - (c) section 157(1) (Guidance); and
  - (2) the other powers and related provisions listed in Schedule 4 (Powers exercised) to the General Provisions of the Handbook.
- B. The rule-making powers referred to above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force on 26 April 2014.

**Amendments to the Handbook**

- D. The Glossary of definitions is amended in accordance with Annex A to this instrument.
- E. The Prudential sourcebook for Mortgage and Home Finance Firms, and Insurance Intermediaries (MIPRU) is amended in accordance with Annex B to this instrument.

**Citation**

- F. This instrument may be cited as the Prudential Sourcebook for Mortgage and Home Finance Firms, and Insurance Intermediaries (Non-Bank Lenders) Instrument 2012.

By order of the Board  
27 September 2012

## Annex A

## Amendments to the Glossary of definitions

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

<i>exposure</i>	<p>...</p> <p>(2) (in accordance with Article 77 of the <i>Banking Consolidation Directive</i> and for the purposes of the calculation of the <i>credit risk capital component</i> and the <i>counterparty risk capital component</i> (including <i>BIPRU 3</i> (Standardised credit risk), <i>BIPRU 4</i> (The IRB approach), <i>BIPRU 5</i> (Credit risk mitigation), <del>and</del> <i>BIPRU 9</i> (Securitisation) <u>or for the purposes of the calculation of the credit risk capital requirement in <i>MIPRU 4.2</i> (Capital resources requirement)</u>) an asset or off-balance sheet item.</p> <p>...</p>
<i>risk weight</i>	<p>(in relation to an <i>exposure</i>) a degree of risk expressed as a percentage assigned to that <i>exposure</i> in accordance with:</p> <p>(a) whichever is applicable of the <i>standardised approach</i> to credit risk and the <i>IRB approach</i>, including (in relation to a <i>securitisation position</i>) under <i>BIPRU 9</i> (Securitisation); <u>or</u></p> <p>(b) <u>(for a <i>firm</i> to which <i>MIPRU 4</i> applies), <i>MIPRU 4.2A.10R</i> to <i>MIPRU 4.2A.13R</i>.</u></p>
<i>risk weighted exposure amount</i>	<p>(in relation to an <i>exposure</i>) the value of an <i>exposure</i> for the purposes of the calculation of <u>(in the case of a <i>BIPRU firm</i>) the <i>credit risk capital component</i> or (in the case of a <i>firm</i> to which <i>MIPRU 4</i> applies) the <i>credit risk capital requirement</i> under <i>MIPRU 4.2A.4R</i>, in both cases after application of a <i>risk weight</i>.</u></p>
<i>securitisation</i>	<p>...</p> <p>(2) (in accordance with Article 4(36) of the <i>Banking Consolidation Directive</i> (Definitions), <del>and</del> in <i>BIPRU</i> <u>and</u> <i>MIPRU 4</i>) a transaction or scheme whereby the credit risk associated with an <i>exposure</i> or pool of <i>exposures</i> is <i>tranchéd</i> having the following characteristics:</p> <p>(a) payments in the transaction or scheme are dependent upon the performance of the <i>exposure</i> or pool of <i>exposures</i>; and</p> <p>(b) the subordination of <i>tranches</i> determines the distribution of <i>losses</i> during the ongoing life of the</p>

transaction or scheme.

*sponsor*

...

- (2) (in *BIPRU*), in accordance with Article 4(42) of the *Banking Consolidation Directive (Definitions)* and in *MIPRU 4* and in relation to a *securitisation* within the meaning of paragraph (2) of the definition of *securitisation*, an *undertaking* other than an *originator* that establishes and manages an *asset backed commercial paper programme* or other *securitisation* scheme that purchases *exposures* from third party entities.

## Annex B

**Amendments to the Prudential sourcebook for Mortgage and Home Finance Firms, and Insurance Intermediaries (MIPRU)**

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

## 4.2 Capital resources requirements

### Applicable guidance within BIPRU

- 4.2.-1 G Unless otherwise specified, where MIPRU 4.2 to MIPRU 4.2D refers to a guidance provision contained in BIPRU, a firm should regard that guidance provision as applying to it in the same way that that provision applies to a BIPRU firm.

### General solvency requirement

- 4.2.1 R A firm must at all times ensure that it is able to meet its liabilities as they fall due.
- 4.2.1A G Specific liquidity requirements for a firm carrying on any home financing or home finance administration connected to regulated mortgage contracts are set out in MIPRU 4.2D.

...

- 4.2.10 R Table: Application of capital resources requirements

	<b>Regulated activities</b>	<b>Provisions</b>
1.	(a) <i>insurance mediation activity</i> ; or (b) <i>home finance mediation activity</i> (or both); and no other <i>regulated activity</i> .	MIPRU 4.2.11R
2.	(a) <i>home financing</i> <u>not connected to regulated mortgage contracts</u> ; or (b) <i>home financing</i> and <i>home finance administration</i> ( <u>not connected to regulated mortgage contracts</u> ); and no other <i>regulated activity</i> .	MIPRU 4.2.12R to MIPRU 4.2.17E
...		

