

Response to Consultation Document: Mortgage Market Review

Issued by the Financial Services Authority

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1.0 Background

1.1 Housing Rights Service was established in 1964 and is the leading provider of independent specialist housing advice services in Northern Ireland. We believe everyone has the right to a decent, safe, affordable home. Our services include:

- Providing a housing advice line
- Undertaking advocacy and legal representation on behalf of people with housing problems
- Providing online advice through our award winning website www.housingadviceNI.org and an email advice service
- Providing a specialist housing advice service within the prisons
- Delivering a skills and knowledge based training programme
- Producing information resources materials
- Supporting (In partnership with Citizens Advice and AdviceNI) generalist advice agencies to deliver high quality housing in their local communities
- Providing client based commitment to influence the development of relevant public policy and legislation
- Providing practical advice and assistance at court for possession proceedings and undertaking preventative policy work through our Preventing Possession Initiative.

All our services are delivered throughout NI and focus on the key areas of preventing homelessness; accessing accommodation; tackling poor housing conditions and affordability.

Funding for our work comes from a range of different sources. Our core services are funded by the Housing Division of the Department for Social Development (NI).

- 1.2 The organisation first became involved in the provision of money advice and debt counselling in the early 1990s when interest rates, and also the number of homes being repossessed, were at record levels. As the primary purpose of our organisation is preventing and alleviating homelessness, our debt advice is only available to clients who have a housing related debt (i.e. *mortgage/ rent or rate arrears*). The service provided is, however, holistic and takes into account all the client's outstanding debts.

In February 2009, Housing Rights Service launched its new "Preventing Possession Initiative." It adopts a twin track approach to preventing homelessness as a consequence of debt-related possession. Firstly an in-situ court representation service is available for owners and tenants facing possession. This seeks to make advice available, free of charge, to people facing the imminent threat of repossession, who do not have their own legal representation and who have not engaged with an advice agency prior to the court date. There is also a policy element to the project. Through engagement with government, lenders and landlords we aim to reduce the likelihood of possession actions being initiated in the first instance and to ensure that viable housing options are available for those at risk of losing their homes.

- 1.3 We welcome this opportunity to respond to the Discussion Paper: The Mortgage Market Review. In particular Housing Rights Service is supportive of the Financial Services Authority's (FSA) decision to make lenders ultimately responsible for assessing and verifying affordability in every sale. We believe that this will help combat irresponsible lending practices and encourage lenders to ensure that mortgage products sold to consumers must be appropriate and affordable.

Housing Rights Service is very much in favour of a more intrusive and interventionist approach to the mortgage market and supports many of the proposals contained in the Mortgage Market Review.

2.0 General comments

Financial crisis and debt are important triggers to homelessness which has a devastating effect on families. Housing Rights Service statistics indicate that in 2008/09, there was more than a 500% increase in the number of clients whom our advisers represented at possession proceedings in court compared to the previous year. Regrettably, in our view, a significant number of these hearings could have been avoided if a more effective regulatory framework had been in place to constrain risky lending and unaffordable borrowing.

Housing Rights Service has long advocated for better regulation of mortgage service providers, particularly sub prime lenders and intermediaries, to promote responsible lending and marketing practices. It is vital that mortgage market providers lend responsibly; ensuring consumers are borrowing in accordance with their income and ability to repay. Housing Rights Service believes that some of our clients would not be in the situation they are currently in if responsible lending practices and appropriate affordability assessments had been conducted from the outset. In fact, had the proper checks and balances been in place, a number of them would not have qualified for mortgages in the first place.

The lack of Government will to intervene in the mortgage market has allowed an alarming number of borrowers with low incomes or in receipt of state benefits to secure mortgages. Our experience shows that in Northern Ireland many people were sold inappropriate mortgage products, often through intermediaries working in the sub prime sector. Housing Rights Service identified that some unscrupulous intermediaries, spurred on by attractive commissions, were not always thorough when it came to checking whether products were affordable for individual, and often vulnerable, consumers.

With the dramatic increase in the number of homeowners facing repossession in Northern Ireland, Housing Rights Service urges the FSA to implement a more interventionist and proactive approach as soon as possible.

In responding to this discussion paper, our comments are focused on consumer protection based on the experience of our clients. We very much support strengthening consumer protections in the mortgage market, including extending the scope of imposing affordability assessments for all mortgage applications and making lenders ultimately responsible for affordability. On this basis, we have responded to those questions which we believe are pertinent to consumer protection.

