Financial Conduct Authority Consultation CP14/20 on the implementation of the Mortgage Credit Directive and the new regime for second charge mortgages

A response by the Intermediary Mortgage Lenders Association

29th December 2014

Introduction

1. The Intermediary Mortgage Lenders Association (IMLA) welcomes the opportunity to respond to this important FCA consultation paper (CP14/20) on the implementation of the Mortgage Credit Directive.

2. IMLA is the representative trade body for mortgage lenders who lend through intermediaries. Our members include banks, building societies and specialist lenders.

Background

3. IMLA has been an active participant in the industry working group convened by the FCA. In preparing this response IMLA has taken the view that it should focus on a narrow range of issues – primarily those areas which have particular salience for the intermediary mortgage market rather than cover the entire CP. We will leave this to other relevant trade bodies such as the BSA, the CML and the FLA. It would make sense if the instructions for using the ESIS were included within the Handbook. This will provide lenders with a consistent understanding of what needs to be included and how the document needs to look, as well as clearly highlighting where lenders have flexibility regarding the documents format / design. IMLA would reiterate that the timeframe for implementing the MCD may be challenging for some lenders, especially if the proposal to implement early is adopted. At the same time individual lenders should be allowed to adopt key measures early if that suits them.

4. IMLA was pleased that through the process of discussion and dialogue it was possible to resolve issues around early repayment charges where the MCD might have damaged the sensible existing approaches. At the same time IMLA, like other trade bodies, remains concerned that the Directive as a whole will do little to benefit the UK mortgage market or the consumers it serves. The UK market is dissimilar to most other mortgage markets in Europe and as a consequence there are real tensions

between the Directive's approach and UK practice. The FCA must continue to work with the industry to minimise the negative impacts of the Directive and to find ways forward that are compatible with current working practices in the UK.

5. IMLA remains concerned that we still have no resolution of the issue of managing mortgage offers in the pipeline on 21 March 2016. The MCD does not discuss pipeline issues. It is important this issue is resolved otherwise there is the potential for significant market disruption in the first half of 2016 as cases uncompleted by this date will have to be reassessed. IMLA recognises that this is a complex issue and is one example of where the MCD requirement is potentially incompatible with the existing process in the UK. There is a need for a transitional period for pipeline business and we would note our previous experience of 'M Day' in 2004 as a solution that worked for the industry. Cases in the pipeline before that date should be allowed to complete under the old rules subject to there being no material change in circumstances. IMLA shares the views expressed by others that the MCD should be applied to new lending only and thus exclude contract variations. This would be of great benefit to lenders and consumers

The Questions Posed

6. IMLA will thus focus on answering 19 of the 58 questions posed in the CP.

Q1: Do you agree with our proposed approach to implementing the transitional arrangements by requiring 'top-up' disclosure?

7. This remains a serious area of concern for members and brokers. Firms vary in how they are approaching the transitional arrangements with some indicating a move to ESIS before March 2019 while others intend to use the top up approach. While it is sensible that firms put in place what works for them (reflecting IT and other system constraints), this may create a confusing landscape for brokers and consumers, not least because there is no requirement for the top up information to be provided with the KFI. The FCA has helpfully set out what it considers necessary to add to the KFI as a top up and is clearly working within the limits of the legislation. The evidence to date in that sourcing systems, a key element in the intermediary market should be able to cope with different approaches, KFI, KFI plus and ESIS. We will need to track this closely. It will be important that all brokers understand the options used by lenders so that they can explain the different approaches adopted. While there may be some consumer confusion, eg, comparing an ESIS issued by one lender against a KFI plus issued by another, we would expect consumers using intermediaries (as will be the case for IMLA members) to find their way through this successfully.

Q3: What difficulties, if any, can you see with using the ESIS instructions and template (see MCOB 5A Annex 1R and 2R) to prepare pre-sale mortgage illustrations?

8. Firms producing the ESIS must ensure they comply fully with the key information requirements about brokers needed for Section 2. In addition for a lender to complete section 4, and calculate the APRC, it must have details of any fees payable to the broker. Both lenders and sourcing systems will need to build in sufficient provisions to include this information in the ESIS. There are concerns that the distribution of fees being paid becomes less clear under the proposed rules.

Q5: Do you agree with the proposed approach to implementing the MCD requirement for a binding offer?

9. Again this is a difficult area and a good example of where the MCD frames issues which sit uncomfortably with UK mortgage market practice. Without doubt firms have a range of views about what constitutes a binding offer and the FCA's approach of letting firms decide themselves what the

binding offer trigger point should be makes considerable sense. We remain concerned that the binding offer requirement will both complicate and limit the self- build market and act against the operation of a prudent retention policy by the lender.

10. There has also been an extensive discussion with the FCA as to what circumstances would be considered as an acceptable basis for the withdrawal of a binding offer. At present fraud is the only basis for withdrawal. Clearly there can be dramatic changes in a customer's circumstances (redundancy/death of a spouse/divorce etc and IMLA members would welcome further guidance around this. In many cases the customer might withdraw but lenders are keen to have a reserve power that might be used if it was not in the customer's best interests to proceed. This is an area where lenders would wish to see further dialogue and guidance.

11. Overall, members take the view that offers currently issued by lenders should be considered as binding. It is on the basis of the lender's offer that conveyancers commit consumers to the transaction/exchange contracts. Failure to complete a purchase after exchange of contracts risks the deposit being lost and contract penalties being incurred. To suggest that the offer is not binding on the lender introduces an element of uncertainty to the process that does not currently exist. The concept of a binding mortgage offer is not familiar to the UK. Our understanding is that the offer is a legal contract which becomes binding when accepted, ie, is the equivalent of a binding offer and should be accepted as such. Lenders certainly take the view that is what they have committed to in terms of the allocation of funds and consumers proceed on the basis they have an offer which binds the lender.

