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Treasury Committee

Mortgage arrears and access to mortgage finance

Fifteenth Report of Session 2008–09

Report, together with formal minutes, oral and written evidence

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Summary

Arrears and repossession levels

Being in arrears and facing the threat of repossession are distressing experiences. Both mortgage arrears and repossession levels are on an upward trend, which is expected to continue in the next few years.

Lender flexibility and forbearance

The evidence we have received suggests that mainstream lenders are, broadly speaking, complying with the FSA's mortgage conduct of business rules. Indeed, we have heard positive examples of some mainstream lenders taking pro–active steps to support consumers in mortgage difficulties. That said, we are extremely concerned by evidence of a lack of flexibility and forbearance in the sub-prime, specialist and second charge sectors to homeowners in arrears. We recommend that the FSA monitors the forbearance policies of mortgage lenders to ensure that repossession is only a tool of last resort.

Mortgage arrears charges

We share the serious concern expressed by many of our witnesses that some lenders are charging high and excessive mortgage arrears fees to customers who fall into mortgage difficulties. Such practices are intolerable, placing additional strain on homeowners already struggling to keep up with their mortgage payments. We note that the FSA has already referred four mortgage firms to enforcement action and understand that part of the case against some of these firms is based on excessive mortgage arrears charges. We suspect these cases represent the tip of the iceberg and call upon the FSA to take a much more robust stance towards tackling and eliminating unfair arrears charges

The lender lottery

We share the concerns expressed by groups such as Shelter, Which? and Citizens Advice that the FSA's principles–based approach in the area of mortgage arrears has given far too much flexibility to lenders to interpret the rules as they wish. The consequence has been a wide divergence in practice amongst firms with consumers treated in an inconsistent manner and little way of establishing whether they are being treated fairly. We agree with the Financial Services Consumer Panel that there is an urgent need for more rules or a more explicit statement of the requirements on firms in guidance to help put some 'grit into the system'.

FSA enforcement

The seemingly leisurely approach of the FSA in terms of completing its mortgage arrears review and enforcing possible breaches in the rules in the area of mortgage arrears is a matter of grave concern. We call upon the FSA to spell out clearly in its mortgage market review how it will improve its performance in terms of bringing miscreant firms to book.

Naming and shaming miscreant firms

Currently the FSA only publishes the names of firms it has found guilty of wrongdoing once enforcement action against the firm has been concluded. The industry has told us that it supports the continuance of this approach, although others have argued that this places the interests of lenders ahead of those of consumers. We have concerns that the balance between disclosure to the public and the need to protect firms before they have been found guilty of wrongdoing has tilted too far towards the interests of the industry.

Government support for homeowners in mortgage difficulties

We welcome the measures which the Government has introduced to support homeowners in mortgage difficulties. However, the need for the introduction of a large number of new initiatives as well as the amendment of schemes in place before the current crisis suggests that adequate safety nets for homeowners in mortgage arrears and/or at risk of repossession were not in place prior to the current recession. We recommend that the Government re-examine its longer-term strategy towards supporting homeowners in mortgage difficulties to ensure that adequate mechanisms to support homeowners are in place even once the current downturn has ended.

Mortgage rescue scheme

The Mortgage Rescue Scheme has directly benefited just six households, despite being designed to assist upwards of 6,000 households. We call upon the Treasury and the Department of Communities and Local Government to explain why their projections for participation in the scheme appear to be so out of step with the picture on the ground and request analysis as to whether this reflects flaws in forecasting, poor design of the scheme or lack of consumer demand.

Securitisation

We are concerned by evidence we have received that certain securitisation agreements and covenants may restrict the ability of lenders to offer forbearance and greater flexibility to homeowners in mortgage difficulties and may restrict their ability to participate in the Home Owners Support Scheme. To this end, we call upon the FSA to move quickly to ensure that securitisation agreements already in place do not act as an obstacle to treating consumers in mortgage difficulties fairly.

Mortgage finance

First time buyers face barriers to getting on the property ladder, such as high deposit requirements and restrictive lending criteria. While we are not advocating a return to past levels of lending, it appears that more needs to be done to help credit–worthy first time buyers access credit. It is likely that restricting some first time buyers has negative effects on an already depressed housing market.

1 Introduction

1. The desire to own property is firmly entrenched in UK society. Home ownership has been an aspiration for recent generations. Whereas at the end of the First World War 80% of households rented from private landlords, home ownership levels now constitute around 70% of all households.[1] Gaining a foothold on the property ladder has, however, become more and more difficult as property prices have risen dramatically in recent years. Many individuals have taken on huge debt burdens, often encouraged by the very permissive lending policies of some major financial institutions.

2. The impact of the recent economic crisis on households has been very considerable. As was the case in the early 1990s, a variety of causes have conspired to increase mortgage arrears and consequently repossessions. Kay Boycott, Director of Communications, Policy and Campaigns at Shelter, told us that her organization estimated that some 6.5 million households were subject to "stress and depression" as a result of their housing costs.[2] People's identities are closely bound up with where they live, and the trauma of having that home repossessed can be very considerable. The downturn in the buy-to-let market and falling rental yields have also meant that the private rented sector has been subject to upheaval with many of those renting property also discovering that mortgage arrears and repossession could affect their lives.

3. We undertook this short inquiry as a follow-up to our wider study of the banking crisis over the last 18 months. We wanted to see how the wider crisis was having an impact on people's lives. We have looked elsewhere at the tangled complexities of the global financial system, a world of credit default swaps, synthetic products, toxic assets and securitized debts. Such abstract terminology seems far removed from the realities of everyday life, but some of the evidence we have received shows how the credit crunch has actually unfolded in households across the UK. Citizens Advice offered a case study of a woman in Cheshire, reported to one of its bureaux:

> A single woman … reported that because she could no longer maintain payments to her non-priority creditors and had fallen into arrears with mortgage and secured loan. The client told the CAB that she had been working 55+ hours per week in an attempt to maintain payments and relying on family contributions. She had a first mortgage of £81,000, and two secured loans, one for £39,000 and the other for £7,600 on a home worth £125,000. Her credit debts totalled £28,000 and had mostly taken out 2–3 years ago to support her unemployed ex-boyfriend. The client told the CAB that she had experienced severe problems with the secured lender to whom she owed £7,600. Although she told this lender that she was considering bankruptcy as a way of dealing with her debt problems, they continued to call her every day making

1 Council for Mortgage Lenders, *Housing Finance Issue 02* (2007), p 3

2 Q 46

> threats of recovery action. The calls included calls to her workplace, and debt recovery agents for the lender passed messages for the client to her colleagues.[3]

4. In another case study, a lone parent in Surrey with two children came back from holiday to the property she had been renting for 10 months to discover that the locks had been changed. A notice announced that a possession order had been made against the property. She was "let … in under supervision [from the lenders] for ten minutes to collect a few necessary possessions, including her son's GCSE work".[4]

5. We announced our inquiry on 17 June with the following terms of reference:

> The inquiry will focus on households affected by the recession and struggling with mortgage arrears and/or at risk of repossession, as well as problems in accessing finance for FTBs [First Time Buyers]. Evidence is sought on:
>
> • the current number of homeowners in mortgage arrears and forecasts for the trend in mortgage arrears over the medium-term
>
> • the number and characteristics of homeowners who have had their properties repossessed, the number in the process of having their homes repossessed, as well as forecasts for the trend in repossession levels over the medium-term
>
> • the treatment by, and the approaches taken, by mortgage lenders towards homeowners in arrears and/or at risk of repossession, including issues relating to the treatment of homeowners by financial institutions specialising in mortgage lending to sub-prime borrowers
>
> • adherence to, and the effectiveness of, Financial Services Authority (FSA) rules and guidance for mortgage lenders on repossession policy and treatment of consumers in arrears as well as the FSA's regulatory approach in this area
>
> • adherence to, and the effectiveness of, codes of conduct, protocols and statements of good practice issued by industry bodies in this area
>
> • issues of concern around the operation of sale and lease-back schemes
>
> • the success of those Government schemes in existence before the financial crisis to support homeowners facing difficulties with mortgage payments and/or at risk of repossession, as well as the effectiveness of initiatives introduced since the financial crisis began; and
>
> • the impact of the credit crunch on access to mortgage finance and the terms on which such finance is offered for first time homebuyers.

6. On 30 June we took evidence from Citizens Advice, Which?, Shelter, the British Bankers' Association, the Building Societies Association, the Intermediary Lenders Association, the

3 Ev 9

4 Ev 12

National Landlords Association and the Council of Mortgage Lenders. On 7 July we heard from the Financial Services Authority, Lord Myners, Financial Services Secretary HM Treasury and John Healey MP, Minister for Housing, Department of Communities and Local Government. We also received some 26 memoranda which have informed our work. We are extremely grateful to all those submitting both written and oral evidence.

2 Mortgage arrears and repossession levels

The picture today: mortgage arrears

7. The most cited sources of mortgage arrears levels in our evidence were those from the Council for Mortgage Lenders (CML) and the Financial Services Authority (FSA), who both regularly release such figures. The CML suggested that there were 205,300 cases of arrears in the first quarter of 2009, an increase of 12% from the previous quarter.[5] The FSA also produced statistics on mortgage lending in the first quarter of 2009. At the end of that quarter, their data showed that 399,000 loan accounts were in arrears of at least 1.5% of the current loan balance.[6] Arrears had risen by 6% compared to the previous quarter and one third compared to one year earlier.[7]

8. The two organisations' measures of arrears differed largely because of the different mortgage types each counted in their statistics and the different maximum level of arrears that they chose to include. For example, the CML's measure of arrears included buy-to-let mortgages but did not include second charge mortgages.[8] Also the CML measure of arrears only counted loans with arrears of 2.5% or more of the mortgage balance while the FSA's figure included all loans with arrears of at least 1.5% of the outstanding balance.[9]

9. Statistics on arrears are usually reported in one of two ways:

- either, the number of households more than a certain number of months in arrears;
- or, the number of households where arrears total x% of the outstanding balance of the mortgage.

The first measure is calculated as accumulated arrears divided by the current monthly payment. Monthly payments are a function of the mortgage interest rate charged, which varies over time. When a household's mortgage interest rate changes, that household can instantly switch from being in arrears to being excluded from the statistics. Thus the interest rate affects the number of months measure more than the percentage of outstanding balance measure. The strength of the influence of the interest rate on the number of months measure also distorts historic comparisons of arrears levels. For these reasons, we have considered only the second measure of arrears.

The picture today: repossessions

10. The CML informed us there were 12,800 repossessions in the first quarter of 2009, an increase of 19% from the previous quarter and over a third from the previous year.[10] FSA

5 Ev 77

6 Financial Services Authority, *Statistics on Mortgage Lending*, June 2009, para 17

7 *Ibid.*

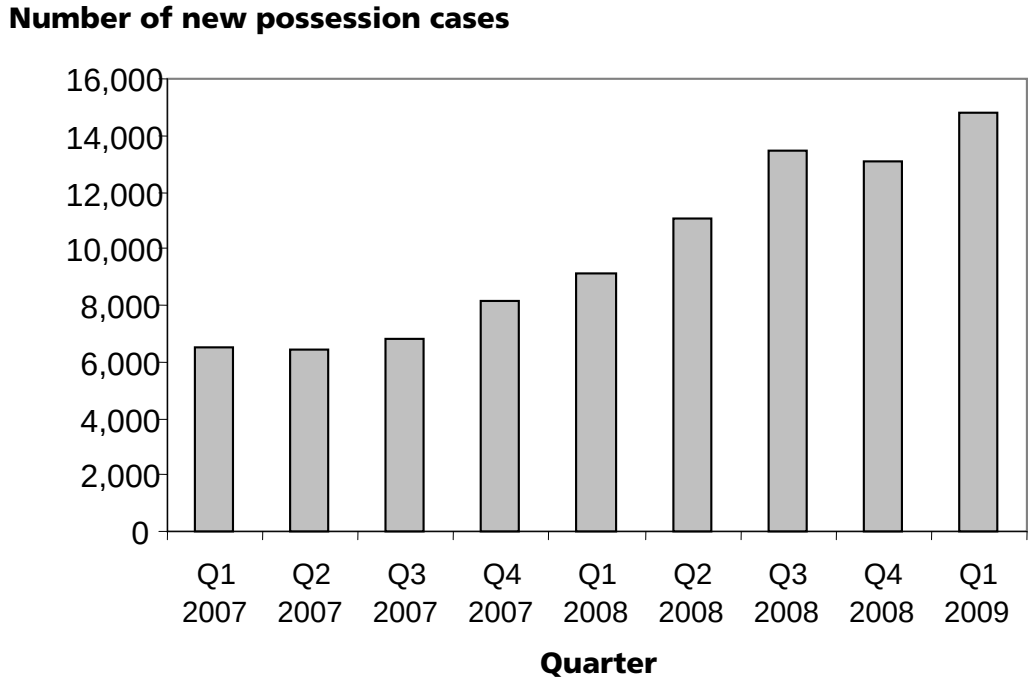
8 Ev 76, 81

9 Ev 77; Financial Services Authority, *Statistics on Mortgage Lending*, June 2009, para 15

10 "First quarter figures suggest 75,000 repossessions this year now looks pessimistic, say CML", Council of Mortgage Lenders press release, 15 May 2009

data showed 14,825 new cases were taken into possession[11] in Q1 2009.[12] This was 13% higher than Q4 2008 and 62% higher than Q1 2008.[13] Despite the large increases in possessions, The FSA figures showed the rate of increase had slowed in the past two quarters, compared to the first three quarters of 2008.[14]

Figure 1: New possessions per quarter



Source: Financial Services Authority, Statistics on Mortgage Lending, June 2009

11. We received evidence about the characteristics of those likely to be repossessed. Shelter informed us that common characteristics included:

- those at the lower end of the income range at which home ownership is possible;
- those made redundant or who have had their income reduced;
- those experiencing relationship breakdown;
- vulnerable households, first–time buyers and the self–employed;
- those who lack basic financial capability and with significant other debts.[15]

11 The FSA define a possession as 'an arrears case where the lender, having formally been granted a Possession Order by a Court, is then able to sell the underlying property and use the proceeds to reduce or pay-off the mortgage debt'.