3.0 Specific responses

Q6. Do you consider that the FSA should prohibit the sale of mortgages to borrowers with multiple high-risk characteristics? If yes, what particular combinations of risk factors should the FSA consider prohibiting and why?

Housing Rights Service would be in favour of prohibiting the sale of mortgages to borrowers with multiple high-risk characteristics. Whilst we acknowledge that financial crisis and debt cannot be totally avoided, taking a holistic view of a person's circumstances could protect potential borrowers from entering into a substantial financial commitment which they may not be able to sustain.

Risk factors which could be taken into account include: poor or bad credit history; high level of debt accrued; low income/disposable income. However, we do not want to be too prescriptive at this stage, particularly given that the FSA's analysis of what causes high default rates is not yet complete. However, if this approach is favoured, it would likely require guidance for lenders to enable a fair assessment

of multiple high risk characteristics as it may be necessary for lenders to retain some discretion for exceptional cases.

Q7. Do you consider that requiring mortgage verification of income by the lender for all mortgage applications is a viable option, and one which is sufficient to ensure responsible and sustainable levels of mortgage lending?

Housing Rights Service supports a robust approach to income verification. We agree that non income verified mortgages, designed to meet the needs of self employed people, were widely used by consumer groups for which they were not originally intended. Our experience shows that there is a significant number of clients currently experiencing mortgage problems who self certified their income. We are of the strong opinion that most of these consumers would not have been given unaffordable mortgages had they been required to verify their income. In most of these cases, intermediaries are involved.

We agree that, in the vast majority of cases, income is capable of being verified. Therefore, the vast majority of consumers should be required to evidence their income. However, we feel that the FSA needs to consider exceptional circumstances where there are consistent problems verifying income, for example self employed construction workers and taxi drivers who may not have wage slips and whose income varies. Housing Rights Service would welcome exploring conditions where self-certification can be used in specific cases, reflecting the initial purpose it was intended for, whilst ensuring that it is not open to exploitation.

Q8. Do you agree with our proposal to require lenders to take ultimate responsibility for affordability?

Housing Rights Service believes that a key problem underlying many of the issues in the mortgage market has been firms' failure to perform proper affordability checks. We wholly support the proposal to make lenders ultimately responsible for assessing affordability and to disallow the passing of this responsibility onto others.

Q9. Do you agree with our proposal to require lenders to assess affordability based on:

(i) the borrowers free disposable income;

Housing Rights Service supports this proposal. In order to get an accurate picture of affordability, assessments must consider the consumer's free disposable income (i.e. income net of all expenditure). We welcome the 'best practice' illustration of calculation (displayed at Exhibit 4.16 of the discussion paper) which reflects the information which our debt advisers use when drawing up a financial statement.

We support a robust assessment of both income and expenditure and believe that a mortgage is only affordable if its level and terms allow the consumer to meet current and future payment obligations.

(ii) a consumer's borrowing capacity;

Housing Rights Service welcomes the proposal to prohibit mortgages to those with negative, zero or low borrowing capacity as this would strengthen consumers against irresponsible lending practices. We agree

with the FSA that, under no circumstances, can the amount of a mortgage be increased above a consumer's borrowing capacity. This is imperative to ensure that the consumer does not borrow irresponsibly which could lead to the accumulation of further debt.

Housing Rights Service has identified failures with regard to clarity and transparency concerning lenders' assessment of applicants' affordability in the 'sub prime' segment of market. Typically, consumers who borrow from the sub prime lender tend to be more vulnerable, less financially literate and more likely to have a poor credit history or a limited ability to repay a loan. Taking this into account, it is therefore important to ensure that all consumers are properly assessed and advised.

Housing Rights Service also welcomes the proposal that the consumer's borrowing capacity will be stress tested for increase in interest rates. We believe that this would be beneficial in assessing and informing the consumer about his/her affordability capacity in the long term should their financial circumstances change or interest rates rise.

(iii) the plausibility of the information obtained;

Housing Rights Service believes that it is essential that borrowers must present an accurate and full picture of their financial circumstances to the lender to allow for an accurate affordability assessment. Housing Rights Service understands that guaranteeing plausibility of consumer information is difficult, in particular expenditure information. We support the FSA's proposal for greater prescription around affordability assessments to ensure that the information provided by the consumer is plausible.

