Guidance for firms supporting borrowers impacted by the rising cost of living

FCA consultation

Restricted
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Building Societies Association

Introduction

The BSA represents all 43 building societies, as well as 7 larger credit unions. Building societies serve almost 26 million consumers across the UK and have total assets of nearly £500 billion. Together with their subsidiaries, they have helped over 3.6 million families and individuals to buy a home with mortgages totalling over £366 billion, representing 23% of total mortgage balances outstanding in the UK. They are also helping over 23 million people build their financial resilience, holding over £342 billion of retail savings, accounting for 18% of all cash savings in the UK. With all of their headquarters outside London, building societies employ more than 51,500 full and part-time staff. In addition to digital services they operate approximately 1,300 branches, holding a rising share of financial services branches in local communities.

Whilst we have not yet seen an increase in borrowers with mortgage arrears, our members remain alert to the economic conditions, which are rapidly changing. Building societies are sensitive to the rising number of people facing a squeezed household budget and have teams who are well trained and experienced in providing tailored support to those who are struggling. Our message remains that anyone who is worried about their finances and ability to pay their mortgage should get in touch with their lender as soon as possible. They will be provided a safe space for a confidential, non-judgmental discussion and members will do everything possible to help each borrower with options based on their own personal circumstances.

The BSA welcomes the opportunity to respond on behalf of its members to the FCA's draft guidance for supporting mortgage borrowers impacted by the rising cost of living. We are pleased that the focus remains on forbearance tailored to the individual borrower's needs and circumstances.

Summary

- It is unfortunate that sections of the media have misinterpreted the FCA's intent, particularly the section on "providing forbearance at scale." FCA should be absolutely clear that it is not advocating self-service blanket customer led forbearance. Experience tells us that blanket interventions are more likely to mask a borrower's true position and lead to inappropriate outcomes. Forbearance tailored to individual needs and circumstances is always the best course of action as highlighted in all of FCA's publications on this subject.

  The only experience some customers have had of lender forbearance was Covid-19 payment deferrals, which were granted on demand as per Government and FCA directive. In light of this it is important that customers' expectations are managed carefully.

- In respect of product switching, we do not feel it is appropriate for lenders to undertake any form of affordability assessment when customers are looking for a simple like-for-like switch. FCA should clarify that even if the reversion rate is lower than the new product rate, lenders do not need to apply an affordability test per MCOB 11.6.3R due to "material changes to affordability".

- This guidance covers 3 particular cohorts of customers; arrears, pre-arrears and others who fall into neither of these categories but wish to make a contract variation to reduce their monthly payment. It may be difficult for lenders to distinguish between the second and third cohort. We understand why the FCA has included this third cohort, however this does create a risk of conflating clearly understood and defined existing process. It would be helpful if the FCA confirm with this third cohort the onus remains on the customer to self-declare any financial difficulty.
- Unfortunately when read together the individual sections of the draft guidance can appear confusing and contradictory. It would be helpful to tackle the individual forbearance solutions under a single heading. Variation to interest-only is mentioned throughout the document; it would provide greater clarity if this had its own section covering the requirements and implications for each customer cohort. Customer journey flow charts for each scenario would be very useful and help avoid misinterpretation.
- "Rising cost of living" should be defined, it could be argued that the cost of living has been rising for decades. We believe that FCA's intention is to address the reduction in disposable income caused by high inflation. If this is the case FCA should say so. Without definition this becomes an open-ended consideration for lenders which could cause problems when the economy recovers. Over-forbearance could become entrenched in some firms. Whilst the pandemic felt like a challenge in need of short term solutions, cost of living and interest rate rises seem likely to be with us into the medium term. Short term solutions will not fix the issues without more significant lifestyle changes.
- FCA has gathered a wealth of information during the pandemic moving into the current difficult economic environment, via supervision activity and numerous lender requests for information. We welcome FCA intention to consult on its "temporary" Tailored Support Guidance (TSG) in the near future. As discussed below consolidation of relevant rules and guidance is important.

General Comments

Consolidation of guidance

Given the recent flurry of FCA publications about supporting customers in financial difficulty, it is helpful that the FCA looks to consolidate this information into short guidance. This will be particularly welcome for firms who may need to adapt their existing processes in order to deal with increased volumes of customer contact.

We believe the following publications are most relevant;

- Mortgages and Coronavirus; Tailored Support Guidance (TSG)
- Borrowers in Financial Difficulty Report (BIFD)
- The June Rising Cost of Living Dear CEO letter
- Existing handbook requirements
- TR18/5 Management of long-term mortgage arrears & forbearance

We suggest FCA incorporates the key messages from the above documents. For example, one notable exclusion from this guidance is FCA expectations around referrals into debt advice. FCA has previously highlighted this is an area that firms need to improve.[1] FCA may want to remind firms of expected practice and the perimeter boundaries for debt counselling.

[1] BIFD report November 2022, section 3.09 & 3.10

It would also be helpful to reference impairment provisioning, particularly in respect of pre-arrears and non-forbearance related contract variations. *FG 11/15 Forbearance and Impairment Provisions Mortgages 2011* seems very relevant. Best practice outlined in this document may be more challenging for firms who utilise self-serve as allowed by the handbook for non-forbearance related contract variations.