6.	<u>Any combination of regulated activities not within rows 1 to 5.</u>	<u>MIPRU 4.2.22R [deleted]</u>
7.	<u>(a) home financing connected to regulated mortgage contracts; or (b) home financing and home finance administration connected to regulated mortgage contracts; and no other regulated activity.</u>	<u>MIPRU 4.2.23R</u>
8.	<u>any combination of regulated activities not within rows 1 to 7.</u>	<u>MIPRU 4.2.22R</u>

4.2.10A G MIPRU 4.2.12R to MIPRU 4.2.23R have the effect that a firm carrying on any home financing or home finance administration which is connected to regulated mortgage contracts will be subject to different capital requirements to a firm that carries on those activities without connection to regulated mortgage contracts. To identify which of the rules in MIPRU 4.2.12R to MIPRU 4.2.23R is applicable, a firm should consider which regulated activities it performs as part of its home financing and home finance administration activities and determine whether any of those regulated activities (no matter what proportion) are connected to regulated mortgage contracts.

...

Capital resources requirement: home financing and home finance administration not connected to regulated mortgage contracts (~~but not home finance administration only~~)

4.2.12 R (1) The capital resources requirement for a firm carrying on only home financing which is not connected to regulated mortgage contracts, or home financing and home finance administration which is not connected to regulated mortgage contracts (and no other regulated activity) is the higher of:

- (a) £100,000; and
- (b) 1% of:
  - (i) its total assets plus total undrawn commitments and unreleased amounts under the *home reversion plan*; less
  - (ii) excluded loans or amounts plus intangible assets (see Note 1 in the table in MIPRU 4.4.4R).

...

...

## Capital resources requirement: home finance administration only

- 4.2.18 R The capital resources requirement for a *firm* carrying on *home finance administration* only, which has all or part of the *home finance transactions* that it administers on its balance sheet, is: ~~the amount which is applied to a firm carrying on home financing or home financing and home finance administration (and no other regulated activity) (see MIPRU 4.2.12R)~~
- (1) in the case of a firm carrying on only home finance administration which is not connected to regulated mortgage contracts, the amount which is applied to a firm under MIPRU 4.2.12R; or
- (2) in the case of a firm carrying on any home finance administration which is connected to regulated mortgage contracts, the amount which is applied to a firm under MIPRU 4.2.23R.

...

## Capital resources requirement: insurance mediation activity and home financing or home finance administration

- 4.2.20 R The capital resources requirement for a *firm* carrying on *insurance mediation activity* and *home financing* or *home finance administration* is the sum of ~~the requirements which are applied to the firm by:~~
- (1) the capital resources requirement rule for a *firm* carrying on *insurance mediation activity* or *home finance mediation activity* (and no other *regulated activity*) (see MIPRU 4.2.11R); and
- (2) (a) in the case of a firm carrying on home financing which is not connected to regulated mortgage contracts, or home finance administration which is not connected to regulated mortgage contracts, the capital resources requirement rule for a firm carrying on home financing or home financing and home finance administration (and no other regulated activity) (see amount which is applied to a firm under MIPRU 4.2.12R); or
- (aa) in the case of a firm carrying on any home financing which is connected to regulated mortgage contracts or any home finance administration that it administers on its balance sheet which is connected to regulated mortgage contracts, the amount which is applied to a firm under MIPRU 4.2.23R; or
- (b) ~~if, in addition to its insurance mediation activity, the firm carries~~ in the case of a firm carrying on home finance administration with all the assets home finance transactions that it administers off balance sheet, the capital resources rule for such amount which is applied to a firm (see under MIPRU 4.2.19R).

## Capital resources requirement: home finance mediation activity and home

financing or home finance administration

- 4.2.21 R (1) If a *firm* carrying on *home finance mediation activity* and *home financing* or *home finance administration* does not hold *client money* or other *client assets* in relation to its *home finance mediation activity*, the capital resources requirement is ~~the amount applied to a firm, according to the activities carried on by the firm, by:~~
- (a) in the case of a firm carrying on home financing which is not connected to regulated mortgage contracts or home finance administration which is not connected to regulated mortgage contracts, the capital resources requirement rule for a firm carrying on home financing or home financing and home finance administrator (and no other regulated activity) (see amount applied to a firm under MIPRU 4.2.12R); or
  - (aa) in the case of a firm carrying on any home financing which is connected to regulated mortgage contracts or any home finance administration that it administers on its balance sheet which is connected to regulated mortgage contracts, the amount applied to a firm under MIPRU 4.2.23R; or
  - (b) if, in addition to its home finance mediation activity, the firm carries in the case of a firm carrying on home finance administration with all the assets home finance transactions that it administers off balance sheet, the amount applied to a firm under capital resources rule for such a firm (see MIPRU 4.2.19R).