We feel that the use of credit reference agencies and official documentation, such as bank statements and utility bills, as well as consumer-provided data can help lenders collect a full and thorough affordability assessment of a consumer's financial circumstances. We believe that a thorough assessment can be carried out without unnecessary intrusion into the consumer's personal circumstances.

(iv) a capital repayment basis?

Housing Rights Service believes there is merit in this approach on the basis that a significant number of our clients were granted an interest only mortgage because they could not afford a repayment mortgage. Even a slight change in circumstances leaves such borrowers vulnerable to default and without the option of switching temporarily to a lower cost mortgage product (i.e. some lenders will allow clients with repayment mortgages who are experiencing difficulties to move to interest only temporarily). We believe that assessing the loan on a capital repayment basis is the most appropriate method of assessing the consumer's long-term sustainability to maintain mortgage repayments.

Q10. Is the increased focus on affordability the right way to ensure sustainability of lending and consumer protection?

Housing Rights Service supports a more thorough and rigorous approach to affordability assessments. It is imperative that the FSA ensures effective affordability assessments are proactively enforced amongst the mortgage market to tackle irresponsible lending and to protect vulnerable consumers.

Q12. *Do you think that the FSA should limit the amount of equity a consumer can withdraw from their home?*

Housing Rights Service would like to see further analysis conducted regarding this proposal; however, we understand that there can be negative consequences for some consumers who borrow against the equity of their homes.

In Northern Ireland, as a result of the property boom and escalating house prices, consumers were borrowing large amounts secured against the equity of their home. As a result of the recession and subsequent crash of the property market, many consumers were left in negative equity because the price of their property decreased substantially, leaving them in considerable debt. In a number of cases the loans were taken out to consolidate debt including mortgage arrears thus turning unsecured debt into secured debt. In our view, lenders could be more responsible when lending on the strength of equity and we believe that this does warrant some level of regulatory intervention.

Q13. *Do you agree that we need to strengthen the selling standards for non advised (information-only) sales to ensure consumers are only entering into contracts which are both affordable and appropriate?*

Housing Rights Service wholly supports this proposal on the basis that we have identified some questionable intermediary practices in Northern Ireland. Stronger selling standards are imperative to ensuring that potential consumer detriment is prevented and the appropriate level of protection is afforded in non-advised sales.

Housing Rights Service welcomes enhancing consumer protection by imposing a basic standardised affordability and appropriateness test. However, we would seek

clarification as to how the FSA is going to ensure affordability tests are implemented in all non-advised sales firms.

Q15. *To what extent should intermediaries retain responsibility for assessing a consumer's ability to repay? How could this work in practice?*

Whilst ultimate responsibility should rightly lie with the lender, the intermediary should still be required to provide, but not verify, a preliminary affordability assessment as they will be advising the consumer on the suitability of a mortgage product. We agree with the view that an intermediary could not properly ascertain the suitability of a mortgage without first assessing a borrower's affordability.

Housing Rights Service welcomes the approach of the FSA to set up industry working groups to determine the framework of an affordable assessment and what it should contain. We believe that by ensuring there is an effective affordability model in place, consumers will be protected against the detriment of irresponsible lending.

Q16. *Do you agree that suitability letters should be introduced as compulsory standard?*

Housing Rights Service welcomes the proposal that suitability letters should be introduced as compulsory standard. We believe that providing customers with a written suitability letter, explaining the particular mortgage product that was recommended and reasons for the choice, will help the client understand the difference between products.

Housing Rights Service believes the advantages outweigh the disadvantages and that suitability letters will educate consumers as to the mortgage products that have been recommended for them. These letters, coupled with preliminary

affordability assessments, will further protect consumers against irresponsible lending practices.

Q17. *What are the implications of applying the Approved Person's regime to all individual mortgage intermediaries?*

Housing Rights Service wholly supports the extension of the Approved Person's Regime to all individual mortgage intermediaries. We believe it will assist in addressing consumer detriment by prohibiting rogue individuals from entering the mortgage industry. We feel the implications of applying the Approved Person's Regime will be positive and will further strengthen consumer protection by ensuring appropriate generic standards are implemented throughout all individual intermediaries.