Clearly firms will also need to pay strong consideration to the guidance on the treatment of vulnerable customers and the new Consumer Duty.

Providing forbearance

Both this guidance and the customer facing information have a strong focus on contract-variations. Some consumer champions and sections of the media have called for blanket solutions such as temporary interest-only. Both this guidance and the consumer facing information does little to explain that these solutions are not suitable for all, with lenders only offering forbearance suitable to the individual customer.

FCA recent publications[2] and this guidance apply to "*borrowers in financial difficulties due to the rising cost of living and those who have not yet missed a payment".* The TSG was introduced to support those impacted by the pandemic. It was fairly simple to determine whether or not somebody had been impacted by Covid-19, for example they may have had ill health or their employer may have utilised the furlough scheme. The rising cost of living impact is not so easy to define. In simple terms we see this as the impact of rising inflation on the cost of goods and services. If somebody loses their job, it is difficult to determine whether this is due to the "rising cost of living".

FCA has outlined that firms should offer forbearance to help borrowers avoid, reduce or manage any payment shortfall. This includes borrowers who have not yet missed a payment. A pre-arrears customer would typically be defined as a customer who has yet to have a payment shortfall/arrears position on their account, but who has been identified (through an income and expenditure assessment) as being reasonably expected to be unable to afford their full contractual monthly payment at a specified time in the foreseeable future.

FCA should confirm that the guidance is not intended to indicate that an income and expenditure assessment at the point of entry into a pre-arrears or arrears support process is no longer required. This affordability assessment typically includes consideration of the causes of financial difficulty and the borrower's financial outlook remain necessary for the provision of tailored support.

Providing forbearance at scale

We welcome FCA providing this guidance for firms who may wish to take a more automated approach. This may be particularly helpful in the event of a significant economic event such as a sharp rise in unemployment.

The guidance explains how firms might automate forbearance by grouping particular cohorts of customers with similar needs and circumstances and offering a range of solutions that may be appropriate. In our view this type of approach may be difficult to reconcile with the FCA's expectations around Consumer Duty. The FCA may want clarify this point, although we expect

[2] Mortgages & Coronavirus; Tailored Support Guidance 21, Dear CEO letter "Rising Cost of Living", June 22

the majority of our members will not utilise this automated option. It is more likely some of our members automate some of the information gathering exercises such as income and expenditure to free up more time for call-handlers to discuss the most appropriate forbearance solution with the customer.

It is unfortunate that some have conflated this section with lenders offering self-certified contract variations. FCA should be clear that all existing rules concerning the application of forbearance options still apply. These robust rules are important to ensure suitable outcomes.

It would be helpful for the FCA to clarify that contract variations which currently can be conducted on a self-serve basis do not require any additional checks to test the customer's financial position. The onus should be for the customer to declare any financial difficulty now or in the future, noting that lenders should provide effective signposting to support the straightforward declaration of financial difficulty. Where a borrower self-identifies as having no financial difficulty and the lender has included the above step, FCA should confirm the lender has met their obligations. We discuss this further in the contract variation for non-forbearance section.

Contract variations for the purposes of forbearance

A contract variation is one option in a range of forbearance tools that may be used to provide tailored support in a pre-arrears or arrears scenario. Both this guidance and the customer facing webpage make numerous mentions of temporary interest-only switches. This has been picked up by the media, who have interpreted it as a relaxation of the current rules. FCA should confirm that the guidance is not intended to suggest that the choice of forbearance option (or other support) should always be a contract variation, or that a contract variation is always the FCA's preferred option.

This guidance explains how switching borrowers to interest-only without a credible repayment strategy on a temporary basis is permissible. We expect this to be a popular customer request for the reasons outlined. However the guidance fails to recognise the difficulty in determining with confidence that the customer will be able to resume full capital and interest repayments in a difficult economic environment.

Once the temporary period is over the customer's circumstances may have changed and they may no longer be able to afford the payments. This then adds to the existing interest-only maturity problem the FCA is currently trying to tackle. We are concerned that this gives consumers the impression that lenders should offer temporary interest-only on demand. Lenders doing this expose themselves to significant risk. We expect our members will want to continue with a robust process to ensure suitability of the given forbearance solution per Principle 6, MCOB 2.5A.

Implications of forbearance arrangements

The masking of credit information has a significant impact as the FCA is aware[3]. It is appropriate that forbearance will continue to be reported as per normal process. However, credit file reporting understandably remains a significant concern for borrowers.

It may be worth reminding firms that temporary arrangements for customers not having a payment shortfall do not constitute an 'Arrangement' in terms of credit reference reporting requirements. Inadvertently filing an 'Arrangement' in such circumstances could lead to customer detriment.

On firms providing information on the impact of differing payments of interest or capital and any total amount payable, we would appreciate clarity on whether this can be verbal or in writing and if it can be illustrative or specific?