...

Capital resources requirement: other combination of activities

- 4.2.22 R The capital resources requirement for a *firm* carrying on any other combination of *regulated activities* which is not set out in MIPRU 4.2.10R to MIPRU 4.2.21R and MIPRU 4.2.23R is: the amount which is applied to a firm carrying on insurance mediation activity and home financing or home finance administration (see MIPRU 4.2.20R)
- (1) if the combination of regulated activities includes carrying on any home financing connected to regulated mortgage contracts or home finance administration connected to regulated mortgage contracts, the sum of the amounts which are applied to a firm under:
    - (a) MIPRU 4.2.20R(1); and
    - (b) MIPRU 4.2.23R; or
  - (2) in all other cases, the sum of the amounts which are applied to a firm under:

- (a) MIPRU 4.2.20R(1); and
- (b) MIPRU 4.2.12R.

Capital resources requirement: home financing and home finance administration connected to regulated mortgage contracts

- 4.2.23 R The capital resources requirement for a *firm* carrying on any *home financing* which is connected to *regulated mortgage contracts*, or *home financing and home finance administration* which is connected to *regulated mortgage contracts* (and no other *regulated activity*), is the higher of:
- (1) £100,000; and
  - (2) the sum of:
    - (a) the credit risk capital requirement calculated in accordance with MIPRU 4.2A; and
    - (b) 1% of:
      - (i) its total assets plus total undrawn commitments and unreleased amounts under the *home reversion plan*; less
      - (ii) intangible assets (see Note 1 in the table in MIPRU 4.4.4R) plus loans, *securitisation positions* and *CIU* positions subject to MIPRU 4.2A.4R.

After MIPRU 4.2 insert the following new sections. The text is not underlined.

**4.2A Credit risk capital requirement**

Application

- 4.2A.1 R This section applies to a *firm* to which MIPRU 4.2.23R applies.

Purpose

- 4.2A.2 G The purpose of MIPRU 4.2A is to:
- (1) set out how a *firm* should calculate its credit risk capital requirement;
  - (2) set out how a *firm* should calculate its *risk weighted exposure amounts* for *exposures* on its balance sheet; and
  - (3) identify which provisions of BIPRU 3 will apply to a *firm*, in addition to the provisions of MIPRU 4.2A, to enable it to make those calculations.

- 4.2A.3 G A *firm* should refer to *BIPRU 5* (as amended by *MIPRU 4.2C.3R*) with regard to the effect of *credit risk mitigation* on the calculation of *risk weighted exposure amounts*.

Calculation of credit risk

- 4.2A.4 R The credit risk capital requirement of a *firm* is 8% of the total of its *risk weighted exposure amounts* for *exposures* that:

- (1) are on its balance sheet; and
- (2) derive from:
  - (a) a loan entered into; or
  - (b) a *securitisation position* originated; or
  - (c) a *CIU* position entered into;
 on or after 26 April 2014; and
- (3) have not been deducted from the *firm's* capital resources under *MIPRU 4.4.4R*;

calculated in accordance with *MIPRU 4.2A*.

- 4.2A.5 R Any arrangements entered into on or after [date to be confirmed] which increase the amount of a loan already advanced or change the security to a loan already advanced or change the contractual terms (other than if the *firm* is exercising forbearance) of a loan already advanced will be subject to the credit risk capital requirement under *MIPRU 4.2A.4R(2)(a)* provided that, where the arrangements only increase the amount of a loan already advanced, such requirement shall only apply to the amount of such increase.

- 4.2A.5A G The arrangements excluded from the credit risk capital requirement include:

- (1) a loan acquired by a *firm* after 26 April 2014 if that loan was made before 26 April 2014;
- (2) arrangements made as a result of forbearance procedures, including:
  - (a) a change in the basis of interest payments from variable to fixed rate; or
  - (b) a change from a repayment mortgage to interest only; or
  - (c) the capitalisation of interest which increases the principal outstanding, where there is no element of new borrowing.

- 4.2A.6 R The *exposure* value of an asset item must be its balance sheet value.

4.2A.7 R When calculating *risk weighted exposure amounts*, a firm must comply with *BIPRU 3.2.3R*, *BIPRU 3.2.9R* to *BIPRU 3.2.19G*, and *BIPRU 3.2.38R* in the same way that these provisions apply to a *BIPRU firm*, except to the extent that a provision is modified or excluded in the table in *MIPRU 4.2A.8R*.