12 Financial Services Authority, *Statistics on Mortgage Lending*, June 2009, para 20

13 *Ibid.*

14 *Ibid.*

15 Ev 130

As well as this, the Building Societies Association suggested that the characteristics of those who have been repossessed included being "unwilling to make realistic arrangement, based upon their circumstances"[16] and delaying contact with their lender until the situation becomes "too serious". [17]

A bleak future?

12. One of the few areas in which the evidence from the charities, consumer groups, the mortgage industry and the regulator concurred was that arrears and repossessions are likely to rise in the future. However, there was much variation around the potential magnitude of the increases. The CML only provided us with forecasts for 2009.[18] They explained that there was too much uncertainty to produce longer term forecasts.[19] They believed there would be 360,000 borrowers in arrears and 65,000 repossessions by the end of 2009.[20] Volterra Consulting predicted repossessions in 2009 to be slightly higher at 67,000.[21] The FSA told us that they did not produce forecasts, though in written evidence they stated that mortgage arrears and repossessions were likely to reach levels similar to those seen in the early 1990s, when annual repossessions were over 70,000.[22] The highest forecast for future repossessions we received was that from Ian Shepherdson, Chief U.S Economist at High Frequency Economics, who estimated repossession levels would reach 100,000–120,000 by 2011.[23] The Government also told us that they did not forecast repossessions.[24]

13. Some witnesses suggested that repossession could sometimes be in the longer term interests of the consumer. The Financial Services Consumer Panel explained that

> If someone cannot afford the interest payments on their [mortgage] loan their debt will increase. If they struggle to make whatever payments that can be negotiated at the same time as their debt is increasing experience is that within 6 months to 2 years they see that they are better off giving up, realising whatever equity that may still be available, and moving to rented accommodation (where they may be eligible for Housing Benefit.)[25]

14. **Being in arrears and facing the threat of repossession are distressing experiences. The evidence we have reviewed shows that both mortgage arrears and repossession levels are on an upward trend, which is expected to continue in the next few years. As**

16 Ev 55

17 *Ibid.*

18 Ev 77

19 Q 188

20 Ev 77

21 Ev 139

22 Q 205, Ev 121

23 Ev 130

24 Q 272

25 Ev 151

recent global events have shown, the fortunes of economies are intimately bound up with that of their housing markets.

What drives repossession?

15. It is important to understand the drivers of repossession in order to provide solutions whether these come from the Government, lenders or regulators.

16. Shelter listed the main factors which could lead to a second wave of repossessions. These included:[26]

- interest rate rises;
- an expected increase in unemployment;
- the lack of mortgage availability; and
- the time–limited nature of Government schemes to help those with mortgage difficulties.

17. One potential issue which provoked disagreement among those who submitted evidence was whether lender forbearance would diminish as house prices recovered, leading to further repossessions. Shelter and Citizens Advice believed that lenders would respond to house price rises by being quicker to repossess.[27] Ms Edwards, Head of Consumer Policy at Citizens Advice, had seen this happen during the last recovery in the housing market, when she worked as a debt advisor:

> In 1996–7 as we began to see house prices increase in East London we certainly saw a lot of lenders who had been forbearing for a while suddenly take possession action because house prices were increasing.[28]

However this view was not universally accepted. Lord Myners, Financial Services Secretary to the Treasury, told us that he did not agree that lenders would forbear less once the housing market started to improve.[29] He explained that in an environment where people were confident about the economic outlook, lenders would not be willing to "curtail the size of their books".[30]

Comparison with the last recession

18. The FSA described current repossession levels as similar to those of the 1990s, despite significant differences in the housing market and wider economy.[31] Perhaps most notably, mortgage interest rates stayed at 14% from 1990 until autumn 1992 while today interest

26 Ev 131

27 Ev 132, Q 25

28 Q 25

29 Q 270

30 *Ibid.*

31 Ev 121

rates have fallen dramatically.[32] The FSA reasoned that the key factors contributing to repossessions today were not the same as those in the last recession.[33] It explained how the shape of the mortgage market had altered over the past 20 years. Mortgage equity withdrawal was far more prevalent in 2007 relative to the 1990s as borrowers topped up their income by remortgaging.[34] The FSA believed that the increasing reliance on equity withdrawal could not endure. They described how throughout 2009–10, a fall in house prices, increasingly restrictive lending criteria and the effective termination of the specialist lending market would mean that borrowers with high debt levels would not be able to refinance outstanding debts.[35] This could trigger an increase in repossession.[36] The FSA also noted the increasing use of unregulated credit and buy-to-let mortgages in recent years which led to losses for landlords when house prices fell[37]

> …even where the original lending decision looked to be affordable, affordability was severely compromised by the overall level of debt secured against their home, including second charges and other forms of unregulated credit."[38]

19. **Much uncertainty remains as to whether any recovery in the housing market would mitigate or exacerbate the scale of repossession. We recommend that the FSA monitors the forbearance policies of mortgage lenders to ensure that repossession is only a tool of last resort.**

32 Ev 121

33 *Ibid.*

34 *Ibid.*

35 *Ibid.*

36 *Ibid.*

37 Ev 122

38 *Ibid.*

3 The regulatory framework

The framework for regulating mortgages

20. The Treasury announced in January 2000 that it would introduce a statutory regime for regulating mortgages, replacing the system of voluntary regulation under the Mortgage Code. The FSA assumed responsibility for regulating mortgage lending, administration, advice and arranging in October 2004, when the mortgage conduct of business rules came into effect. As a result all first charge loans over residential property entered into on or after 31 October 2004 are regulated by the FSA. The FSA's responsibility was initially limited to first–charge mortgages on residential properties and lifetime mortgages, but in April 2007 their responsibility was extended to cover home reversion and home purchase plans.[39]

21. The FSA does not regulate second charge lending—a second charge mortgage is a mortgage secured against an asset such as a house which is already granted as security to the first charge lender—which is the responsibility of the Office of Fair Trading (OFT) under the 1974 Consumer Credit Act.[40] We note that in certain respects consumers are better protected under the Consumer Credit Act However, there are many commentators who are calling for the FSA to take over the regulation of secondary lending.[41]

22. **We believe that the issue of the regulation of second charge mortgages should be reviewed by the Government. This Report focuses mainly on the principles and rules relating to first mortgages regulated by the FSA and it would be a cause for concern if second mortgages (likely to be taken out by those with greater needs) were less well regulated**

23. Neither does the FSA regulate buy-to-let (BTL) mortgages. This is because when the Government introduced mortgage regulation through the FSA it drew a distinction between occupiers who faced losing their homes if things went wrong, and BTL landlords, whose properties are investments and who do not face the risk of losing their home. As a result consumer protection regulation was not extended to BTL mortgages.[42] Finally, the FSA assumed responsibility for regulating sale and rent back (SRB) schemes on 1 July 2009.[43]

24. The FSA's mortgage regime includes rules and guidance for mortgage lenders on arrears and repossessions, with the aim of ensuring that customers are treated fairly when they fall into mortgage difficulties. This is contained in section 13 of the mortgage rules. More specifically, the mortgage conduct of business rules in this area state that "a firm must deal fairly with any customer who (a) is in arrears on a regulated mortgage contract; or (b) has a mortgage shortfall debt". It goes on to state that "firm must put in place, and

39 Ev 122

40 Ev 123

41 Ev 151

42 Ev 123

43 Ev 122–123

operate in accordance with, a written policy (agreed by its respective governing body) and procedures for complying with the requirement to deal fairly with customer in arrears. Such written policy and procedures should include:

- using reasonable efforts to reach an agreement with a customer over the method of repaying any payment shortfall or mortgage shortfall debt;
- adopting a reasonable approach to the time over which any shortfalls in payments can be made good; and
- liaising, if the customer makes arrangements for this, with a third party source of advice regarding the payment shortfall or mortgage shortfall debt.

Importantly, the mortgage conduct of business rules state that repossession of the property should only take place "where all other reasonable attempts to resolve the position have failed". Additionally, charges imposed on a customer in arrears should not exceed a reasonable estimate of the cost of the additional administration required as a result of the customer being in arrears.[44]

25. There are also various industry codes of conduct that sit alongside the FSA's mortgage conduct of business rules. The CML has published industry guidance on arrears and repossessions which it explained expanded on "treating customers fairly, existing mortgage conduct of business rules and other issues raised by the FSA and the Financial Ombudsman Service".[45] The CML guidance in this area is voluntary, although CML believed that it had been widely adopted by its members and that many members had undertaken gap analysis between this guidance and their arrears policies.[46]

The lender lottery

26. We requested evidence on the treatment by mortgage lenders of homeowners in arrears or at risk of repossession as well as their adherence to the FSA's rules in this area. Shelter explained that, whilst there had "certainly been a significant improvement in practices towards homeowners in difficulty among many lenders", there were still "variations in practice" which meant that some borrowers were "particularly vulnerable to harsh or unfair treatment".[47] Kay Boycott, Director of Communications, Policy and Campaigns for Shelter, expanded on this theme, explaining that there were also "variations within lenders" as well as between lenders which meant that borrowers with the same lender were often being treated very differently.[48] Shelter concluded that these differences in treatment by lenders towards households in mortgage difficulties had led to what is described as "the lender lottery".[49]

44 FSA, *Mortgages: Conduct of Business,* January 2007

45 Ev 79

46 *Ibid.*

47 Ev 132

48 Q 30

49 Ev 132

27. Citizens Advice and Shelter both cited research that they had jointly undertaken (together with AdviceUK and the Money Advice Trust) on the treatment by lenders towards households with mortgage and secured loan arrears. The results of the survey—based upon interviews with both advisors and borrowers—showed that, of those in mortgage arrears, some 57% were satisfied with the way they were treated by their lender, but that 27% said their lender offered them no help when told about their repayment problems.[50]

28. Both Shelter and Citizens Advice pinpointed poor arrears management practices amongst "sub-prime lenders" and "second charge lenders" as a particularly problematic area.[51] Ms Jackie Bennett, Head of Policy for CML, agreed that there were particular problems amongst second charge lenders. She said that feedback from her members indicated that some homeowners were in "trouble because they have second and other unsecured charges against their properties".[52] She added that it was not necessarily the first charge mortgage that was the problem, but often other borrowing.[53] Shelter also highlighted a separate piece of research that it had conducted specifically with respect to sub-prime lenders, which they argued demonstrated "particularly poor practice among sub-prime lenders":

- 20% of those falling behind with payments reported that their lender had not been in contact with them;

and that amongst those who had been in contact with their lender,

- 38% rated their lender's willingness to renegotiate a new payment plan as poor or very poor as against 27% who rated it as good or excellent
- 48% reported the range of options discussed with their lender as poor/very poor, compared with 21% who said this was good or excellent.[54]

Shelter argued that "there were a number of practices—particularly among sub-prime lenders—that clearly contravene FSA rules and guidance",[55] whilst Ms Sue Edwards, Head of Consumer Policy for Citizens Advice, told us that the results of its research work indicated that "mainstream lenders were much better at offering forbearance than sub-prime and second charge lenders".[56] Ms Edwards went on to tell us that Citizens Advice had seen "some cases where lenders were not complying" with MCOB 13.[57] Citizens Advice also expressed strong concerns that, whilst MCOB [FSA: Mortgages and Home

50 Ev 47, 132

51 Ev 48, 132

52 Q 175

53 *Ibid.*

54 Ev 132

55 *Ibid.*

56 Q 24

57 Q 30

Finance Conduct of Business sourcebook] 13 states that repossession should only be used as a last resort, "not all lenders appear to be using court action only as a last resort".[58]

