

The Rt Hon Nicky Morgan MP
Chair of the Treasury Select Committee
Treasury Committee
House of Commons
Committee Office
London
SW1A 0AA

15 February 2019

**RE: 'Mortgage Prisoners'**

At the hearing on 15 January 2019, members of the Committee asked for more information about how many 'mortgage prisoners' might be helped by the FCA's proposed rule changes. You also asked how many customers are in arrears. I am writing to provide further information on both points.

In our Mortgages Market Study we identified that there were around eight million mortgages with authorised lenders. Of these, two million had been on a reversion rate for six months or longer.¹ We estimated² that 30,000 of these customers would benefit from switching, but were unable to do so, despite being up to date with payments on their existing mortgage. This number includes the following groups:

- Group One - 10,000 customers of active, authorised lenders; and
- Group Two - 20,000 customers of firms that are no longer lending commercially, despite being authorised to do so (inactive lenders).

We also estimated that there was a third group of 120,000 customers of firms that are not authorised for mortgage lending (unregulated entities) who could potentially benefit from switching but may be unable to do so (Group Three).³

Customers in arrears

Rushanara Ali asked me specifically about customers who are in arrears. As we set out in the Mortgages Market Study, we did not include customers in arrears in our estimates of the three groups set out above. This is because our aim was to identify those customers who were up to date with payments on their existing mortgage, but still unable to switch. As they are in financial difficulty, a customer in arrears is by definition not up to date with payments and is therefore not demonstrating that they are able to afford their existing mortgage.

Of those customers with authorised lenders that had been on a reversion rate for six months or more, we identified around 100,000 customers who were in arrears. A further 20,000 customers of unregulated entities were also in arrears.⁴

¹ We consider those that switch within six months of moving on to a reversion rate as being active and engaged.

² As of H2 2016

³ Firms that are not authorised by the FCA for mortgage lending do not need to report to the FCA on the mortgages they hold, and we therefore do not hold substantial data on these mortgages. Our assumptions and analysis were therefore impacted by significant data limitations including a lack of data at a consumer level, use of different sources of data at different reporting dates and the possibility that the sale of mortgage books to firms occurred between the time periods reviewed.

Customers in Group One are able to benefit from an industry agreement and will be further helped by our rule changes

We have already made significant progress for the customers in Group One. As you know UK Finance, the Building Societies' Association and the Intermediary Mortgage Lenders' Association have reached an agreement with their members that enables borrowers on a reversion rate to move to a better deal with their existing lender where they meet certain criteria. These criteria include being up to date with payments, and having a minimum of 2 years and £10,000 left on their mortgage. Sixty-seven authorised lenders, making up 95% of the residential mortgage market, have signed up to the agreement. These lenders committed to writing to all qualifying customers by the end of 2018 (unless they had already recently written to them). We are working closely with the lender trade bodies to monitor the impact of this through our industry working group. We expect that the terms of the agreement should benefit most of the customers in Group One.

As you know, I have also confirmed our intention to consult on changes to our responsible lending rules to provide for a more proportionate, relative affordability assessment. Customers in Group One who may currently fall outside of the industry agreement may nevertheless be able to switch to lenders which take advantage of our proposed rule changes.

Customers in Groups Two and Three may be able to benefit from our proposed rule changes

Not all customers in Group Two or Three will necessarily be helped by our proposed affordability rule changes. It will be a commercial decision for a lender to determine whether or not to use the new affordability rules for anyone seeking to re-mortgage. Some people will have specific circumstances that are likely to put them outside the risk appetite of some lenders. As previously indicated to the Committee, such circumstances could include mortgage customers who:

- are in arrears⁵
- have very high loan to value mortgages
- other considerable debts
- have mortgages in negative equity.

We have more information available on the customers comprising Group Two than Group Three. Based on this information, we have produced profiles of the types of consumer comprising Group Two. These are:

- Interest only or part repayment and part interest only borrowers. These customers often have loan-to-value (LTV) ratios of greater than 80%.
- Interest only or part repayment and part interest only borrowers who are borrowing into retirement. These customers either have LTV ratios of greater than 60% or are in non-standard employment/retired.
- Capital repayment borrowers, a number of whom have LTV ratios of greater than 90%, or who are retirees.
- Borrowers who were considered credit-impaired at the time they took out their mortgages, though their position may have since improved.

⁴ Due to data constraints, we used a different definition of 'in arrears' for customers of unauthorised entities. This was an arrears balance of greater than 1.5% of the outstanding balance.

⁵ As set out above, customers in arrears were excluded from our estimates of Groups One, Two and Three. However, it is possible that some consumers could have gone into arrears since 2016 when the analysis was undertaken. It is equally possible that some of those identified as being in arrears in 2016 could have since recovered.

We do not have equivalent data on the consumers comprising Group Three. However, the profiles above are likely to represent a reasonable proxy for those consumers as well.

It is not currently possible to say from these profiles who will or will not benefit from our rule changes. We are engaging closely with lenders and lender trade bodies to understand the extent to which firms may be interested in taking on certain customers and how these options will be communicated to affected customers. As you know from my previous letter, it may be that we see a two-tier approach, with the larger lenders offering a choice to those with the simplest needs, and a range of more specialist lenders able to manually underwrite more complex cases.

I hope you will understand that it is difficult to speculate beyond this on who will or will not be helped, particularly as the rules themselves have not yet been finalised.

Customers in arrears are already helped by the FCA's forbearance rules

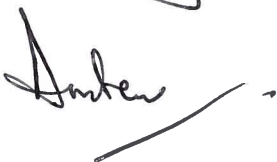
The Committee also asked how best to help customers who cannot benefit from the rule changes (e.g. those in arrears) stay in their homes. As mentioned at the hearing, this may require a wider public policy response and would therefore need to involve the government rather than the FCA.

FCA rules require firms to have a written policy and procedures in place for dealing fairly with any customer who has a payment shortfall (that is, where periodic sums due remain unpaid in breach of the terms of the mortgage contract), including those customers who are in arrears. Firms must provide various pieces of information to customers in arrears, and supply the customer with a leaflet from the Money Advice Service⁶ outlining actions customers can take when having problems paying their mortgage. Firms must also make customers aware of any Government schemes designed to assist borrowers in payment difficulties.

When dealing with a customer in payment difficulties, firms must make reasonable efforts to agree with the customer (or via a third party such as a debt advisor) as to how the shortfall is to be repaid. If a reasonable payment arrangement cannot be found, firms cannot repossess the property unless all other reasonable attempts to resolve the situation have failed. This includes considering, in light of the individual circumstances of the customer, a different term or type of mortgage. Firms must also provide customers with a reasonable time period in which to sell the property themselves.

In addition, firms must establish and implement clear, effective and appropriate policies and procedures for the fair and appropriate treatment of customers whom the firm understands, or reasonably suspects, to be particularly vulnerable.

I hope that you have found the above information helpful.

Yours Sincerely


Andrew Bailey
Chief Executive

⁶ <https://www.moneyadviceservice.org.uk/en/articles/mortgage-arrears-if-you-have-problems-paying-your-mortgage>