4.2A.8 R This table belongs to *MIPRU 4.2A.7R*

<b><i>BIPRU</i> provision</b>	<b>Adjustment</b>
All provisions of <i>BIPRU 3.2</i>	A reference to a provision of <i>BIPRU 3</i> , <i>BIPRU 5</i> or <i>BIPRU 9</i> must be read in conjunction with <i>MIPRU 4.2A.8R</i> , <i>MIPRU 4.2B.3R</i> and <i>MIPRU 4.2C.3R</i>
All provisions of <i>BIPRU 3.2</i>	All references to <i>capital resources</i> in <i>BIPRU 3.2</i> are replaced by references to capital resources calculated under <i>MIPRU 4.4</i>
<i>BIPRU 3.2.14G</i>	The last two sentences do not apply
<i>BIPRU 3.2.38R</i>	The references to <i>BIPRU 14</i> , <i>BIPRU 13.3.13R</i> and <i>BIPRU 13.8.8R</i> (Exposure to a central counterparty) do not apply
<i>BIPRU 3.2.10R</i> and <i>BIPRU 3.2.19G</i>	The references to €1m are replaced by references to £1m.

4.2A.9 R For the purposes of applying a *risk weight*, the *exposure* value must be multiplied by the *risk weight* determined in accordance with *MIPRU 4.2A.10R*, *MIPRU 4.2A.11R*, *MIPRU 4.2A.12R* or *MIPRU 4.2A.13R*.

4.2A.10 R To calculate *risk weighted exposure amounts* on *exposures* secured by mortgages on residential property, *risk weights* must be applied to all such *exposures*, unless deducted from capital resources calculated under *MIPRU 4.4*, in accordance with *BIPRU 3.4.56R* to *BIPRU 3.4.88G*.

4.2A.11 R To calculate *risk weighted exposure amounts* on *exposures* in *CIUs*, *risk weights* must be applied to all such *exposures*, unless deducted from capital resources under *MIPRU 4.4*, in accordance with *BIPRU 3.4.114R* to *BIPRU 3.4.125R*.

4.2A.12 R *Risk weighted exposure amounts* for *securitised exposures* must be calculated in accordance with *MIPRU 4.2B*.

4.2A.13 R To calculate *risk weighted exposure amounts* on *exposures* other than those provided for in *MIPRU 4.2A.10R* to *MIPRU 4.2A.12R*, *risk weights* must be applied to all such *exposures*, unless deducted from capital resources calculated under *MIPRU 4.4*, in accordance with *BIPRU 3.5.5G* as though that provision were a *rule*.

- 4.2A.14 G Rather than *risk weighting exposures* individually under *MIPRU 4.2A.13R*, a *firm* should apply a single *risk weight* to all *exposures* in each *exposure* class.
- 4.2A.15 R If a *firm* calculates *risk weighted exposure amounts* under *MIPRU 4.2A.13R* and is directed by *BIPRU 3.5.5G* to the “normal rules”, it must, in the calculation of those *risk weighted exposure amounts*, comply with *BIPRU 3.4* in the same way that that section applies to a *BIPRU firm*.
- 4.2A.16 R *Exposures* must be assigned a *risk weight* of 100% if *MIPRU 4.2A.10R* to *MIPRU 4.2A.13R* do not set out a calculation for *risk weighted exposure amounts* applicable to that *exposure*.
- 4.2A.17 R A *firm* must apply *BIPRU 3.4.96R* to *BIPRU 3.4.102R* to all past items due.
- 4.2A.18 G A *firm* may apply *BIPRU 3.5.6G* and *BIPRU 3.5.7G* to *exposures*. *MIPRU 4.2C* sets out the amendments to the *BIPRU 5 rules* referenced within these provisions.

## 4.2B Securitisation

### Application

- 4.2B.1 R This section applies to a *firm* to which *MIPRU 4.2.23R* applies.

### Purpose

- 4.2B.2 G The purpose of *MIPRU 4.2B* is to set out:
- (1) how a *firm* that is required to calculate the credit risk capital requirement under *MIPRU 4.2.23R* should calculate the *risk weighted exposure amounts* for *securitisation positions*; and
  - (2) the requirements that investors, *originators* and *sponsors* of *securitisations* on the balance sheet will have to meet (*BIPRU 9.3.1AR* and *BIPRU 9.3.15R* to *BIPRU 9.3.20R*).