29. We also received evidence that many mainstream lenders were exercising increased flexibility and forbearance towards homeowners in mortgage difficulties. Jackie Bennett told us of the pro-active attempts by some lenders to make contact and engage with consumers in mortgage arrears.[59] The BSA told us that they had worked in conjunction with Money Advice Trust (MAT) to produce a consumer leaflet which gave "straightforward advice on mortgage repayment difficulties". It also outlined some of the measures BSA members were taking to support consumers in mortgage difficulties, including amending the repayment term of the mortgage to interest only, extending the term of the mortgage, payment holidays and changes to the date when mortgage payments were made.[60]

30. The FSA, in its written submission, explained that in late 2007 it had become increasingly concerned by evidence, both from its own mortgage effectiveness review and from external reports by charities such as Shelter and Citizens Advice, "that some mortgage lenders were failing to treat their customers fairly when they fell into arrears".[61] As a result it had reviewed the arrears management policy and practices of a sample of mortgage lenders. The FSA published its findings in August 2008 which concluded that "mainstream lenders were largely complying with our requirements", but that there were particular concerns with specialist lenders, including that the suggestion that they:

- operated a 'one size fits all' approach, focused too strongly on recovering arrears according to a strict mandate, without reference to the borrower's circumstances;
- were too ready to take court action; and
- had lower standards of systems and controls in place to control mortgage arrears handling, including training and competency arrangements.[62]

The review also noted issues with lenders in general, including that some:

- could have done more to consider customers' individual circumstances and offer more options to resolve the arrears problem;
- imposed charges in circumstances that could result in the unfair treatment of customers; and
- did not exercise sufficient oversight of third parties contracted to carry out mortgage arrears and repossessions handling activities on behalf of lenders.[63]

58 Ev 48

59 Q 136

60 Ev 55

61 Ev 123

62 "FSA reiterates call for firms to treat customers fairly in current market conditions", FSA press notice, 5 August 2008

63 *Ibid.*

31. We asked industry representatives for their views on lender practice and adherence to the FSA's rules. The CML told us that adherence to the FSA's rules (TCF [Treating Customers Fairly] and MCOB 13) by mortgage lenders was prevalent and highlighted the FSA's 2008 thematic review of lenders' practices in arrears and repossessions, which found that mainstream lenders were largely complying with the FSA's requirements in this area, demonstrated that "the rules are both effective and are substantially being adhered to". The CML did, however, acknowledge that the FSA had identified "some areas for improvement and the need for further work, particularly in the specialist lending sector" and said that they themselves were working with the sector on this.[64]

32. **The evidence we have received suggests that mainstream lenders are, broadly speaking, complying with the FSA's mortgage conduct of business rules. Indeed, we have heard positive examples of some mainstream lenders taking pro–active steps to support consumers in mortgage difficulties. That said, we are extremely concerned by evidence of a lack of flexibility and forbearance in the sub-prime, specialist and second charge sectors to homeowners in arrears.**

Mortgage arrears charges

33. The issue of mortgage arrears charges levied upon people who fall behind with mortgage payments emerged as a major theme of our inquiry. The FSA's mortgage conduct of business rules cover this area and state that:

> A firm must ensure that any regulated mortgage contract that it enters into does not impose, and cannot be used to impose, a charge for arrears on a customer except where that charge is a reasonable estimate of the cost of the additional administration required as a result of the customer being in arrears.[65]

Mr Jon Pain, Managing Director, Retail Markets at the FSA, explained that the rules were "fairly specific" in this area and that there could only be "a recovery of the costs borne by the firm" and the rules were "not designed to allow the firm to generate a profit from handling arrears cases". He explained that, whilst the rules allowed for the recovery of costs, they expected charges to be "proportionate to the costs involved".[66]

34. Which? told us that they were "concerned about the levying of excessive charges on consumers in mortgage arrears" and that these excessive charges worsened the financial position of consumers already in mortgage difficulties.[67] Dominic Lindley, Principal Policy Advisor for Which?, explained that some lenders were "imposing charges of £50 or £60 a month" on people who were in arrears.[68] In its written submission Which? expanded on Mr Lindley's statement and explained that firms were levying a variety of fees and charges on consumers who fell behind with their mortgage payments, including:

64 Ev 79

65 FSA, *Mortgages: Conduct of Business,* January 2007

66 Q 209

67 Ev 59

68 Q 31

- charges of £25 to £35 for missing a payment/direct debit, which could be on top of any fee levied by the consumers' current account provider for missing the payment;
- charges for sending letters/making telephone calls of up to £35 for each occasion;
- monthly administration charges when a consumer is in arrears ranging from £25 to £60; and
- charges incurred if the lender makes an appointment for the consumer with a debt counseller or collection agent of up to £150.[69]

Table 1: Examples of mortgage arrears charges being levied by lenders

Bank / Sub-Prime lender	Monthly arrears fee	Unpaid direct Debit / Standing Order/ Cheque	Arrears letter [sending a letter or default notice to the customer / general correspondence	Visit of debt counsellor or collection agent	Instruction Solicitors / collection costs
Nationwide	£20 [Charged if account is one of more months in arrears and there is no agreement to repay]	£27.50	£10	£95 [described as an arrears visit)	£150 summons fee; £240 solicitor's pre-enforcement litigation costs
West Bromwich	£35	£35	£20	£150	£100
Halifax	Not available	£35	1st letter free, Each further letter/telephone call £35	£100	£125
Abbey	£35	£32	Not available	£79.50	£195 Instruction and £70.50 processing fee
GMAC	£50	£30	Not available	£100	£100
Capstone (Preferred and Southern Pacific mortgages)	£60–rising to £115 a month when they have instructed a solicitor	£25	Not available	Not available	Not available

Source: Which?

Mr Lindley said that lenders had "not justified these charges in any way". He gave the example of one lender whom the FSA had found "trying to recoup its advertising costs against these charges" which Mr Lindley asserted was "totally against the rules".[70] Mr Lindley told us that Which? wanted to see the lenders "open their books and justify these charges and provide a full breakdown of what this £35 or £55 a month is actually supposed to cover in terms of administrative cost". Which? wanted to see not only "lower charges" but also to see all charges suspended where a consumer had "made an agreement with a lender to repay their arrears".[71] Ms Edwards picked up on this point, telling us that Citizens

69 Ev 61

70 Q 35

71 Q 32

Advice Bureaux had seen a lot of sub-prime lenders charging customers in arrears even where the borrower had made a repayment arrangement with the lenders and was sticking to the arrangement.[72]

35. Both Which? and Citizens Advice referred to debt advice charges being made by some lenders.[73] Citizens Advice said it frequently saw cases "where lenders have charged £100 for one of their debt counsellors to visit their customers", with many lenders "making compulsory charges to borrowers for debt advice" before they would "negotiate over an arrears plan.[74] Sue Edwards said that £100 charged for a debt counseller seemed to be "very steep", but noted that such fees were commonplace, even in cases where Citizens Advice were already negotiating with the lender on the client's behalf.[75] She referred to one lender who had asked Citizens Advice to "pay a £60 charge in order to deal with them".

36. We asked industry representatives whether they agreed that some lenders were levying excessive charges on people in mortgage difficulties. Responding to the specific charge about some lenders continuing to charge arrears fees even where an agreement had been reached with the mortgage holder to pay off the arrears, Ms Jackie Bennett, Head of Policy for the CML, explained that its industry guidance was against such practices. She justified arrears charges as being permitted under the rules "for the additional work that having someone in arrears can cause", and went on to explain that there was a "balance to be struck" in this area and that "if the cost was not borne by those people in arrears were not charged it has to be passed on to the wider population", such that "everybody's mortgages would be more expensive".[76] Mr Adrian Coles, Director-General for the Building Societies Association (BSA), suggested that the problem of excessive charging was concentrated in the specialist or sub-prime sector. He argued that "building societies especially are not guilty of the crime that is being suggested", adding that he suspected that "most mainstream lenders would also come into that category".[77] Ms Bennett said that where excessive charges were being levied these could be investigated by the FSA.[78]

37. Jon Pain acknowledged that the FSA had found instances of "inappropriate" and "excessive" charges and that part of the enforcement action it was taking against four firms related to mortgage arrears charges.[79] The FSA would be re-examining arrears charges as part of the mortgage market review, with a view to seeing "whether the rules need amending". Lord Myners expressed his own concern "that charges could be excessive" and agreed that arrears charges should be a major focus of the FSA's work on the mortgage market.

72 Q 34

73 Ev 59

74 Ev 48–49

75 Q 33

76 Q 95

77 Q 94

78 Q 104

79 Qq 209–210

38. In its written submission Which? outlined its suggested remedy to the problem calling on:

- lenders to provide an itemised breakdown of the additional costs their arrears charges are supposed to cover;
- the FSA/OFT to review all arrears charges made by mortgage providers and secured lenders to determine whether they are reasonable with any excessive charges automatically refunded to consumers;
- all arrears charges to be suspended if a consumer has made an agreement to pay off the arrears;
- consumers in discussions with an independent debt agency to be given a 90 day charge-free window in which to negotiate an arrangement for the repayment of arrears;
- consumers to be allowed to change their payment date without charge to help minimise the possibility of missing payments or getting into arrears; and
- double dipping of fees (levying a fee for the missed payment on both the current account and the mortgage) where a consumer has a current account and a mortgage with the same bank should be stopped.[80]

39. **We share the serious concern expressed by many of our witnesses that some lenders are charging high and excessive mortgage arrears fees to customers who fall into mortgage difficulties. Whilst we have not received conclusive evidence that the mortgage arrears charges levied by lenders are excessive and go beyond recouping additional administrative costs, we fear that some lenders are using arrears charges as an alternative profit stream. Indeed, the wide variation in the level of mortgage arrears charges levied by different firms adds weight to such a view.**

40. **Such practices are intolerable, placing additional strain on homeowners already struggling to keep up with their mortgage payments. We note that the FSA has already referred four mortgage firms to enforcement action and understand that part of the case against some of these firms is based on excessive mortgage arrears charges. We suspect these cases represent the tip of the iceberg and call upon the FSA to take a much more robust stance towards tackling and eliminating unfair arrears charges. As a first step we believe lenders must be required to provide an itemised breakdown of the additional costs their arrears charges are supposed to cover. This would help shed valuable light on whether such charges are reasonable and justifiable as industry representatives claimed was the case amongst mainstream lenders. Alongside this, we believe that the FSA and OFT respectively should review all mortgage arrears charges made by mortgage providers and secured lenders to determine whether they are reasonable.**

80 Ev 61–62

Changes to MCOB rules

41. The FSA has said that, as part of its Mortgage Market Review, it will re-examine the mortgage conduct of business rules.[81] We asked witnesses whether the FSA's principles-based approach in this area was ensuring that customers who found themselves in mortgage arrears were being treated fairly, and also whether the rules around mortgage arrears remained effective, given the very different economic climate the UK faced, or whether the rules needed to be amended.

42. A number of organisations criticised the FSA's principles-based approach in this area. Ms Sue Edwards ascribed part of the problem of compliance with the FSA's rules to the fact that the rules were, "a bit vague".[82] Mr Dominic Lindley, for Which?, reiterated this point, explaining that the FSA's rules were "very principles-based" making it "difficult for consumers to know what they [the rules] actually mean let alone the firms".[83] Shelter made a similar point, explaining that a principles-based approach left "far too much flexibility for lenders to interpret [the rules] how they choose", with the consequence that "consumers are not treated consistently and have no way of establishing what is 'fair' practice and what is not".[84]

43. The Financial Services Consumer Panel expanded on this theme in its submission. It explained that MCOB 13 contained "relatively few actual rules that are binding on lenders" and said that it "would like to see either more rules or a more explicit statement of what is required from the guidance". As an example, the Panel cited MCOB 13.3.4 which sets down guidance that firms should give borrowers "a reasonable period of time to consider any proposals for payment". In its view, "it would be reasonable for this to be enshrined as an obligation on firms and perhaps with a specified time period rather than merely guidance".[85]

44. Responding to the charge that the FSA's rules were "vague", Peter Williams, for the Intermediary Mortgage Lenders Association (IMLA), contended that the CML's guidance in this area supplemented the FSA's rules and brought together "principles and practice in a very, very creative way".[86] Adrian Coles, for the BSA, spoke of the "balance to be drawn between principles which are vague … and rules which are so detailed that the lender cannot step outside of the rules and give a tailor–made service to people's particular circumstances".[87] He concluded that the CML's guidance in this area had "got that balance right". We asked Jackie Bennett, Head of Policy for the CML, whether the CML monitored member compliance with their guidelines. Ms Bennett said that, whilst she was unable to tell us how many adhered to the guidelines, she believed that a large number had compared

81 Ev 124

82 Q 30

83 *Ibid.*

84 Ev 133

85 Ev 150

86 Q 117

87 Q 120

their policies and practices against the CML guidance and made amendments where practices fell short.[88]

