Financial Services Consumer Panel
AN INDEPENDENT VOICE FOR CONSUMERS OF FINANCIAL SERVICES

Telephone: 020 7066 9346
Email: enquiries@fs-cp.org.uk

Terence Denness
Policy, Risk and Research Division
Financial Conduct Authority
25 The North Colonnade
Canary Wharf
London E14 5HS

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Dear Terence,

CP14/20 - Implementation of the Mortgage Credit Directive and the new regime for second charge mortgages

This is the Financial Services Consumer Panel's response to the Financial Conduct Authority's Consultation Paper on implementing the Mortgage Credit Directive (MCD).

The UK mortgage market has been subject to a great deal of change in the last couple of years with the introduction of the Mortgage Market Review, so we are pleased that the FCA proposes to implement the MCD, wherever possible, using existing rules. We welcome the FCA's desire to cause as little further disruption for consumers as possible.

The Panel strongly supports the Government's decision that second charge mortgage lending should come under the FCA's mortgage regime as part of the Directive implementation. It has always struck us as odd that second charge lending was previously regulated in the same way as more generic credit products. Considering the second charge market has consistently suffered from a higher rate of repossessions than first charge mortgages, and arrears and forbearance is an area where the FCA conduct regime for mortgages works well, we are pleased the two will now be regulated in broadly the same way. For consumers, certainly, it will be more straightforward.

We are, however, concerned about the 'regulatory gap' for second charge lending until March 2016, and the potential for regulatory arbitrage during this period.

Specific comments

APRC calculations

The Panel supports the idea of applying the MCD APRC calculation across all forms of mortgage lending, as this will give consumers a clear basis for comparison.

However, the requirement for a second APRC for variable rate loans may mislead consumers. The highest rate payable in the last 20 years is no indication of where rates will go in the next 20. At the moment, given that rates have recently been low, the projected 'worst case' scenario rate will not appear very high. Consumers must not be left believing rates are guaranteed to stay low in the future.

Whilst we do understand that this proposal is a requirement set out in the Directive, we do not believe the information will provide any benefit to consumers. The current requirement on firms to apply appropriate interest rate stress tests, having regard to both the market expectations and any prevailing Financial Policy Committee recommendation, will give consumers a far more realistic prediction of possible interest rate changes and how these will affect repayment amounts. To apply an interest rate stress test, as well as a 20 year 'worst case scenario' may lead to mixed messages for consumers.

Foreign currency loans

The Panel fully supports the policy intention here to protect consumers taking on exchange rate risk by purchasing property in another member state or using a currency which differs to that of their income.

However, we are concerned about the unintended consequences of this proposal. One example might be for a UK family home in the UK where the main earner is posted overseas (possibly still paid in sterling). There is likely to be no exchange rate risk, yet it would appear that this would be classed as a foreign currency loan.

We agree with the FCA that this is likely to capture only a very small number of consumers. However, we are concerned that if lenders pull out of this type of lending, then those consumers already in this position may be unable to move home or re-mortgage, in effect becoming mortgage prisoners as a result.

Equity Release

The Panel has concerns about the possibility of new 'hybrid' products being developed that require a nominal repayment of capital and therefore would fall outside the current regulatory regime for lifetime mortgages and into the MCD regulations.

Current equity release lifetime mortgages have no contractual requirement for full repayment of capital which is why the exemption applies to these products. It seems possible, however, that new products which require a nominal repayment of capital (even very small sums) could be developed in future which would place these products outside of equity release regulation and into the regime covered by the MCD. We have two main concerns:

- Lifetime mortgages Key Facts Illustrations (KFI) are designed to reflect the different features of a lifetime mortgage and include information on the benefits and more importantly the specific risks associated with the product. The new ESIS required for standard mortgages will not necessarily highlight the specific risks that relate to true equity release schemes (i.e. that the debt could erode equity).
- Currently advisers working in the equity release market are required to hold a relevant and specific qualification. If products that are ostensibly equity release products fall into the MCD, unqualified advisers and those who do not have proficiency in the equity release market will be permitted to sell these products. All forms of equity release lifetime mortgages should remain outside of the scope of the Directive, to ensure consumers receive the right advice and adequate protections.

Transitional Arrangements

The Panel remains concerned about the lack of a formal transitional period ahead of full implementation, particularly for mortgages already in the pipeline. A situation where consumers have to return to the beginning of the process if they have not completed by 21 March 2016, would not serve anyone's interests.

Second Charge mortgages

The Panel strongly supports the proposal to move second charge mortgage lending into the regulated mortgage regime. We acknowledge that second charge mortgages can be beneficial to consumers but we also believe that it is important consumers are aware of all of the options available to them, as well as the potential consequences.

Ideally we would like the transfer to happen more quickly, given there will be a 'regulatory gap' until March 2016 when the Directive will be fully implemented. We are concerned that the FCA will not be collecting performance or sales data on second charge mortgages until 2016, and are therefore worried about firms engaging in regulatory arbitrage during this period. Furthermore, we strongly oppose any proposals to delay the data reporting requirements even further, past March 2016. At the very least, we urge the FCA to collect data with immediate effect, on the total number of mortgages taken out, and how these are split between first and second charge loans. It is important the FCA knows at the earliest opportunity if second charge mortgage sales start to increase disproportionately.

In addition, given the importance the FCA placed on the need for fully advised sales in the Mortgage Market Review, we find it surprising that second charge lenders may be able to go beyond the implementation date of March 2016 without moving to an advised model. For both the advising and selling standards, and the data reporting requirements, the Panel urges the FCA to ensure consumers are treated consistently and firms are supervised appropriately from the earliest opportunity.

The Panel strongly supports the proposals for advice, creditworthiness assessments and additional information in the initial disclosure at the start of the sale. We believe that all mortgages should be aligned in regulation in order to have a consistent approach from lenders providing clearer information and comparisons for consumers. In addition, we believe the enhanced protections for second charge borrowers, and both fair and appropriate fees and charges should be consistency applied for all loans.

Yours sincerely

Sue Lewis
Chair
Financial Services Consumer Panel