### Calculation of risk weighted exposure amount for securitisation positions

- 4.2B.3 R To calculate the *risk weighted exposure amount* for *securitisation positions*, a *firm* must comply with *BIPRU 9* in the same way that that section applies to a *BIPRU firm*, except to the extent that a provision of *BIPRU 9* is modified or excluded in the table in *MIPRU 4.2B.4R*.
- 4.2B.4 R This table belongs to *MIPRU 4.2B.3R*

<i>BIPRU</i> provision	Adjustment
All sections of	All references to <i>capital resources</i> in <i>BIPRU 9</i> are replaced by references to capital resources calculated

<i>BIPRU 9</i>	under <i>MIPRU 4.4</i>
All sections of <i>BIPRU 9</i>	A reference to a provision of <i>BIPRU 3</i> , <i>BIPRU 5</i> or <i>BIPRU 9</i> must be read in conjunction with <i>MIPRU 4.2A.8R</i> , <i>MIPRU 4.2B.4R</i> and <i>MIPRU 4.2C.4R</i>
<i>BIPRU 9.1.1R</i>	This <i>rule</i> does not apply
<i>BIPRU 9.1.2G</i>	This provision does not apply
<i>BIPRU 9.1.8AG(3)</i>	The words “and these should be taken into account under the <i>overall Pillar 2 rule</i> ” do not apply
<i>BIPRU 9.1.9G</i>	This provision does not apply
<i>BIPRU 9.1.10G</i>	This provision does not apply
<i>BIPRU 9.2</i>	This section does not apply
<i>BIPRU 9.3.7R</i> to <i>BIPRU 9.3.14R</i>	These <i>rules</i> do not apply
<i>BIPRU 9.3.15R</i>	The first sentence of this <i>rule</i> is amended to read as follows: “A <i>firm</i> , whether acting as <i>sponsor</i> or <i>originator</i> , must apply the same sound and well defined criteria used for credit granting in respect of <i>exposures</i> held on its balance sheet to <i>exposures</i> to be securitised.”
<i>BIPRU 9.3.16R</i>	This <i>rule</i> is amended to read as follows: “A <i>firm</i> must apply the same standards of analysis to <i>exposures</i> under <i>BIPRU 9.3.15R</i> regardless of whether it has purchased or originated those <i>exposures</i> .”
<i>BIPRU 9.3.17R</i>	Where a <i>firm</i> is an <i>originator</i> , it must comply with this <i>rule</i> as it applies to a <i>credit institution</i>
<i>BIPRU 9.3.18R</i>	Where a <i>firm</i> is an <i>originator</i> or <i>sponsor</i> of a <i>securitisation</i> , it must comply with this <i>rule</i> in the same way that it applies to a <i>credit institution</i>
<i>BIPRU 9.3.19R</i>	Where a <i>firm</i> is an <i>originator</i> or <i>sponsor</i> of a <i>securitisation</i> , it must comply with this <i>rule</i> in the same way that it applies to a <i>credit institution</i>
<i>BIPRU 9.3.21G</i>	This provision does not apply
<i>BIPRU 9.3.22G</i>	This provision does not apply
<i>BIPRU 9.4.1R</i>	This <i>rule</i> is amended to read as follows: “The <i>originator</i> of a <i>traditional securitisation</i> may exclude <i>securitised exposures</i> from the calculation of <i>risk</i>

	<i>weighted exposure amounts and expected loss amounts if significant credit risk associated with the securitised exposures has been transferred to third parties and the transfer complies with the conditions in BIPRU 9.4.2R to BIPRU 9.4.10R.</i> ”
<i>BIPRU 9.4.11R to BIPRU 9.4.18G</i>	These provisions do not apply
<i>BIPRU 9.5.1R(1)</i>	This <i>rule</i> is amended to read as follows: “An <i>originator</i> of a <i>synthetic securitisation</i> may calculate <i>risk weighted exposure amounts</i> , and, as relevant, <i>expected loss amounts</i> , for the <i>securitised exposures</i> in accordance with <i>BIPRU 9.5.3R</i> and <i>BIPRU 9.5.4R</i> , if significant credit risk has been transferred to third parties, either through funded or unfunded credit protection, and the transfer complies with the conditions in (2) – (5).”
<i>BIPRU 9.5.1R(3)</i>	The reference to <i>BIPRU 4.10</i> (Credit risk mitigation under the IRB approach) does not apply
<i>BIPRU 9.5.1R(6)</i>	This <i>rule</i> does not apply
<i>BIPRU 9.5.1R(7)</i>	This <i>rule</i> does not apply
<i>BIPRU 9.5.1AG to BIPRU 9.5.1FG</i>	These provisions do not apply
<i>BIPRU 9.5.3R(1)</i>	The reference to <i>BIPRU 9.9 to BIPRU 9.14</i> is replaced by a reference to <i>BIPRU 9.9 to BIPRU 9.11</i> The reference to <i>BIPRU 3</i> is replaced by a reference to <i>MIPRU 4.2A</i> The reference to <i>BIPRU 4</i> (IRB approach) does not apply
<i>BIPRU 9.5.3R(2)</i>	This <i>rule</i> does not apply
<i>BIPRU 9.5.4R</i>	The reference to <i>BIPRU 9.9 to BIPRU 9.14</i> is replaced by a reference to <i>BIPRU 9.9 to BIPRU 9.11</i>
<i>BIPRU 9.5.7R</i>	The reference to <i>BIPRU 4.10</i> (Credit risk mitigation under the IRB approach) does not apply
<i>BIPRU 9.5.8R</i>	The reference to <i>BIPRU 9.9 to BIPRU 9.14</i> is replaced by a reference to <i>BIPRU 9.9 to BIPRU 9.11</i>
<i>BIPRU 9.6.8G</i>	This provision does not apply
<i>BIPRU 9.7.3G</i>	This provision does not apply