45. The BSA called for the FSA to be "clear and concise with the requirements upon firms in relation to arrears and possessions, with the aim of making existing rules clearer", but cautioned against "adding additional requirements to MCOB".[89] Jackie Bennett felt the MCOB 13 rules, when combined with CML industry guidance which put "a lot more colour around what lenders should be doing on a day-to-day basis" were "fit for purpose". She explained that the CML had developed guidance in this area because "the high level principles that were set out by the FSA were not detailed enough for lenders to be able to understand exactly what sections meant".[90]

46. However, others disagreed with Ms Bennett's assertion that there was no need to revisit the rules in this area. The Financial Services Consumer Panel explained that the MCOB rules were "written after a period of sustained growth in UK house prices when mortgage arrears were low and when the vast majority of borrowers in arrears had the opportunity to voluntarily sell their properties to repay their debt". It concluded that "with hindsight, there was insufficient regard to ensuring that the rules establish the best balance between the interests of lenders and borrowers for a much more difficult time for the mortgage and housing markets".[91]

47. **We share the concerns expressed by groups such as Shelter, Which? and Citizens Advice that the FSA's principles-based approach in the area of mortgage arrears has given far too much flexibility to lenders to interpret the rules as they wish. The consequence has been a wide divergence in practice amongst firms with consumers treated in an inconsistent manner and little way of establishing whether they are being treated fairly. We agree with the Financial Services Consumer Panel that there is an urgent need for more rules or a more explicit statement of the requirements on firms in guidance to help put some 'grit into the system'. We note the arguments put forward by the industry that the FSA's high–level principles in this area are complemented by more practical industry guidance, but believe the need for industry guidance in this area actually illustrates the deficiencies of the FSA's current approach. Industry guidelines are not a substitute for more robust rules—they are voluntary not binding, there is often little monitoring or supervision and there are no sanctions for non-compliance.**

48. **We note that the FSA has begun moving from a principles to an outcomes-based approach and trust the FSA's Mortgage Market Review, which includes a re-examination of the mortgage conduct of business rules, will lead to a shift in this direction with a better balance between high-level principles and rules that are binding upon firms. The FSA's Mortgage Market Review must also give serious consideration as to whether the mortgage conduct of business rules need revising. The rules were drawn up in the early part of this decade in a very different economic environment and there is**

88 Q 158

89 Ev 56

90 Q 117

91 Ev 150

concern, expressed by the Financial Services Consumer Panel amongst others, that revisions need to be made to ensure the rules are appropriate for the very different economic circumstance prevailing today.

FSA enforcement

49. We requested evidence on the action that the FSA took against lenders who breached its rules in this area as well as its broader regulatory approach towards enforcing its rules on mortgage arrears. As we have noted previously, the FSA announced on 22 June 2009 that four firms had been referred to enforcement and Ms Lesley Titcomb, Director Small Firms and Contact at the FSA, also informed us that the FSA was considering referring a number of other firms to enforcement.[92] We asked Jon Pain how long this enforcement action would take to complete. He told us that the length of time would depend on "their level of complexity, but three to six months is a normal part of that process.[93]

50. Shelter suggested that "there have been serious weaknesses in the FSA's regulatory approach to date, and that overall the FSA has been slow to tackle non–compliance".[94] A similar point was made by the Financial Services Consumer Panel, who expressed concern that, despite the fact that the FSA had written to the chief executives of all mortgage lenders and administrators in November 2008 giving them until January 2009 to ensure that their customers in arrears were being treated fairly, the FSA's June 2009 review found poor practice was still prevalent, particularly amongst specialist lenders and third party administrators.[95]

51. Shelter suggested that the length of time the FSA was taking to conduct its thematic mortgage arrears review was excessive. Between publication of the first phase of the review in August 2008, and the second phase in June 2009, approximately 40,000 more households were repossessed. Shelter also criticised the leniency with which the FSA had treated lenders who were found to have breached the mortgage conduct of business rules. It accused the FSA of adopting "a carrot rather than a stick approach" which had "left borrowers at the mercy of unscrupulous lenders for far too long". Shelter pointed out that, after the first phase of its mortgage arrears review, which found serious weaknesses in the way some lenders were handling arrears, the FSA had called for lenders to treat customers fairly and published examples of good and poor practice, but had taken no enforcement action against specific lenders.[96]

52. **The FSA stated in its submission said that "in late 2007, we became increasingly concerned by evidence, both from our own mortgage effectiveness review and from external reports by charities such as Citizens Advice and Shelter, that some mortgage lenders were failing to treat their customers fairly when they fell into mortgage arrears'. Yet it was not until June 2009 that the FSA announced that it was finally taking**

92 Q 224

93 Q 228

94 Ev 132

95 Ev 150–151

96 Ev 132–133

enforcement action against four firms. Furthermore such enforcement action against these firms could potentially take up to a year to conclude. During this period of time, which included the FSA's investigation, over 40,000 more homes were repossessed. The seemingly leisurely approach of the FSA in terms of completing its mortgage arrears review and enforcing possible breaches in the rules in the area of mortgage arrears is a matter of grave concern. We call upon the FSA to spell out clearly in its mortgage market review how it will improve its performance in terms of bringing miscreant firms to book.

Naming and shaming miscreant firms

53. A major issue to emerge during the course of our inquiry was the FSA's approach towards naming firms against which it is taking enforcement action or which it has found guilty of poor practice or breaching FSA rules. For example, the FSA has not published the names of the four firms currently subject to enforcement action and has not named those firms who had performed poorly in its August 2008 review of mortgage arrears policies and practices by lenders.

54. Jon Pain, for the FSA, explained this was because firms referred to enforcement action were only named once that action was concluded and that "until the full enforcement process is complete, it would be unjust to say they are guilty before they are proven guilty".[97] Eric Leenders, Executive Director responsible for retail banking at the British Bankers Association, offered a similar argument, telling us that the names of firms should "remain confidential" until enforcement action was concluded. He added that "where there is an investigation there is not necessarily guilt" and that where an issue was resolved "to the satisfaction of the regulator that is probably something that could be dealt with in–house".[98] However, Shelter dismissed the argument propounded by Mr Leenders, of the need to maintain anonymity while suspected breaches are being investigated, insisting that:

> The firms referred for enforcement have been found categorically in breach of FSA regulations and we see no reason not to name them while they are undergoing enforcement action.[99]

Shelter said that this "lack of transparency in the regulatory regime" was a "significant barrier to securing improved practice and behaviour across all lenders", a point which was also stressed by Dominic Lindley for Which? who argued that until firms saw a real penalty from this disclosure, they were hardly likely to change their practices.[100]

55. Which? told us that they had submitted a Freedom of Information request—which had been rejected by the FSA—asking for the names of firms who had performed poorly in the FSA's August 2008 review of mortgage arrears, but were told that the FSA, despite

97 Q 227

98 Q 109

99 Ev 132

100 *Ibid.*

acknowledging that the information would benefit consumers, had come down against disclosure on the grounds that:

- disclosure to the public of the names of the firms with whom we had discussions…would be likely to undermine theirs and other firms' willingness to engage in a dialogue with us and to provide us with information.
- disclosure could affect [a] firm's brand and reputation in the market in which it operates, thereby making it more difficult for it to win new business.
- the publicity could lead to an increase in complaints from customers which, on analysis may turn out not to be justified, so not only causing additional burdens on the firm but also disappointing customer expectations.
- Section 348 of the Financial Services and Markets Act 2000 ("FSMA") restricts the FSA from disclosing "confidential information" it has received except in certain limited circumstances (none of which apply here). Confidential information for these purposes is defined as information which relates to the business or other affairs of any person and which was received by the FSA for the purposes of or in the discharge of its functions under FSMA and which is not in the public domain. Any information received by the FSA from the firms regarding their arrears and repossession practices has been received for the purpose of carrying out our supervision of those firms, so falls within Section 348.[101]

Which? argued that none of the above justifications offered by the FSA stood up to "external scrutiny". It contended that the FSA had "provided no evidence that disclosure of the names of the firms which have been treating customers unfairly would reduce firms' willingness to provide it with information" and, that regardless, "a strong regulator should not be relying on the voluntary disclosure of information in order to do its job effectively". Which? also argued that the provisions of Section 348 of FSMA contained "important gateways which allow the FSA to disclose information in certain circumstances", including "the ability for the FSA to disclose information to third parties to enable or assist the FSA to perform its functions". This, Which? maintained, meant the FSA could publish information "in pursuance to its function of providing guidance, information or advice in order to meet its regulatory objectives such as securing the appropriate degree of protection for consumers".[102]

56. Which? concluded that the excuses offered by the FSA for not revealing this information were symptomatic of "the cosy relationship the FSA has with the financial services industry".[103] In Dominic Lindley's view, such a policy demonstrated that the FSA placed:

101 Ev 63

102 *Ibid.*

103 *Ibid.*

> the commercial interests of firms which are trying unfairly to evict people from their homes and levying unfair charges are more important than the public interest and the interest of consumers in disclosing this information.[104]

57. We asked Jon Pain and Leslie Titcomb whether they had concerns that, during the period the FSA was taking enforcement action against these four firms, customers of these firms could be treated unfairly or the firm could gain new unsuspecting customers who risked being treated unfairly. Mr Pain tried to offer reassurance that "as part of that enforcement action … we are taking a very close look in terms of their treatment of customers as part of our supervisory activities on a daily basis".[105] He added that some of those lenders might no longer be active in the mortgage market and that, even where they were, he hoped that new customers would not go immediately into arrears.[106]

58. **Currently the FSA only publishes the names of firms it has found guilty of wrongdoing once enforcement action against the firm has been concluded. The industry has told us that it supports the continuance of this approach, although others have argued that this places the interests of lenders ahead of those of consumers. We have concerns that the balance between disclosure to the public and the need to protect firms before they have been found guilty of wrongdoing has tilted too far towards the interests of the industry.**

59. **Whilst we would not go so far as to describe the FSA's stance on naming firms guilty of wrongdoing as symptomatic of the cosy relationship between the FSA and industry as others have done, we understand why such a suspicion lingers. We were, for instance, surprised that the FSA, in part, justified its decision to reject a freedom of information request in this area on the grounds that publication would damage its relationship with firms who might as a consequence be less willing to provide the FSA with information. Such a softly softly approach contradicts the pronouncements by Hector Sants, Chief Executive of the FSA, who has publicly stated that he wanted firms to be afraid of the regulator. We invite him to add substance to this statement by informing claimants whether or not their cases are being investigated. The impression given at the moment is that it is the FSA that is scared of the firms it is charged with regulating. One possible approach would be for the FSA to publish information on the breadth of practice in the sector which of itself would highlight outliers.**

The pre–action protocol

60. The pre–action protocol came into existence in November 2008 and was designed to "help protect homeowners who may be facing the threat of repossession". These new court protocols were to "help make repossessions a last resort" and set out "clear guidance on the steps that lenders are expected to take before bringing a claim in the courts to ensure that repossessions are a last resort". As a result, lenders would:

104 Q 36

105 Q 226

106 Q 232

> now be expected to demonstrate that they have tried to discuss and agree alternatives to repossession when borrowers get into trouble with their mortgage repayments. If a case reaches court, lenders will be required to tell the court precisely what they have done to comply with the protocol.[107]

61. Jackie Bennett, for CML, explained that the reason for introducing a protocol in this area was because the UK had been through a period where fewer arrears and repossession cases were coming to court. The protocol helped familiarise judges with the mortgage conduct of business rules and ensured that "the lender has been through all the steps … and that repossession really is a last resort".[108] The BSA told us that the protocol did not result in additional requirements for lenders to adhere to, as much of the protocol reflected the existing requirements of MCOB 13. It felt that the main impact of the protocol was in relation to evidential requirements, which the lender had to provide to the court, to demonstrate the protocol had been adhered to.[109]

62. There was support—from the CML amongst others—for the introduction of a pre–action protocol in the submissions we received, whilst Citizens Advice told us that "the combined effect of lower interest rates, negative equity and the pre-action protocol appears to have been to encourage lenders to take court action as a last resort".[110] It cautioned, however, that it had received evidence that the protocol was not generally being observed by sub-prime and second charge lenders and that it continued to see cases where the protocol had not been observed.[111] The Financial Services Consumer Panel expressed satisfaction that, since the introduction of the protocol, judges were at least aware of the FSA rules in this area (which had previously not been the case). The panel did, however, express concerns regarding "a lack of clarity about how much judges can take failure to keep to these rules into account in a possession action" and said they were looking "to the FSA and the Ministry of Justice to take steps to bring more clarity to this arena in England and Wales". The panel concluded by stating that:

> Repossession proceedings can come to court very quickly and although the mortgage arrears pre-action protocol appeared to be a helpful initiative we consider that it is relatively toothless. The protocol sets down little by way of sanctions in the event that firms fail to abide by its requirements. We would be keen to see the FSA include some elements of the protocol as new rules within the amended MCOB 13.[112]

63. **The pre-action protocol has been helpful but should be more specific including the giving of examples of unreasonable actions by lenders (for example excessive charging of arrears) which the court may take into account.**