Customers not requiring forbearance – but wanting to reduce their monthly payments (contract variations)

In practical terms it may prove difficult for lenders to distinguish between this cohort and pre-arrears customers. This group is difficult to define. For example, it could include customers rolling off fixed rate mortgages and moving to a new higher rate or individuals who simply wish to make variations to their mortgage for unrelated reasons. This particular cohort of customer would need to self-declare financial difficulty as per existing rules and process. FCA should confirm that there are no obligations on lenders beyond this.

As highlighted by the guidance, customers can conduct some of this activity without advice or the need for affordability assessments. Existing contract-variation processes such as simple product switches and term extensions should not be disrupted by introducing steps to test the borrower's ability to meet their mortgage payment. These self-serve options will signpost access to support for borrowers experiencing financial difficulty, giving the customer the opportunity to drop out of the online journey and speak to an advisor who would assess their circumstances and take the appropriate action. Firms will be mindful of both the importance of providing clear information about the ability to seek support, and the need to operate account management journeys that do not slow down and inconvenience individuals wishing to make simple adjustments to their mortgage.

Interest rate switches

Mortgage lenders do not assess affordability where an internal customer is up to date with payments and looking to switch product without any additional borrowing. This is not co-

[3] FS20/6 June 2020 Section 2.44

incidental. The voluntary industry agreement on switching[4] was agreed after extensive discussions with FCA following on from the Mortgage Market Study[5]

FCA confirms that where the new rate is higher than the previous rate, as long as the reversion rate is higher firms can dis-apply MCOB 11.6.3R. As the FCA is aware recent economic uncertainty created the unusual situation of some reversion rates being lower than initial product rates, although this has largely corrected itself, we believe there are still examples of this in the market. We do not believe that there are any circumstances where an affordability assessment would be warranted on a like for like switch. A requirement to do so may disrupt a customer's ability to switch. Some borrowers may fail this test. What options would this leave the borrower and lender?

The requirement for an affordability test per MCOB contradicts recent industry activity and FCA comment, and it could result in poorer outcomes for borrowers. The Mortgage Market Review (MMR) introduced this rule. PS12/16 states that an affordability assessment is not required for a "*rate switch or retention deal*", it must be noted that it makes no mention of a comparison with any prevailing SVR. Three examples of changes that are likely to be material to affordability are shared[6]. It is surprising that the scenario described above is not mentioned.

We seek clarity on this rule. Without this clarity lenders may be required to build controls which would stop borrowers proceeding through journeys in the scenario described and could risk adding to the mortgage prisoner population.

Term extensions

No comments.

Variation to interest-only

Whilst most lenders will offer temporary interest only as a forbearance tool, it is unlikely that most lenders offer permanent switches to interest-only for non-forbearance reasons.

Implications of contract variations

No comments

Exceptions to the requirement to provide advice

No comments

FCA customer facing information

FCA outlines different forbearance options such as term extension, moving to interest-only and temporary switch to interest-only. FCA has focused solely on contract-variations. We expect that customers will have a preference towards the options outlined by the FCA and

[4] Industry Voluntary Agreement on Switching 2018

[5] MS16/2.3 Mortgage Market Study Final Report 2019

[6] PS12/6 Mortgage Market Review 2012 Section 3.11.

other consumer advocates. This immediately puts the lender on the back-foot when they carry out an assessment and then offer the most suitable option to the customer. We suggest the FCA explain what the normal customer journey would look like, i.e. contact your lender, they will assess your needs and circumstances via an income and expenditure exercise and then offer you the most suitable forbearance option.

Our members recognise the importance of keeping people in their homes and the long term detriment of repossession and homelessness. It is incumbent on the FCA to emphasise to individuals that the cost of living is increasing and that it is important for consumers to live within their means and adapt lifestyles as necessary. This is what many people will already be doing as a matter of course. Mortgage lenders should not be in a position where they reduce payments for those who are living beyond their means so that an unsustainable lifestyle can be maintained, postponing for another day the point when the mortgage has to be repaid.

It is important that individuals understand the importance of first of all assessing what they can do to help themselves, and if they are still in difficulty, working with their lenders to see what support assistance and forbearance is suitable.

Next Steps

Although this guidance introduces nothing new it is likely to influence customer behaviour, members may need some time to consider this alongside other recent publications. FCA should give lenders some-time after the holiday period to digest and prepare.

Given that "cost of living" challenges may be with us for some time, we look forward to FCA consolidating some of its temporary guidance into the handbook via the upcoming consultation on the TSG.

We appreciate FCA's collaborative approach and continued engagement on this important matter. If you would like to discuss this response please contact harinder.chohan@bsa.org.uk.

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The Building Societies Association (BSA) is the voice of the UK's building societies and also represents a number of credit unions.

We fulfil two key roles. We provide our members with information to help them run their businesses. We also represent their interests to audiences including the Financial Conduct Authority, Prudential Regulation Authority and other regulators, the Government and Parliament, the Bank of England, the media and other opinion formers, and the general public.

Our members have total assets of over £481 billion, and account for 23% of the UK mortgage market and 18% of the UK savings market.