<i>BIPRU 9.8.1R</i>	The reference to <i>BIPRU 9</i> is replaced by a reference to <i>MIPRU 4.2B</i>
<i>BIPRU 9.8.2R</i>	The reference to <i>BIPRU 9</i> is replaced by a reference to <i>MIPRU 4.2B</i>
<i>BIPRU 9.8.7R</i>	The references to <i>BIPRU 4.10</i> (Credit risk mitigation under the IRB approach) do not apply
<i>BIPRU 9.9.1R</i>	The reference to <i>BIPRU 9.9</i> to <i>BIPRU 9.14</i> is replaced by a reference to <i>BIPRU 9.9</i> to <i>BIPRU 9.11</i>
<i>BIPRU 9.9.2R</i>	The reference to <i>BIPRU 9.9</i> to <i>BIPRU 9.14</i> is replaced by a reference to <i>BIPRU 9.9</i> to <i>BIPRU 9.11</i>
<i>BIPRU 9.9.4R(2)</i>	This <i>rule</i> does not apply
<i>BIPRU 9.9.5R</i>	This <i>rule</i> does not apply
<i>BIPRU 9.9.6R</i>	The reference to <i>BIPRU 9.14</i> does not apply
<i>BIPRU 9.9.7R</i>	The reference to <i>BIPRU 4.10</i> (Credit risk mitigation under the IRB approach) and the reference to <i>BIPRU 9.14</i> do not apply
<i>BIPRU 9.9.9R</i>	The words “subject to the provisions of <i>GENPRU</i> that deal with the deduction of <i>securitisation positions</i> at stage M in the relevant <i>capital resources table</i> ” do not apply
<i>BIPRU 9.10.1R</i>	The references to the <i>IRB approach</i> do not apply
<i>BIPRU 9.10.2R</i>	This <i>rule</i> does not apply
<i>BIPRU 9.10.3R</i>	The reference to <i>BIPRU 9.12.8R</i> does not apply
<i>BIPRU 9.10.4R</i> to <i>9.10.7R</i>	These <i>rules</i> do not apply
<i>BIPRU 9.12</i>	This section does not apply
<i>BIPRU 9.13</i>	This section does not apply
<i>BIPRU 9.14</i>	This section does not apply
<i>BIPRU 9.15</i>	This section does not apply

- 4.2B.5 G Subject to *BIPRU 9.3.6G*, for the purposes of *BIPRU 9.4.1R* and *BIPRU 9.5.1R* the transfer of credit risk to third parties should only be considered significant if the proportion of risk transferred is broadly commensurate with, or exceeds, the proportion by which *risk weighted exposure amounts*

are reduced.

4.2B.6 G For measuring the reduction in risk and *risk weighted exposure amounts*, an *originator* should assess the *securitisation positions* it holds against the underlying *exposures* as if they had never been *securitised*.

4.2B.7 G An *originator* should use an appropriate method, consistent with its own internal processes, to assess whether the risk transferred is significant.

4.2B.8 G If the result of:

(1) applying a *risk weight* of 1250% to all positions that an *originator* holds in the *securitisation*; or

(2) deducting all those positions from capital resources;

is a reduction in the *originator's* capital requirement compared to the capital requirements that would apply had it not transferred the *securitised exposures*, then the *originator* may treat the risk transferred as significant for the purposes of *BIPRU 9.4.1R* and *BIPRU 9.5.1R*.

## 4.2C Credit risk mitigation

### Application

4.2C.1 R This section applies to a *firm* to which *MIPRU 4.2.23R* applies where that *firm* wishes to apply *credit risk mitigation* to the calculation of its *risk weighted exposure amounts* under *MIPRU 4.2A*.

### Purpose

4.2C.2 G The purpose of *MIPRU 4.2C* is to set out which provisions of *BIPRU 5* a *firm* should comply with in the recognition of *credit risk mitigation* in the calculation of *risk weighted exposure amounts* for the purposes of the calculation of the credit risk capital requirement under *MIPRU 4.2.23R*.

### General

4.2C.3 R A *firm* that wishes to recognise *credit risk mitigation* in the calculation of *risk weighted exposure amounts*, must comply with *BIPRU 5* in the same way that that section applies to a *BIPRU firm*, except to the extent that a provision of *BIPRU 5* is modified or excluded in the table in *MIPRU 4.2C.4R*.