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107 "Securing a fair framework for homeowners", HM Treasury press notice, 22 October 2009

108 Q 121

109 Ev 56

110 Ev 52,79

111 Ev 52

112 Ev 151

Sale and rent back in the private sector

64. Sale and rent back refers to the practice whereby a homeowner sells their home to a private landlord with the landlord allowing them to remain there paying rent as a tenant. The National Landlords Association (NLA) explained that the sale and rent back market has existed as a sub-market of the private rental sector for some time, but that it had "gained prevalence in the last few years". It estimated that at its height in 2007, the market comprised approximately 2000 firms and individual landlords offering sale and rent back services, but said that this figure had declined sharply over the last 18 months.[113]

65. We asked witnesses whether the size of the private sector sale and rent back market would increase as a result of the economic downturn. Kay Boycott felt that this was "certainly possible", but that equally things could go the other way if the introduction of the FSA interim regime led some firms to exit the market.[114] Peter Williams, for IMLA, had no such doubts, telling us that size of the market would increase, a comment echoed by Adrian Coles.[115]

66. The NLA explained that homeowners turned to sale and rent back for a number of reasons. These included: long term illness affecting individuals or close relatives causing reduction in household income and therefore the affordability of home ownership; marital/partnership breakdown leading to the loss of one income stream; over-indebtedness; or where a fixed interest rate period comes to an end, potentially increasing mortgage repayments with the mortgage moved to the standard variable rate.[116]

67. There has been much criticism of private sector sale and rent back schemes after a number of high–profile cases where landlords have been shown to have acted unscrupulously. Citizens Advice told us that it had been "concerned for some time about the growth of completely unregulated sale and rent back schemes" and that evidence suggested that "homeowners in a financially and emotionally vulnerable situation end up selling their homes for much less than they are worth, in return for a tenancy that offers little security of tenure".[117] Industry groups also acknowledged that the sector was not without its problems. For example, the BSA acknowledged the "very significant financial harm that sale and lease back schemes can cause homeowners".[118]

68. Shelter outlined the sort of practices which went on and which had brought the industry into disrepute:

- transactions which often involved significant loss of equity in the home, with sales typically at 15–20% or more (sometimes up to 40%) below market value;

113 Ev 155

114 Q 57

115 Q 147

116 Ev 155

117 Ev 51

118 Ev 57

- leaseback arrangements which were predominantly on assured shorthold tenancies, with a minimum six month contract, with many people evicted by their landlord once the six month contract has ended;
- cases where the buyer/landlord fails to keep up with mortgage payments, with the home subsequently repossessed and the tenants (former owners) evicted;
- limited information provided up front with the consequence that consumers were often hit by additional fees and charges and higher rents once they were past the point of sale.

Finally, Shelter said that, in its experience, sale and lease back companies generally did not offer or signpost towards independent advice on alternative options which might be better for the consumer.[119]

69. Mr John Socha, Vice-Chairman of the NLA, admitted that there had been "cases where there had been [a] quite appalling loss of value to the person who owns the house".[120] However, he rejected calls for private sector sale and rent back to be banned, whilst Adrian Coles said that the sale and rent back had a useful and respectable role to play "if it is run properly":

> to say under no circumstances whatsoever can a homeowner ever sell their home to a future landlord and then rent it, if that deal is done transparently and fairly that is what we want. We should not outlaw all practice, it can work very well.[121]

Regulation of the sale and rent back sector

70. Historically, the private sector sale and rent back market has been unregulated. However, in response to the problems discussed above, the Treasury announced that the FSA would take on responsibility for regulating such schemes on 1 July 2009. As a result, an interim regime for the sector was introduced. Under this, firms will need to meet the FSA's threshold conditions including the requirement to have adequate resources and to be run by fit and proper people. Registered firms will also have to comply with the FSA's Principles for Businesses. The interim regime will be succeeded by a "more comprehensive regime", which is intended to start on 30 June 2010 and on which the FSA will consult in autumn 2009.[122]

71. When questioned as to whether poor practices within the sector would become a thing of the past once FSA regulation began, John Socha said that this would be the case.[123] Sue Edwards, for CAB, welcomed "the very swift action by the FSA, the OFT and the Government" to introduce regulation in this area, telling us that they acted promptly in

119 Ev 133

120 Q 143

121 Q 144

122 Ev 122–123

123 Q 148; Mr Socha gave evidence to the Committee on 30th June 2009, the day before the FSA's interim regime for the sale and rent back sector came into force.

response to concerns raised by CAB, Shelter and the Council of Mortgage Lenders.[124] Kay Boycott for Shelter, welcomed the interim regime, but stressed that the FSA must ensure that the regulations had "teeth" and stressed that the FSA must move to enforcement "very quickly where companies are not complying".[125] Ms Boycott also expressed some disappointment that the interim regime did not require independent valuations.[126] Shelter expanded on 'independent valuation' in written evidence, expressing disappointment that the "concern that the provision requiring an independent valuation has been removed" during the course of the FSA's consultation on the interim regime.[127] The Consumer Credit Counselling Service also welcomed the interim rules and guidance introduced by the FSA, but expressed continuing concern that the interim regulations might lead to increased consumer confidence and more applications from consumers interested in private sector sale and rent back, but without the protection that a full regulatory regime would provide. It argued that, as a result, consumers "should receive independent legal and debt advice" before committing to sale and rent back and that, additionally, "it should be incumbent on each company offering sale and lease back to fully disclose its interim status and the impact that has on each customer". [128]

72. The BSA in its written submission argued that for regulation to be effective it must be properly policed by the FSA and that this would "require the deployment of a significant resource from the FSA to ensure that they can find unregulated operators". It cautioned that this would not be an easy task "in view of the reliance of many of the less reputable operators on direct approaches to householders, local newspaper classified advertising and adverts in shop windows to get business".[129] Mr Socha from the NLA made a similar point, explaining that his organisation was asking the FSA (and other relevant bodies) to advertise to consumers that they should only enter into such arrangements with FSA registered firms.[130]

73. **We are extremely concerned by the evidence we have received of dubious and unscrupulous practices in the private sale and rent back market. Such practices have caused misery and suffering to many families and have brought the sale and rent back industry into disrepute.**

74. **We welcome the decision to bring the sector under the regulation of the FSA. However, we have concerns that the interim regulatory regime for the sector—which will be in force until 30 June 2010—may not afford full protection to consumers and may even give some a false sense of security. The FSA must therefore ensure that there will be no slippage in the date for the full regime to come into force and should consider whether this date could be moved forward. We are also surprised that the**

124 Q 60

125 Q 52

126 *Ibid.*

127 Ev 133

128 Ev 111

129 Ev 57

130 Qq 152–153

interim regulations do not contain a requirement for 'independent valuation', despite the fact that the FSA's original proposals in this area contained just such a provision. We seek clarification as to the grounds upon which the FSA made this decision and whether it will include 'independent valuation' as a requirement under the comprehensive regulatory regime which is to be introduced in 2010.

75. **There is also a danger that whilst reputable sale and rent back firms will register with the FSA, many others will continue to operate in the 'dark', away from the prying eyes of regulatory scrutiny. The FSA should therefore set out how it intends to register and monitor the activities of those sale and rent back firms and landlords who may try to slip under the radar. At the same time, the FSA must demonstrate that its regulatory regime in this area has real 'bite' and that it will move to enforcement action much more quickly than has hitherto been the case with respect to breaches of its mortgage conduct of business rules.**

4 Government support for households in mortgage difficulties

Overall Government strategy

76. We have already outlined a number of measures that the Government has introduced to support households in mortgage difficulties and to limit repossessions, including a new mortgage pre-action protocol introduced by the Civil Justice Council which makes it clear that repossession should be used as a last resort. Other measures announced by the Government include:

- agreement with major lenders to wait at least three months before initiating repossession proceedings; and
- a £10m package to increase the provision of legal and debt services to households in difficult financial circumstances.

77. Additionally, through the course of the current economic downturn, the Government has introduced a number of new schemes to support homeowners in mortgage difficulties as well as amending policies which were in place prior to the current recession. Budget 2009 outlined the Government's approach in this area, stating that "the Mortgage Rescue Scheme (MRS), and Homeowners Mortgage Support Scheme together with changes to Support for Mortgage Interest (SMI) will help to ensure that homeowners who experience a temporary fall in income, lose employment, or are otherwise vulnerable, are able to remain in their home".[131] We discuss the success or otherwise of these, the Government's three flagship measures, directly to support homeowners in difficulty in greater detail below, as well as the coherence and overall Government strategy in this area.

78. Lord Myners, the Financial Services Secretary to the Treasury, stressed that any assessment of policy in this area must take place in the context of the wider macroeconomic environment and Government measures to support the wider economy.

> It is through ensuring through fiscal policy that there is demand in the economy which supports employment and an accommodating monetary stance, and certainly one of the things which is clearly different this time in this mortgage cycle from previous ones is that we have much lower interest rates at the moment than in previous times of increase in arrears and foreclosure.[132]

79. Kay Boycott praised the Government's response to problems in the housing market, saying that Shelter recognised that policies to help homeowners had "been put in place quite quickly, certainly versus the last recession". However, Ms Boycott also argued that the introduction of new schemes and the modification of existing ones demonstrated that

131 HM Treasury, *Budget 2009 Building Britain's future*, HC 407, April 2009, pp 104–105

132 Q 269

adequate "long–term safety nets were not in place" prior to the current recession.[133] A similar point was also made by the CML who stated that "it would be difficult to attribute success to any of the Government schemes to help homeowners facing difficulties before the financial crisis", and bemoaned the fact "engaging with Government on the ineffectiveness of the safety net prior to the financial crisis was challenging".[134] Kay Boycott also expressed concern about the "lack of consumer awareness around all these schemes", saying that "every time an extra scheme is introduced it adds to consumer confusion about which scheme you are talking about", and urged the Government to increase publicity to raise public awareness of the options open to them.[135]

80. **We welcome the measures which the Government has introduced to support homeowners in mortgage difficulties. However, the need for the introduction of a large number of new initiatives as well as the amendment of schemes in place before the current crisis suggests that adequate safety nets for homeowners in mortgage arrears and/or at risk of repossession were not in place prior to the current recession. We recommend that the Government re–examine its longer–term strategy towards supporting homeowners in mortgage difficulties to ensure that adequate mechanisms to support homeowners are in place even once the current downturn has ended. A part of any review of strategy should be an examination of the adequacy of existing insurance models to protect mortgage holders against adversity and the potential of alternatives.**

Homeowners Support Scheme

81. The Homeowners Mortgage Support Scheme (HMS) was launched in April 2009.[136] Its objective is to "enable households that experience a significant and temporary loss of income as a result of the economic downturn to defer a proportion of the interest payments on their mortgage for up to two years". The deferred interest payments will be rolled up and added to the principal, with the borrower paying this off when their financial circumstances improve, with the aim of maintaining an affordable monthly payment by extending the term of the mortgage. The Government will guarantee the deferred interest payments in return for banks' participation in the scheme.[137]

82. Every Government-backed lender—the Lloyds Banking Group, Northern Rock, the Royal Bank of Scotland, Bradford & Bingley—has signed-up to the HMS scheme. Other high street lenders, including Barclays, HSBC, Nationwide and Santander, have agreed to provide comparable or equivalent arrangements to their customers, but will therefore not enjoy the security of the Government guarantee. The Government estimates that lenders covering approximately 80% of the mortgage market will be providing what the

133 Q 9

134 Ev 80

135 Q 10

136 "New homeowners support scheme begins", Department for Communities and Local Government press notice, 21 April 2009

137 "New scheme to help people at risk of repossession", HM Treasury press notice, 3 December 2008

Department for Communities and Local Government described as "enhanced support to their customers".[138]

83. We were told by a number of organisations, including Which? and the BSA, that it was too early to judge the success of the scheme given that HMS was only introduced in April 2009 and that figures on participation would only be published later in the year.[139]

84. We asked witnesses about how the 'equivalent' schemes introduced by some lenders compared to the Government's Homeowners Support Scheme. Ms Boycott told us that it had been very difficult for Shelter "to get hold of the data that allows us to do that direct comparison and it is certainly very difficult for us then to communicate to our advisors".[140] We also asked witnesses about the 20% of lenders who were not participating in HMS nor offering their customers any equivalent scheme. Kay Boycott said she wanted to see "all lenders signing up or providing equivalent schemes—a point which was echoed by Which? who argued participation should be made "compulsory", especially given that non-participants included "a disproportionate part of the sub-prime market where consumer detriment is likely to be greatest".[141] We asked Lord Myners what the Government was doing to ensure the remaining 20% of the market was covered. He replied that the Government was "actively in discussion with them" and agreed that it was important to increase participation amongst this group because "that is where the majority of the problems lie".[142] However, Lord Myners told us that compelling lenders to participate in HMS was "extraordinarily difficult", and that the Government would try and increase participation through engagement, discussion and encouragement.[143]

85. **We welcome the introduction of the Homeowners Support Scheme (HMS) which has the potential to provide valuable assistance to homeowners in mortgage difficulties. We recognise that it is too early to make an assessment of how many homeowners have benefited from the scheme and therefore whether HMS can be judged a success. That said, increased disclosure of the details of equivalent schemes operated by some lenders is important, not least so that consumers and advisors have a clearer idea of the support they should be receiving from lenders. Finally, firms representing 20% of the market place are neither in HMS or offering equivalent support to their customers. Whilst there are practical difficulties around securitisation covenants for some in offering such support—something we discuss in greater detail below—the Government must make it a priority to increase participation. Raising participation is especially important as evidence suggests that it is largely sub-prime or specialist lenders who are not participating in such schemes and these are precisely the firms whose customers are most likely to be in mortgage difficulties. Whilst we hope that persuasion will be**

138 "New homeowners support scheme begins", Department for Communities and Local Government press notice, 21 April 2009

139 Ev 58, 66

140 Q 13

141 Q 18

142 Q 298

143 Q 302

sufficient to convince more lenders to sign up, the Government should not rule out compulsion if this approach fails.