Q21. *Do you agree that simplified scope of service labelling, limited to 'independent' or 'restricted advice' and also describing a non-advised service as 'information-only', will result in better consumer understanding of the services on offer?*

Housing Rights Service wholly welcomes these proposals. It is often our experience that consumers do not understand the various types of services available and how they interact with other. We have identified that consumers often believe that all intermediaries provide advice and that many are unaware that some provide information only and some can provide restricted advice.

Housing Rights Service supports proposals to simplify the scope of the service labelling to the three categories above. We believe this will lead to greater consumer understanding and will educate consumers as to the type of service they will be provided by various firms.

Q23. *Do you agree that the limitations on the rationality of consumer behaviour in the mortgage market support the case for regulatory intrusion?*

Housing Rights Service supports the case for more regulatory intervention to protect consumers. It is important to bear in mind that there are inherent differences between lenders, their intermediaries and borrowers. Lenders are experts in the mortgage market field, whereas the vast majority of consumers struggle to understand the complexities of this market. This situation is even worse for consumers with vulnerabilities who, regrettably, have ended up with mortgage products which are entirely inappropriate to their needs.

Q24. *Do you agree that the FSA has a role in preventing the extension of credit to individuals who are unable to afford such high levels of debt?*

Housing Rights Service agrees that the FSA has a role in preventing the extension of credit to those who are unable to afford such high levels of debt. We welcome proposals that will help prohibit sales to consumers exhibiting multiple high-risk characteristics as we feel this will protect vulnerable consumers from irresponsible lending practices. It is imperative that the FSA ensure, as far as possible, that lenders and intermediaries are acting within the appropriate standards and that affordability forms the basis for all lending decisions.

Q26. *Do you have any comments on our proposals to strengthen our approach to firms' arrears management practices?*

Housing Rights Service welcomes the FSA proposals to increase consumer protection through strengthening firms' arrears management practice. We fully support a compulsory non-exhaustive list of tools that firms must employ to help

consumers in arrears. Housing Rights Service believes this will allow consumers to have access to adequate assistance to help them manage their way out of arrears, prevent unnecessary repossessions and retain their homes.

Housing Rights Service wholly supports the proposals to ban certain unfair, excessive charging practices. In particular, we welcome the ban of charges when a consumer is adhering to an existing arrangement to repay arrears. This is a significant burden that many of our clients have experienced; they are unable to address their existing debts because excessive monthly arrears administration charges are accruing. Housing Rights Service believes this ban will allow consumers to concentrate on dealing with their existing debt without the added burden of accruing charges and consumers will be able to manage their way out of debt more effectively.

Housing Rights Service wholly agrees with the proposals to implement a more interventionist and robust approach to monitoring and enforcing unfair charging practices in the mortgage market.

Q27. Do you consider that the mortgage market fees and charges reflect the underlying costs or are consumers paying excessive charges?

Housing Rights Service believes that unnecessary and excessive arrears charges are a significant problem within the mortgage market. These charges unload further financial burden on consumers who are already struggling to clear existing debts. Charges also vary greatly and we believe they are often not reflective of true underlying costs. Some lenders even continue to add charges where an acceptable repayment agreement has been reached.

Housing Rights Service welcomes the FSA's research to help develop a better understanding of charging that will allow them to identify and challenge unfair

and excessive practices. We urge the FSA to complete this work as soon as possible to prevent any further consumer detriment and look forward to the outcome of this research.

Q28. *What would be the impact of consumers not being allowed to roll up intermediary fees and products into the mortgage loan?*

Housing Rights Service believes prohibiting consumers from rolling up fees could be an obstacle for many borrowers who may not be able to afford the fees upfront. However, in our view, it's the level of product fees being charged that needs to be addressed. Fees can be excessive. If these fees were more reasonable and reflected the true cost of the administration, many consumers would not have to roll up the fees into the loan and could afford to pay upfront. Housing Rights Service believes that it is imperative that lenders and intermediaries disclose the full cost of all fees to the borrower from the outset. From our experience, we have found that many consumers are financially unaware as to the amount of fees they are including into the loan and to the interest that this fee will accumulate by the end of the loan term.

Housing Rights Service looks forward to reading the results of the FSA's ongoing supervisory work into the levels of lender product charges and lender charging models and hopes that this will lend to more reasonable and fair charging practices, reflecting the true cost of administration.

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