4.2C.4 R This table belongs to *MIPRU 4.2C.3R*

<b><i>BIPRU</i> provision</b>	<b>Adjustment</b>
All provisions of <i>BIPRU 5</i>	A reference to a provision of <i>BIPRU 3</i> , <i>BIPRU 5</i> or <i>BIPRU 9</i> must be read in conjunction with

	<i>MIPRU 4.2A.8R, MIPRU 4.2B.4R and MIPRU 4.2C.4R</i>
<i>BIPRU 5.1</i>	This section does not apply
<i>BIPRU 5.3.2R</i>	The words “without prejudice to <i>BIPRU 5.6.1R</i> ” do not apply
<i>BIPRU 5.4.1R</i>	This rule does not apply
<i>BIPRU 5.4.8R</i>	This rule does not apply
<i>BIPRU 5.4.16R</i>	This rule does not apply
<i>BIPRU 5.4.18R</i>	The second sentence of this <i>rule</i> does not apply The words “ <i>BIPRU 5.4.19R</i> to <i>BIPRU 5.4.21R</i> ” are replaced by the words “ <i>BIPRU 5.4.21R</i> ”
<i>BIPRU 5.4.19R</i>	This <i>rule</i> does not apply
<i>BIPRU 5.4.20R</i>	This <i>rule</i> does not apply
<i>BIPRU 5.4.22R</i>	The reference to <i>BIPRU 5.4.20R</i> does not apply
<i>BIPRU 5.4.23R</i> to <i>BIPRU 5.4.66R</i>	These provisions do not apply. A <i>firm</i> must only use the <i>financial collateral simple method</i>
<i>BIPRU 5.6</i>	This section does not apply
<i>BIPRU 5.7.4R</i>	This <i>rule</i> does not apply
<i>BIPRU 5.7.12R</i>	This <i>rule</i> does not apply
<i>BIPRU 5.7.19R</i>	This <i>rule</i> does not apply
<i>BIPRU 5.7.23R</i>	The words “ <i>BIPRU 3.2.20R</i> to <i>BIPRU 3.2.26R</i> ” are replaced by the words “ <i>MIPRU 4.2A.8R</i> to <i>MIPRU 4.2A.11R</i> and <i>MIPRU 4.2A.14R</i> ”
<i>BIPRU 5.7.23R(3)</i>	The first clause of this <i>rule</i> is amended to read as follows: “E is the <i>exposure</i> value according to <i>MIPRU 4.2A.5R</i> and <i>BIPRU 3.2.3R</i> ; The second clause of this <i>rule</i> does not apply
<i>BIPRU 5.7.24R</i>	The words “ <i>BIPRU 3.2.20R</i> to <i>BIPRU 3.2.26R</i> ” are replaced by the words “ <i>MIPRU 4.2A.8R</i> to <i>MIPRU 4.2A.11R</i> and <i>MIPRU 4.2A.14R</i> ”.
<i>BIPRU 5.7.24R(1)</i>	This <i>rule</i> is amended to read as follows: “E is the <i>exposure</i> value according to <i>MIPRU 4.2A.5R</i> and

	<i>BIPRU 3.2.3R.</i> ”
<i>BIPRU 5.7.27R</i>	The references to <i>BIPRU 4.10R</i> and the <i>IRB approach</i> do not apply
<i>BIPRU 5.8.8R</i> and <i>BIPRU 5.8.9R</i>	These <i>rules</i> do not apply

## 4.2D Liquidity resources requirements

### Application

- 4.2D.1 R This section applies to a *firm* carrying on any *home financing* or *home finance administration* connected to *regulated mortgage contracts*, unless as at 26 April 2014 its *Part IV permission* was and continues to remain subject to a restriction preventing it from undertaking new *home financing* or *home finance administration* connected to *regulated mortgage contracts*.

### Adequacy of liquidity resources

- 4.2D.2 R A *firm* must at all times maintain liquidity resources which are adequate, both as to amount and quality, to ensure that there is no significant risk that its liabilities cannot be met as they fall due.
- 4.2D.3 G In assessing the adequacy of liquidity resources, a *firm* should have regard to the overall character of the resources available to it, which enable it to meet its liabilities as they fall due. A *firm* should ensure that:
- (1) it holds sufficient assets which are marketable, or otherwise realisable;
  - (2) it is able to generate funds from those assets in a timely manner; and
  - (3) it maintains a prudent funding profile in which its assets are of appropriate maturities, taking into account the expected timing of its liabilities.