12. We note the reference within the consultation to firms being left to "establish the precise trigger' for the binding offer. Some members are of the view that the reflection period should be triggered from the date that the mortgage offer is issued to the customer. The guidance at 6A.3.3 should be amended to limit the circumstances when an offer might be withdrawn (and remain compatible with both the Directive and UK regulatory regime) e.g. fraud, property title unacceptable, material change in customer circumstances impacting affordability (e.g. loss of employment). Alternatively, the guidance could be removed to allow lenders to each make their own decision on when they are issuing a binding offer. The approach set out above would also work for retentions/self-builds provided that allowable conditions had been met.

Q6: Do you agree that the MCD consideration period is better enacted as a pre-sale reflection period, rather than a post-sale cooling-off period?

13. The binding offer is also the starting point for a new requirement for consumers to have time to reflect on the offer with the option for this to be a 7 day reflection on the offer and before entering into a contract or a 7 day right of withdrawal post the contracted offer. The FCA proposes to adopt the former. IMLA would see this as sensible. The latter makes little sense in a UK context. The receipt of a formal offer is the point where the consumer is most likely to reflect on the mortgage offer.

Q7: Would it simplify matters, for example in terms of the compliance obligations for firms, to apply the MCD approach to the APRC calculation to all lending rather than just that covered by the directive?

14. Yes it would.

Q8: Do you agree with our proposed approach to specifying a benchmark that firms may need to use when calculating a second APRC?

15. We agree with the approach recommended and it will be for the FCA to ensure lenders are consistent in their approach to this requirement

Q9: Do you agree with our proposed approach to transposing the MCD requirements on financial promotions and the wider simplification of our rules in this area?

16. Yes

Q10: What challenges do you see in providing consumers with an adequate explanation, for example in an execution-only sale?

17. Lenders do not see too many difficulties with giving customers an adequate explanation provided the customer is given clear guidance on how they should indicate that they have read and understood the relevant details. There is an expectation that we will see an increase in the number of execution only sales moving into advised sales as a reflection of the extra questions customer may now ask.

18. On knowledge and competency IMLA welcomes the fact that lenders will have until 2017 to comply. IMLA agrees that existing CeMAP Level Three qualifications for mortgage sellers are sufficient. This will help minimises the impact on firms.

Q11: What do you consider will be the impact of the new MCD rules on the availability of foreign currency mortgages?

19. IMLA would accept there is some merit in having rules to warn customers who choose to take their mortgages out in a foreign currency though there remain questions about the frequency and timing of such warnings. However, it is much less clear why warnings must be provided to customers resident in the UK and who take their mortgage out in sterling, but are paid in a different currency. The changes required to cater for these rules could be costly for lenders, but the number of customers affected is anticipated to be small. This could lead to a contraction in mortgage availability for customers who are not paid in sterling.

20. It would be helpful to clarify what is meant by "other arrangements" (2A.3.1.R.(2)) regarding foreign currency loans. Is it intended that the warnings given in the ESIS will be sufficient to meet this rule?

Q12: What do you think will be the impact of this approach on firms and consumers

21. We would like to know whether funds drawn from unsecured loans, credit cards or overdrafts which are used as a deposit or to pay ground rent, for example, will be covered by the directive? How would the FCA envisage that firms might manage this lending?

Q13: What, if any, might be alternative approaches that would allow us to meet our legal obligations when implementing the Directive for this type of lending?

22. No comment

Q14: Do you consider that the proposed transitional approach is effective in allowing firms to prepare early for the implementation of the MCD?

23. Yes

Q34: Do you agree with our proposed approach to shared equity loans?

24. It remains unclear to IMLA why certain government schemes are exempt from the MCD. Clearly all shared equity loan arrangements are important in a period where affordability and not least around deposits is stretched. The FCA rightly highlights the risks associated with shared equity loans whether private sector or government. Given those risks and the limited approach to responsible lending requirements set out by the FCA, there is the possibility that consumers will not fully understand the loan arrangements they are entering into. This remains a matter of concern to IMLA.

25. One suggestion would be to exclude only those loans where repayment is only required on sale or disposal of the property ***and*** where no interest is charged during the shared equity term could be excluded. Government and social housing providers might be encouraged to comply on a voluntary basis.

Q51: Do you agree with our proposed rules requiring firms to make customers aware of alternative finance options where they are looking to increase their secured borrowing?

26. While there is a case for this, there are significant doubts about whether there is a need for the FCA to make rules regarding this. In all likelihood lenders will develop processes to deal with this and address the customer's needs.

Q52: Do you agree that these proposed rules should form part of the initial disclosure, applicable to both advised and execution only sales?

27. Again as per Q51 there are arguments for and against this. If rules were introduced they should form part of the initial disclosure.

Q53: Do you agree with our proposal to transpose the CONC 7 provisions for vulnerable customers into MCOB 13?

28. Yes, this is a sensible set of safeguards. It gives lenders a consistent base to work off.

Q54: Do you agree with the scope of our proposed information sharing requirements?

29. The requirement for notices is already covered by the Civil Procedure Rules and we do not feel there is a need for further regulation in this area which in our view is likely to increase costs to the consumer.

Q55: Do you agree that our proposed information sharing requirements should apply to all firms with a regulated mortgage secured against the property?

30. Yes but subject to the comments in 54

Q56: Do you agree with the amendments made to PERG?

31. We would welcome further clarity on impact of the changes to business lending

Further information

32. This revised response has been prepared by Peter Williams, Executive Director of IMLA in conjunction with the Directors of IMLA. If there are any questions or comments these should be directed to Peter Williams on 07718120858 and consultpwilliams@btinternet.com