Securitisation agreements, participation in HMS and lender forbearance

86. Dominic Lindley linked non–participation in HMS or equivalent schemes to securitisation covenants, telling us that Which? had become concerned that there were "some terms in the securitisation agreements which are actually preventing lenders from joining the [HMS] scheme or from setting up an equivalent scheme". This is because, for example, the terms of a securitisation might prevent an extension of the loan term or conversion to interest-only for a period, both of which might otherwise be legitimate means of dealing with distressed borrowers in particular circumstances. Mr Lindley stressed that lack of participation amongst such firms in HMS or restrictions on their ability to show forbearance was a particular problem given that "arrears rates among people whose mortgages have been securitised are twice those … for whom they were not securitised" with the consequence that there was "a big segment of the market outside the scheme where people are in arrears".[144]

87. Mr Lindley said that Which? had raised the issue with the FSA who had looked into the matter. Indeed, the FSA announced on 22 June 2009 that it had identified:

> terms in securitisation covenants which could lead to inequitable treatment of borrowers in arrears, by restricting the scope for the lender to exercise flexibility and forbearance, for example, by prohibiting an extension of the loan term or conversion to interest only for a period.

On the same day, the FSA released a statement which said that:

> We expect all customers to be treated fairly and to be offered a relevant range of options for resolving arrears. It is not acceptable for a firm to use terms included in a securitisation as justification for not treating customers fairly.

The statement concluded by saying that the FSA did "not expect to see future securitisations that contain provisions that could potentially lead to the less fair treatment of borrowers".[145]

88. We asked both the FSA and Lord Myners whether some securitisation covenants did indeed limit scope for lender forbearance or flexibility towards mortgage holders in arrears as well as participation in HMS and, if so, what they were doing to tackle the problem. Jon Pain told us that the FSA was aware of the issue and that it was looking to address this matter as part of its mortgage market review, which it expected to be completed later this year. Lord Myners expressed concern that some securitisation agreements restricted the ability of the lender or lender's agents to offer flexibility and forbearance, but pointed out that "even where there is a documentary restriction, there are waiver processes" that could be used to override covenants. He believed that future problems could be addressed by

144 Q 16

145 FSA, 'FSA statement on securitisation, 22nd June 2009

constructive engagement with the industry, but reiterated that "the FSA is very clear that in future it will not accept forms of securitisation documents which do not allow appropriate forbearance engagement".[146]

89. **We are concerned by evidence we have received that certain securitisation agreements and covenants may restrict the ability of lenders to offer forbearance and greater flexibility to homeowners in mortgage difficulties and may restrict their ability to participate in HMS. To this end, we call upon the FSA to move quickly to ensure that securitisation agreements already in place do not act as an obstacle to treating consumers in mortgage difficulties fairly. Equally, we would welcome details of how the FSA intends to ensure that future securitisation covenants do not contain such provisions and the timetable to which it is acting.**

The Mortgage Rescue Scheme

90. The Mortgage Rescue Scheme (MRS) has been operational in England since January 2009 (separate schemes are either in place or being developed in Scotland, Wales and Northern Ireland.). The scheme is intended to help homeowners who are at risk of homelessness as a result of mortgage repossession and who fall within a priority need category.[147] It has two elements:

- Government mortgage to rent option: A Registered Social Landlord pays off the entire mortgage and the householder pays rent to the housing association at a level they can afford. This scheme is designed to assist the most vulnerable households on low incomes who are unlikely to be able to sustain a mortgage
- A shared equity option: This involves a Registered Social Landlord providing an equity loan to the homeowner to enable the homeowner's monthly mortgage payments to be reduced. This option is designed to assist homeowners who have an equity share in their home and are facing a payment shock.[148]

The Treasury estimates that the MRS will cost £285m and it was envisaged that the scheme would assist 6,000 homeowners. It was announced as part of the 2009 Budget that the scheme was being expanded to help people in negative equity (where the total of their secured loans exceeds the value of their property) from 1 May 2009.[149]

91. The latest figures published by the Department of Communities and Local Government show that, to date, just six households have benefited from the MRS.[150] Sue Edwards, for Citizens Advice, acknowledged that this was "obviously quite a small

146 Q 268

147 These comprise: (1) dependent children, (2) pregnant women, (3) vulnerable due to old age, physical/mental disability/other special reason.

148 Ev 66

149 HM Treasury, *Budget 2009 Building Britain's future*, HC 407, April 2009, p 104, para 5.69

150 Qq 64–66

number", but added that her organisation was dealing with "quite a large number of enquiries" about the Scheme.[151]

92. Ms Jackie Bennett, for the CML, said that the MRS had acted as a catalyst for homeowners in mortgage difficulties to approach their lenders. She said that homeowners who had approached local authorities about the scheme were often "people who have not been in touch with their lenders before" and that this had provided an opportunity for local authorities to get "people to engage with lenders and money advisors".[152] John Healey, Minister for Housing, defended the MRS when he appeared before us, accusing those who focused on the headline figures of six households of "looking at the wrong end of the telescope". Mr Healey told us that more than 5,000 households had received advice from local authorities as a result of the scheme and that many homeowners who approached their local authority about the MRS "were then referred to their lender or specialist money advice". He concluded "simply to look at the numbers at the end of the scheme is to omit its importance much earlier on".[153]

93. **The Mortgage Rescue Scheme has directly benefited just six households, despite being designed to assist upwards of 6,000 households. We call upon the Treasury and the Department of Communities and Local Government to explain why their projections for participation in the scheme appear to be so out of step with the picture on the ground and request analysis as to whether this reflects flaws in forecasting, poor design of the scheme or lack of consumer demand. We note the comments made by John Healey, Minister for Housing, that MRS has acted as a catalyst for people in mortgage difficulties receiving advice and assistance from lenders and money advisors. This is, of course, to be welcomed, although we do question whether it is the most cost–effective way to raise people's awareness of the need to, in the first instance, work together with their lender to resolve mortgage payment difficulties.**

Support for mortgage interest

94. The principal Government scheme in existence prior to the current financial crisis was Income Support for Mortgage Interest (ISMI). This is a state benefit paid towards the mortgage interest payment, available to homeowners who are also in receipt of income support, Job Seekers Allowance or other income–related allowances. SMI is only available for loans taken out to purchase the property, or for specific home improvement. As such, borrowers who have taken out second loans for a purpose other than home improvements are not eligible to claim assistance.

95. On 5 January 2009, the Government announced reforms to SMI:

- since 5 January 2009, homeowners will only have to wait 13 weeks, instead of 39 weeks, to be eligible for support. This is broadly in line with the three month limit by which

151 Q13

152 Q 161

153 Q 274

time banks would consider mortgage payments to be seriously in arrears and as CML noted greatly enhanced lender's ability to show forbearance;

- as a temporary measure, from 5 January 2009 the capital limit for loans on which ISMI is based was increased from £100,000 to £200,000.

These two reforms were worth £100m and were estimated to assist 10,000 claimants. This follows an earlier change announced in the 2008 Pre–Budget Report, where the Chancellor announced that the Government would "maintain the level of support at the current interest rate for the next months for existing claimants so that net support to such claimants is increased". [154]

96. The BSA told us that they welcomed the January 2009 changes to the ISMI regime, but expressed concern that the changes were not permanent and considered they did "not go far enough to make a significant difference to borrowers in financial difficulty". They advocated an overhaul to SMI, including an expansion of the criteria to make it available to all loans secured on the property and to be payable at a rate of interest due under the terms of the mortgage contract, not as a standard rate set by the Department for Work and Pensions.[155] Citizens Advice also welcomed the decision to extend SMI support, but said it was "extremely concerned about the introduction of a two year maximum period of SMI support for jobseekers allowance claimants. It argued that:

> the proper way to deal with claimant responsibilities and work incentives is through the requirement for people claiming JSA to ensure they are doing all they can to look for work, rather than through an arbitrary limit on housing costs. We believe that the two year limit on housing costs for JSA claimants should be removed immediately.[156]

97. John Healey defended the two year cap, telling us that it was in place because the "purpose of the scheme was not to provide government support in perpetuity", but to help tide people through a temporary dip in their earnings.[157]

98. As noted earlier, presently support for mortgage interest is paid on income-related benefits, principally income-related jobseekers allowance, but not on contributions-based jobseekers allowance, which most people with a National Insurance record will receive for their first six months of unemployment. Sue Edwards told us that she had come across examples of people having difficulty receiving SMI because they were on contributions-based jobseekers allowance and who as a result would not qualify for SMI. We raised this issue with John Healey who told us that the Government had no plans to change the eligibility criteria for SMI at the present moment, but promised the Government was "monitoring" the situation.[158] In response to suggestions that one way forward would be to link eligibility for SMI to tax credits rather than income-related allowances, Mr Healey

154 HM Treasury, *Pre- Budget Report 2008 Facing global challenges: Supporting people through difficult times*, Cm 7484, November 2008, p 96

155 Ev 57

156 Ev 49

157 Q 290

158 Q 286

defended the present arrangements and cautioned against building too much complexity into the system.[159]

99. **We recommend that the Government should review the Support for Mortgage Interest (SMI) scheme as part of the Pre-Budget Report this autumn, and consider the costs of linking the scheme to either: a contribution-based Jobseekers Allowance or to the tax credits system. As part of that review the Government should examine: the payment of actual interest rates instead of the SMI standard interest rate, the issues surrounding second charge mortgages and what steps would be needed to lift the two year cap on SMI payments.**

159 Q 287

5 Mortgage Finance

Trends in mortgage lending

100. Gross mortgage lending is at its lowest level for almost ten years.[160] As the Bank of England outlined in its first Trends in Lending publication, restricting credit to households could cause an even deeper economic downturn.[161] We heard evidence about the state of mortgage lending today and how this has affected first time buyers. We also reflect on the future of the sub-prime sector. A question which needs to be addressed is whether the risks to the stability of the mortgage market caused by lending to less credit-worthy borrowers are offset by the benefit of allowing more to realise the dream of owner-occupation?

101. According to data from the Bank of England, the key factor contributing to falling gross mortgage lending is a sharp decrease in remortgaging activity.[162] Lenders have attributed this decline to low standard variable rates, which makes remortgaging relatively unattractive.[163] The Bank of England in their June 2009 Trends in Lending report, added that low house prices contribute to diminished demand for remortgaging, as some borrowers have insufficient equity to be able to get a mortgage with a different lender.[164] The House Builders Federation told us that lenders "are looking for any reason to refuse a loan" and that credit scoring had become increasingly restrictive.[165]

From feast to famine

102. A number of organisations told us that a return to former levels of lending, such as 125% loan-to-value (LTV) mortgages, would be undesirable.[166] However, Which? believed that the current scarcity of credit for mortgages was a cause for concern.[167] This had been particularly difficult for first time buyers, an important group in the market if the housing market is to recover, as the CML noted.