### Systems and controls requirements

- 4.2D.4 R A *firm* must have in place robust strategies, policies, processes and systems that enable it to identify, measure, manage and monitor *liquidity risk* over the appropriate set of time horizons for its business activities, to ensure that it maintains adequate levels of liquidity resources. These strategies, policies, processes, and systems must be appropriate to the *firm's* business lines, currencies in which it operates, and its *group* companies and must include adequate allocation mechanisms of liquidity costs, benefits and risks.
- 4.2D.5 R The strategies, policies, processes and systems referred to in *MIPRU 4.2D.4R* must be proportionate to the nature, scale and complexity of the

*firm's* activities and the risk profile of the *firm*.

- 4.2D.6 R A *firm* must have in place reliable management information systems to provide its *governing body*, *senior managers* and other appropriate personnel with timely and forward-looking information on the liquidity position of the *firm*.
- 4.2D.7 R A *firm* must ensure that its *governing body* reviews regularly (and not less frequently than annually) the continued adequacy of any strategies, policies, processes and systems in place in accordance with *MIPRU* 4.2D.4R

Stress testing and contingency funding plans

- 4.2D.8 R A *firm* must consider alternative scenarios in which its liquidity position could be impacted. The consideration of alternative scenarios must include and deal with off-balance sheet items and other contingent liabilities, including those of *securitisation special purpose entities (SSPEs)* or other special purpose entities, in relation to which the *firm* acts as *sponsor* or provides material liquidity support. These scenarios must be incorporated into the stress testing under *MIPRU* 4.2D.9R.
- 4.2D.9 R In order to ensure compliance with *MIPRU* 4.2D.2R, a *firm* must:
- (1) conduct on a regular basis appropriate stress tests so as to:
    - (a) identify sources of potential liquidity strain; and
    - (b) ensure that the risks of current liquidity exposures can be adequately managed; and
  - (2) analyse the separate and combined impact of possible future liquidity stresses on its:
    - (a) cash flows;
    - (b) liquidity position; and
    - (c) solvency; and
  - (3) make, as soon as is practicable after a test has been performed, and maintain a written record of all stress tests and their results
- 4.2D.10 R A *firm* must ensure that its *governing body* reviews regularly the stresses and scenarios tested and the assumptions underlying the funding position of the *firm* to ensure that their nature and severity remain appropriate and relevant to it.
- 4.2D.11 G For the purpose of *MIPRU* 4.2D.10R a review should take into account:
- (1) changes in market conditions;
  - (2) changes in funding sources and inflows;

- (3) changes in the nature, scale or complexity of the *firm's* business model and activities; and
- (4) the *firm's* practical experience in periods of stress.
- 4.2D.12 R A *firm* must adjust its strategies, internal policies and limits on liquidity risk, taking into account the outcome of the alternative scenarios referred to in *MIPRU* 4.2D.8R.
- 4.2D.13 R (1) A *firm* must have in place contingency funding plans setting out adequate strategies and proper implementation measures in order to address potential liquidity shortfalls.
- (2) The contingency funding plans must be:
- (a) in writing;
- (b) approved by the *firm's governing body*;
- (c) regularly tested; and
- (d) updated on the basis of the outcome of the stress tests, testing alternative scenarios set out in *MIPRU* 4.2D.8R.
- 4.2D.14 G A contingency funding plan sets out a *firm's* strategies for managing liquidity shortfalls in emergency situations. Its aim should be to ensure that, in each of the stresses set out in *MIPRU* 4.2D.11R, it would have sufficient liquidity resources to ensure that it can meet its liabilities as they fall due.

Amend the following as shown.

#### 4.4 Calculation of capital resources

The calculation of a firm's capital resources

...

- 4.4.8 R (1) This rule applies to a *firm* which:
- (a) carries on:
- (i) *insurance mediation activity*; or
- (ii) *home finance mediation activity* (or both); and
- (b) in relation to those activities, holds *client money* or other *client assets*; or

~~but is not carrying on home financing or home finance administration.~~

- (b) carries on home financing or home finance administration connected to regulated mortgage contracts (or both) unless as at 26 April 2014 its Part IV permission was and continues to remain subject to a restriction preventing it from undertaking new home financing or home finance administration connected to regulated mortgage contracts.

...

...

## Schedule 1 Record keeping requirements

G ~~There are no record keeping requirements in MIPRU.~~

1 The aim of the guidance in the following table is to give the reader an overview of the relevant record keeping requirements.

2 It is not a complete statement of those requirements and should not be relied on as if it were.

<u>Handbook reference</u>	<u>Subject of record</u>	<u>Contents of record</u>	<u>When record must be made</u>	<u>Retention period</u>
<u>MIPRU 4.2D.9R (3)</u>	<u>Stress tests</u>	<u>All stress tests performed by a firm to which MIPRU 4.2D.1R applies, and the results of those tests</u>	<u>As soon as practicable after a test has been performed</u>	<u>Not specified</u>

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