



Key Contact

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“... a key theme of the review is to apply a more intrusive approach to regulation...”

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THE MORTGAGE MARKET REVIEW

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Overview

The FSA's much-anticipated discussion paper on the Mortgage Market Review was published on 19 October. The FSA's aim is to create a mortgage market that is sustainable for all participants, and that works better for consumers. The paper is extensive in scope and sets out the issues that the FSA believes must be tackled to achieve these outcomes and the options for addressing them.

Background

The regulator's self-appraisal of its own contribution to the problems in the mortgage market is a key driver of the proposed reform. The FSA believes its existing regulatory framework has been shown to be ineffective in limiting high risk lending and unaffordable borrowing and the paper therefore outlines a more intrusive and interventionist style of regulation.

Key topics

The key areas of discussion in the review are:

- imposing affordability assessments for all mortgages and making lenders bear the ultimate responsibility for assessing a consumer's ability to pay;
- making income verification a requirement in every case, thereby effectively banning self-certification (or 'self-cert') mortgages;
- banning the sale of products which contain certain 'toxic combinations' of characteristics that put borrowers at risk;
- banning arrears charges on those borrowers who have an agreed arrangement in place, to ensure firms do not profit from consumers in arrears;
- requiring all mortgage advisers to be held individually responsible to the FSA;
- proposed extension of the FSA's scope to cover buy-to-let lending and all lending secured on a home.

Ability to pay

At present the FSA does not prescribe any standardised approach to assessing a consumer's ability to repay a mortgage. As a result current practices vary. By imposing affordability assessments the FSA expects there to be a reduction in the number of unaffordable and unsuitable mortgage transactions and a decrease in arrears and repossession rates.

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No more ‘self-cert’?

Self-cert mortgages were originally designed to meet the needs of self-employed borrowers but the FSA believes recent lending practice has meant that their reach has grown beyond the consumer groups for which they were intended. FSA analysis has shown that self-cert borrowers take out larger loan amounts than borrowers with standard products and fall into arrears much more frequently. It is for these reasons that the FSA proposes to ban these products.

Toxic combinations

The FSA has resisted placing a ban on high loan-to-value, high debt-to-income and credit impaired mortgages. However the ‘toxic’ mix of a combination of high loan-to-value, credit impaired and unstable income could potentially justify a ban on these types of product in the future. The review calls for further analysis of this area before a decision is made as the FSA does not currently have enough evidence to determine which of these combinations (if any) result in higher arrears rates.

Price regulation?

The review proposes to prohibit firms from imposing arrears charges on those borrowers who have an agreed arrangement in place. This marks a substantial change in approach from the regulator which in the past has deliberately veered away from becoming a regulator of price.

One reason given by the FSA to support its becoming more involved in price regulation is ‘that many consumers lack the desire and ability to compare charges and focus exclusively on the headline interest rate instead’. As a result a key theme of the review is to apply a more intrusive approach to regulation to ‘help protect consumers from themselves’.

Approved Persons

The paper proposes to extend the Approved Persons Regime, through the application of CF30 (customer function) and CF10 (compliance oversight) to mortgage (and other home finance) advisers. The FSA believes that this proposed extension should improve the standards of fitness and propriety among individual mortgage advisors, prohibiting rogue individuals from the industry.

Scope extension

The FSA believes that by extending regulation to second charge loans the regulatory framework for firms and consumers will be simplified, and that unified regulation will allow better oversight both prudentially and in the assessment of loan affordability. As with the second charge market the regulation of buy-to-let would be seen to strengthen oversight arrangements and offer the potential for protecting consumers making investment decisions on property.

Targeted and proportionate change

The mortgage consumer demographic is made up of a complex mix of individuals, from the financially capable to the financially vulnerable, all of whom seek financial services from a complex market of different types of lenders and intermediaries. In summary one of the biggest challenges for the Mortgage Market Review is to make sure that the right consumers benefit from targeted and proportionate changes.

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