> The position of would-be FTBs [first time buyers] is very important for a lasting recovery of the housing market. Until the funding position improves materially, market conditions are likely to remain difficult and any upturn hesitant.[168]

103. In its written evidence, Which? expressed concern that first time buyers were having difficulties entering the housing market because of a fall in availability of 90% LTV mortgages.[169] There are fewer than one tenth the number of 90% LTV products today

160 Bank of England, *Trends in Lending*, June 2009, p 8

161 *Ibid.*, p 4

162 *Ibid.*, p 8

163 *Ibid.*, p 8

164 *Ibid.*, p 8

165 Ev 101

166 Ev 67, 134

167 Ev 67

168 Ev 80–81

169 Ev 67

compared to one year ago.[170] Which? also informed us that substantially higher margins were being charged on those 90% LTV mortgages that are on offer, and the rates charged on 90% mortgages were significantly higher than those for 75% LTV mortgages.[171]

Table 2: Number of products available at 90% LTV and difference spread between average rate charged and the Bank of England base rate

Date	Number of Products available at 90% LTV	Average Rate	Bank of England Base Rate	Difference
Jan-07	3148	6.20%	5.00%	1.20%
Jun-07	3481	6.51%	5.50%	1.01%
Jan-08	1541	6.72%	5.50%	1.22%
Jun-08	785	7.73%	5.00%	2.73%
Jan-09	179	6.24%	2.00%	4.24%
Jun-09	127	6.29%	0.50%	5.79%

Source: moneysupermarket.com

104. The mortgage lenders explained how current incentives created by credit rating agencies and the FSA prevented them from offering higher LTV mortgages. Mr Coles from the BSA described how larger exposure to higher LTV lending might increase the likelihood of a lender being downgraded by a credit rating agency.[172] A serious consequence of such a downgrading would be to increase the lender's cost of borrowing from the wholesale market.[173] Mr Coles told us that having a large proportion of high LTV lending might also encourage the FSA to take "severe action" against the lender because the FSA's stress tests assume a very severe reduction in house prices.[174]

105. Both the industry representatives and Government told us that they believed the number of 90% LTVs would increase in the future as stability and confidence returned and house prices rose.[175] However, in the interim before an economic recovery, there is a worrying lack of opportunities for first time buyers. Which? informed us that the requirement for a 25% deposit would act as a significant barrier to entry to first time buyers, with savings of £31,000 needed on a house at the average price for a first time buyer.[176] In London this figure rose to £51,000.[177] The CML have anecdotal evidence to suggest that 80% of younger first time buyers relied on relatives for financial support when paying deposits. John Healey and Lord Myners both noted that renting was rapidly becoming the preferred option for young people.[178]

170 Bank of England, *Trends in Lending*, June 2009, p 9

171 Ev 68

172 Q 184

173 *Ibid.*

174 *Ibid.*

175 Qq 184, 312

176 Ev 67

177 *Ibid.*

178 Qq 325-326

106. Some evidence suggested policy solutions to help first time buyers get a foot on the property ladder. The CML advocated cutting stamp duty.[179] Which? suggested that the Government could insure the additional risk for 90% LTV mortgages to encourage lenders to offer them more readily.[180] Peter Williams from IMLA told us there was little interest from industry or the Government in these insurance schemes. Lord Myners supported Mr Williams when he stated that providing insurance of this kind was not a matter for the Government and that the private sector would offer insurance if they thought it would be profitable.[181]

107. The Government runs a number of schemes which are designed to help people get on the property ladder such as HomeBuy Direct where first time buyers are helped to move into new properties by being offered an equity loan of up to 30% of the purchase price,[182] and the New Build HomeBuy scheme whereby new homes are offered for sale where individuals buy a share of their home and pay subsidised rent on the remaining share.[183]

108. We received only very limited evidence about the HomeBuy schemes. IMLA criticised the schemes in England for having unclear aims and limited monitoring of performance. It also noted that the scale and the content of the schemes were constantly changing. Mr Healey emphasised that these schemes were designed to encourage home building and that he believed they could achieve this and help first time buyers.

109. Mr Williams, Deputy Director-General of IMLA, told us there was an "unprecedented" shortage of mortgage finance[184] and his views were echoed by others, including Ms Bennett from the CML.[185] The Communities and Local Government Committee has recently examined a Government scheme designed to encourage lending, namely the Government's Asset-backed Securities Guarantee Scheme. This scheme aims to improve access to wholesale funding for banks and building societies.[186] We have not taken much evidence in this area but note the conclusions of that Committee:

> According to the evidence we have received, the Asset-backed Securities Guarantee Scheme, one of the most important of the weapons in the Government's armoury for tackling the effects of the credit crunch on its housing policy, is not working. [187]

179 Ev 81

180 Ev 67, 69

181 Q 312

182 Guidance from Communities and Local Government

http://www.communities.gov.uk/housing/buyingselling/ownershipschemes/homebuy/HomeBuyDirect/

183 Guidance from Communities and Local Government

http://www.communities.gov.uk/housing/buyingselling/ownershipschemes/homebuy/newbuildhomebuy/

184 Q 189

185 Q 188

186 "Statement on Financial Intervention to support lending in the economy ", HM Treasury press notice, 19 Jan 2009

187 Communities and Local Government Committee, Eighth Report of the Session 2008-9, *Housing and the credit-crunch: follow up*, HC 568, p 14, para 28

Existing borrowers

110. Which? highlighted in its written evidence how the mortgage market failed to operate in consumers' interest.[188] Specifically Which? highlighted the fact that, because of falling house prices and tighter lending criteria, some consumers were not able to switch mortgage providers in search of a better deal.[189] This issue is pressing as the CML told us that there will be 1.6m deals maturing in the 18 month period from the start of 2009 to mid-2010, a substantial number given there are 12m mortgage customers in the UK today.[190] Evidence from Shelter stated that borrowers needed a sufficient choice of affordable mortgages.[191] A lack of available good value rates for consumers who were coming off short term deals might lead to an increase in arrears and repossessions as consumers' costs could increase significantly when deals expired. The CML told us that lenders were working hard to discuss potential future payment shocks with borrowers when their fixed term deals expired.[192] One issue of importance is the timing of these discussions—we are unclear whether they occur *before* the consumer chooses the fixed term deal or soon before the deal ends when monthly payments may increase. Shelter emphasised that re-mortgaging should not push borrowers to arrears and repossessions.[193]

Competition in the sector

111. We received mixed evidence about the state of competition in the mortgage market. On the one hand, we heard from Lord Myners that there is a "very competitive market for mortgages",[194] while Mr Williams from IMLA described the UK mortgage market as "not fully funded or competitive at the moment".[195]

112. Which? supported the view that competition in the mortgage market had weakened,[196] citing as evidence the spread of variable mortgage rates over the Bank of England base rate. Mr Jon Pain from the FSA informed us that the specialist lender section of the mortgage market had become "virtually non-existent" which might further damage competition in that market.[197]

113. **First time buyers face barriers to getting on the property ladder, such as high deposit requirements and restrictive lending criteria. While we are not advocating a return to past levels of lending, it appears that more needs to be done to help credit–worthy first time buyers access credit. It is likely that restricting some first time buyers has negative effects on an already depressed housing market.**

188 Ev 67

189 *Ibid.*

190 Q 263

191 Ev 134

192 Q 179

193 Ev 134

194 Q 316

195 Q 180

196 Ev 67

197 Q 259

114. **It is vital that consumers understand that their mortgage payments will vary over time, especially during a period when interest rates are far more likely to go up than to fall. This is the responsibility of lenders and this is a matter that should be enforced by the FSA.**

115. **We are concerned that decreased competition in the mortgage market could lead to unfair practices towards consumers. The FSA need to be vigilant in their supervision of lenders to prevent anti-competitive practices.**

The future of the sub-prime sector

116. In an earlier report, *Financial Stability and Transparency*,[198] we included the following definition of sub-prime mortgages:

> Sub-prime mortgages are loans made to borrowers who are perceived to have high credit risk, often because they lack a strong credit history or have other characteristics that are associated with high probabilities of default.[199]

117. Sub-prime mortgages are regularly blamed for starting the present financial crisis. For example, the Financial Times states that "the rising defaults on sub-prime mortgages in the US triggered the global financial crisis".[200] We asked FSA representatives about whether the sub-prime sector should be closed down.[201] Mr Pain emphasised that in the Mortgage Market Review, the FSA would consider the sub-prime lenders' mechanism for raising funds and whether consumers who used specialist lenders needed more protection.[202] He remarked that affordability was the key issue for the FSA, and that consumers should enter the mortgage market knowing that they could sustain their mortgage payments over the lifetime of the mortgage.[203] He told us that many lenders were using "sophisticated tools" which could assess true affordability, but that the whole mortgage market should adopt these techniques.[204]

118. Evidence from IMLA stated that in recent years the sub-prime sector had accounted for 10–15% of the total volume of mortgages in a year.[205] They noted that firms in this sector were funded through the capital markets via securitisation where they sold their mortgage debt to other lenders, as opposed to obtaining funding from deposits.[206] Jon Pain commented that the capital market funding channel was now effectively closed and the sub-prime sector of the mortgage market had virtually ceased to exist.[207] Mr Pain informed

198 Treasury Committee, Sixth Report of Session 2007-8, Financial Stability and Transparency, HC 371,

199 Speech by Chairman Ben S. Bernanke, at the Federal Reserve Bank of Chicago's 43rd Annual Conference on Bank Structure and Competition, Chicago, Illinois, 17 May 2007

200 "In depth: Sub-prime fall-out", *FT.com*, www.ft.com/indepth/subprime

201 Q 259

202 *Ibid.*

203 Qq 261-263

204 Q 246

205 Ev 86

206 *Ibid.*

207 Q 259

us that arrears levels in the sub-prime sector were higher than in the mainstream mortgage market, and added that this was to be expected. He stressed that while the arrears rate for specialist lenders was near 10%, that implied 90% of borrowers in this sector were keeping up with their payments.[208]

119. **Arrears rates in the sub-prime sector are higher than those in the rest of the mortgage market. We note that the current sub-prime arrears rate of 10% is likely to rise given that arrears are predicted to increase. However we acknowledge that there are borrowers who use sub-prime lenders who are able to sustain their mortgage payments. We agree with the FSA that the important issue is for all lenders to consider the affordability of a mortgage for each potential customer. The FSA should ensure that all lenders perform adequate affordability tests, approved by the regulator, and improve their understanding of borrowers' ability to repay.**

208 Q 261

Conclusions and recommendations

Mortgage arrears and repossession levels

1. Being in arrears and facing the threat of repossession are distressing experiences. The evidence we have reviewed shows that both mortgage arrears and repossession levels are on an upward trend, which is expected to continue in the next few years. As recent global events have shown, the fortunes of economies are intimately bound up with that of their housing markets. (Paragraph 14)

2. Much uncertainty remains as to whether any recovery in the housing market would mitigate or exacerbate the scale of repossession. We recommend that the FSA monitors the forbearance policies of mortgage lenders to ensure that repossession is only a tool of last resort. (Paragraph 19)

The regulatory framework

3. We believe that the issue of the regulation of second charge mortgages should be reviewed by the Government. This Report focuses mainly on the principles and rules relating to first mortgages regulated by the FSA and it would be a cause for concern if second mortgages (likely to be taken out by those with greater needs) were less well regulated (Paragraph 22)

4. The evidence we have received suggests that mainstream lenders are, broadly speaking, complying with the FSA's mortgage conduct of business rules. Indeed, we have heard positive examples of some mainstream lenders taking pro–active steps to support consumers in mortgage difficulties. That said, we are extremely concerned by evidence of a lack of flexibility and forbearance in the sub-prime, specialist and second charge sectors to homeowners in arrears. (Paragraph 32)

5. We share the serious concern expressed by many of our witnesses that some lenders are charging high and excessive mortgage arrears fees to customers who fall into mortgage difficulties. Whilst we have not received conclusive evidence that the mortgage arrears charges levied by lenders are excessive and go beyond recouping additional administrative costs, we fear that some lenders are using arrears charges as an alternative profit stream. Indeed, the wide variation in the level of mortgage arrears charges levied by different firms adds weight to such a view. (Paragraph 39)

6. Such practices are intolerable, placing additional strain on homeowners already struggling to keep up with their mortgage payments. We note that the FSA has already referred four mortgage firms to enforcement action and understand that part of the case against some of these firms is based on excessive mortgage arrears charges. We suspect these cases represent the tip of the iceberg and call upon the FSA to take a much more robust stance towards tackling and eliminating unfair arrears charges. As a first step we believe lenders must be required to provide an itemised breakdown of the additional costs their arrears charges are supposed to cover. This would help shed valuable light on whether such charges are reasonable and justifiable as industry representatives claimed was the case amongst mainstream lenders. Alongside this, we believe that the FSA and OFT respectively should review all

mortgage arrears charges made by mortgage providers and secured lenders to determine whether they are reasonable. (Paragraph 40)

7. We share the concerns expressed by groups such as Shelter, Which? and Citizens Advice that the FSA's principles-based approach in the area of mortgage arrears has given far too much flexibility to lenders to interpret the rules as they wish. The consequence has been a wide divergence in practice amongst firms with consumers treated in an inconsistent manner and little way of establishing whether they are being treated fairly. We agree with the Financial Services Consumer Panel that there is an urgent need for more rules or a more explicit statement of the requirements on firms in guidance to help put some 'grit into the system'. We note the arguments put forward by the industry that the FSA's high–level principles in this area are complemented by more practical industry guidance, but believe the need for industry guidance in this area actually illustrates the deficiencies of the FSA's current approach. Industry guidelines are not a substitute for more robust rules—they are voluntary not binding, there is often little monitoring or supervision and there are no sanctions for non-compliance. (Paragraph 47)

8. We note that the FSA has begun moving from a principles to an outcomes-based approach and trust the FSA's Mortgage Market Review, which includes a re-examination of the mortgage conduct of business rules, will lead to a shift in this direction with a better balance between high-level principles and rules that are binding upon firms. The FSA's Mortgage Market Review must also give serious consideration as to whether the mortgage conduct of business rules need revising. The rules were drawn up in the early part of this decade in a very different economic environment and there is concern, expressed by the Financial Services Consumer Panel amongst others, that revisions need to be made to ensure the rules are appropriate for the very different economic circumstance prevailing today. (Paragraph 48)

9. The FSA stated in its submission said that "in late 2007, we became increasingly concerned by evidence, both from our own mortgage effectiveness review and from external reports by charities such as Citizens Advice and Shelter, that some mortgage lenders were failing to treat their customers fairly when they fell into mortgage arrears'. Yet it was not until June 2009 that the FSA announced that it was finally taking enforcement action against four firms. Furthermore such enforcement action against these firms could potentially take up to a year to conclude. During this period of time, which included the FSA's investigation, over 40,000 more homes were repossessed. The seemingly leisurely approach of the FSA in terms of completing its mortgage arrears review and enforcing possible breaches in the rules in the area of mortgage arrears is a matter of grave concern. We call upon the FSA to spell out clearly in its mortgage market review how it will improve its performance in terms of bringing miscreant firms to book. (Paragraph 52)

10. Currently the FSA only publishes the names of firms it has found guilty of wrongdoing once enforcement action against the firm has been concluded. The industry has told us that it supports the continuance of this approach, although others have argued that this places the interests of lenders ahead of those of consumers. We have concerns that the balance between disclosure to the public and

the need to protect firms before they have been found guilty of wrongdoing has tilted too far towards the interests of the industry. (Paragraph 58)

11. Whilst we would not go so far as to describe the FSA's stance on naming firms guilty of wrongdoing as symptomatic of the cosy relationship between the FSA and industry as others have done, we understand why such a suspicion lingers. We were, for instance, surprised that the FSA, in part, justified its decision to reject a freedom of information request in this area on the grounds that publication would damage its relationship with firms who might as a consequence be less willing to provide the FSA with information. Such a softly softly approach contradicts the pronouncements by Hector Sants, Chief Executive of the FSA, who has publicly stated that he wanted firms to be afraid of the regulator. We invite him to add substance to this statement by informing claimants whether or not their cases are being investigated. The impression given at the moment is that it is the FSA that is scared of the firms it is charged with regulating. One possible approach would be for the FSA to publish information on the breadth of practice in the sector which of itself would highlight outliers. (Paragraph 59)

12. The pre-action protocol has been helpful but should be more specific including the giving of examples of unreasonable actions by lenders (for example excessive charging of arrears) which the court may take into account. (Paragraph 63)

13. We are extremely concerned by the evidence we have received of dubious and unscrupulous practices in the private sale and rent back market. Such practices have caused misery and suffering to many families and have brought the sale and rent back industry into disrepute. (Paragraph 73)

14. We welcome the decision to bring the sector under the regulation of the FSA. However, we have concerns that the interim regulatory regime for the sector—which will be in force until 30 June 2010—may not afford full protection to consumers and may even give some a false sense of security. The FSA must therefore ensure that there will be no slippage in the date for the full regime to come into force and should consider whether this date could be moved forward. We are also surprised that the interim regulations do not contain a requirement for 'independent valuation', despite the fact that the FSA's original proposals in this area contained just such a provision. We seek clarification as to the grounds upon which the FSA made this decision and whether it will include 'independent valuation' as a requirement under the comprehensive regulatory regime which is to be introduced in 2010. (Paragraph 74)

15. There is also a danger that whilst reputable sale and rent back firms will register with the FSA, many others will continue to operate in the 'dark', away from the prying eyes of regulatory scrutiny. The FSA should therefore set out how it intends to register and monitor the activities of those sale and rent back firms and landlords who may try to slip under the radar. At the same time, the FSA must demonstrate that its regulatory regime in this area has real 'bite' and that it will move to enforcement action much more quickly than has hitherto been the case with respect to breaches of its mortgage conduct of business rules. (Paragraph 75)

Government support for households in mortgage difficulties

16. We welcome the measures which the Government has introduced to support homeowners in mortgage difficulties. However, the need for the introduction of a large number of new initiatives as well as the amendment of schemes in place before the current crisis suggests that adequate safety nets for homeowners in mortgage arrears and/or at risk of repossession were not in place prior to the current recession. We recommend that the Government re–examine its longer–term strategy towards supporting homeowners in mortgage difficulties to ensure that adequate mechanisms to support homeowners are in place even once the current downturn has ended. A part of any review of strategy should be an examination of the adequacy of existing insurance models to protect mortgage holders against adversity and the potential of alternatives. (Paragraph 80)

17. We welcome the introduction of the Homeowners Support Scheme (HMS) which has the potential to provide valuable assistance to homeowners in mortgage difficulties. We recognise that it is too early to make an assessment of how many homeowners have benefited from the scheme and therefore whether HMS can be judged a success. That said, increased disclosure of the details of equivalent schemes operated by some lenders is important, not least so that consumers and advisors have a clearer idea of the support they should be receiving from lenders. Finally, firms representing 20% of the market place are neither in HMS or offering equivalent support to their customers. Whilst there are practical difficulties around securitisation covenants for some in offering such support—something we discuss in greater detail below—the Government must make it a priority to increase participation. Raising participation is especially important as evidence suggests that it is largely sub-prime or specialist lenders who are not participating in such schemes and these are precisely the firms whose customers are most likely to be in mortgage difficulties. Whilst we hope that persuasion will be sufficient to convince more lenders to sign up, the Government should not rule out compulsion if this approach fails. (Paragraph 85)

18. We are concerned by evidence we have received that certain securitisation agreements and covenants may restrict the ability of lenders to offer forbearance and greater flexibility to homeowners in mortgage difficulties and may restrict their ability to participate in HMS. To this end, we call upon the FSA to move quickly to ensure that securitisation agreements already in place do not act as an obstacle to treating consumers in mortgage difficulties fairly. Equally, we would welcome details of how the FSA intends to ensure that future securitisation covenants do not contain such provisions and the timetable to which it is acting. (Paragraph 89)

19. The Mortgage Rescue Scheme has directly benefited just six households, despite being designed to assist upwards of 6,000 households. We call upon the Treasury and the Department of Communities and Local Government to explain why their projections for participation in the scheme appear to be so out of step with the picture on the ground and request analysis as to whether this reflects flaws in forecasting, poor design of the scheme or lack of consumer demand. We note the comments made by John Healey, Minister for Housing, that MRS has acted as a catalyst for people in mortgage difficulties receiving advice and assistance from

lenders and money advisors. This is, of course, to be welcomed, although we do question whether it is the most cost–effective way to raise people's awareness of the need to, in the first instance, work together with their lender to resolve mortgage payment difficulties. (Paragraph 93)

20. We recommend that the Government should review the Support for Mortgage Interest (SMI) scheme as part of the Pre-Budget Report this autumn, and consider the costs of linking the scheme to either: a contribution-based Jobseekers Allowance or to the tax credits system. As part of that review the Government should examine: the payment of actual interest rates instead of the SMI standard interest rate, the issues surrounding second charge mortgages and what steps would be needed to lift the two year cap on SMI payments. (Paragraph 99)

Mortgage finance

21. First time buyers face barriers to getting on the property ladder, such as high deposit requirements and restrictive lending criteria. While we are not advocating a return to past levels of lending, it appears that more needs to be done to help credit–worthy first time buyers access credit. It is likely that restricting some first time buyers has negative effects on an already depressed housing market. (Paragraph 113)

22. It is vital that consumers understand that their mortgage payments will vary over time, especially during a period when interest rates are far more likely to go up than to fall. This is the responsibility of lenders and this is a matter that should be enforced by the FSA. (Paragraph 114)

23. We are concerned that decreased competition in the mortgage market could lead to unfair practices towards consumers. The FSA need to be vigilant in their supervision of lenders to prevent anti-competitive practices. (Paragraph 115)

24. Arrears rates in the sub-prime sector are higher than those in the rest of the mortgage market. We note that the current sub-prime arrears rate of 10% is likely to rise given that arrears are predicted to increase. However we acknowledge that there are borrowers who use sub-prime lenders who are able to sustain their mortgage payments. We agree with the FSA that the important issue is for all lenders to consider the affordability of a mortgage for each potential customer. The FSA should ensure that all lenders perform adequate affordability tests, approved by the regulator, and improve their understanding of borrowers' ability to repay. (Paragraph 119)

Formal minutes

Tuesday 21 July 2009

Members present

John McFall, in the Chair

Nick Ainger	John Mann
Mr Graham Brady	Mr James Plaskitt
Jim Cousins	John Thurso
Mr Michael Fallon	Mr Mark Todd
Ms Sally Keeble	Mr Andrew Tyrie
Mr Andrew Love	Sir Peter Viggers

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Mortgage arrears and access to mortgage finance

Draft Report (*Mortgage arrears and access to mortgage finance*), proposed by the Chairman, brought up and read.

Ordered, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 119 read and agreed to.

Summary read and agreed to.

Resolved, That the Report, be the Fifteenth Report of the Committee to the House.

Ordered, That the Chairman make the Report to the House.

Ordered, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134 (Select committees (reports)).

Written evidence was ordered to be reported to the House for printing with the Report, together with written evidence reported and ordered to be published on 30 June and 2 and 7 July.

* * * *

[Adjourned till Tuesday 15 September at 9.30 am

Witnesses

Tuesday 30 June 2009

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Kay Boycott, Director of Communications, Policy and Campaigns, Shelter**, Sue Edwards,** Head of Consumer Policy, Citizens Advice Bureau and **Dominic Lindley,** Principal Policy Adviser, Which? Ev 1

Jackie Bennett, Head of Policy, Council of Mortgage Lenders, **Eric Leenders,** Executive Director-Retail Banking, British Bankers' Association**, Adrian Coles,** Director-General, Building Societies Association, **Peter Williams,** Deputy Director-General, Intermediary Mortgage Lenders Association and **John Socha**, Vice-Chairman, National Landlords Association Ev 11

Tuesday 7 July 2009

Jon Pain, Managing Director, Retail Markets and **Lesley Titcomb,** Sector Leader, Retail Intermediaries and Mortgages, Financial Services Authority Ev 25

Lord Myners CBE, Financial Services Secretary, HM Treasury and **Rt Hon John Healey MP,** Minister for Housing, Department for Communities and Local Government Ev 33

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20	National Federation of Property Professionals (NFoPP)	Ev 137
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Oral evidence

Taken before the Treasury Committee

on Tuesday 30 June 2009

Members present

John McFall, in the Chair

Nick Ainger
Mr Graham Brady
Jim Cousins
Mr Michael Fallon
Ms Sally Keeble
Mr Mark Todd
Mr Andrew Tyrie
Sir Peter Viggers

Witnesses: **Ms Kay Boycott**, Director of Communications, Policy and Campaigns, Shelter, **Ms Sue Edwards**, Head of Consumer Policy, Citizens Advice Bureau and **Mr Dominic Lindley**, Principal Policy Adviser, Which?, gave evidence.

Q1 Chairman: Good morning and welcome to our evidence session on mortgage arrears and access to mortgage finance. Can you introduce yourselves for the shorthand writer, please.
Mr Lindley: I am Dominic Lindley, Principal Policy Adviser at Which?.
Ms Edwards: I am Sue Edwards and I am Head of Consumer Policy at Citizens Advice.
Ms Boycott: I am Kay Boycott, Director of Communications, Policy and Campaigns at Shelter.

Q2 Chairman: This is a terrible room which I do not like. The acoustics are terrible and we cannot hear so I have to prevail on you to lean forward and shout! Thank you very much. Kay, your Chief Executive, Sam Younger, has warned about the risk of a second wave of repossessions beginning in 2010. Can you outline why you believe that there will be this second wave because the statistics at the moment do not indicate that is the case and the Council for Mortgage Lenders has actually revised downwards its previous estimates in terms of the number of repossessions?
Ms Boycott: Certainly this year there has been a revision downwards, although I think it is important to note that they are still at their highest level since 1991. Recently an economist, Ian Shepherdson has done some work saying in 2011 he thinks there are going to be 100,000 to 120,000 repossessions, and some work that we have been doing with York University has looked into some of the reasons why that might be. There are four main reasons. First of all, interest rates are currently very low and could be seen almost as arrears management in its own right and interest rates at some point are very likely to go up. Also unemployment is rising and what we do know from some economic forecasting is that for every 10% of sustained unemployment you get a 30% increase in arrears and repossessions. That is another factor. The other thing is a lot of the schemes that have been put in place are actually time-limited so when we get to the end of next year these schemes start to end and at the moment we are concerned that there is not an exit strategy in place for those. Finally, current lender forbearance does seem to be predicated (again based on some work we have been doing with lenders) on market conditions. At the moment it is not in lenders' interests to repossess quickly. That may change as the market picks up and that may lag behind where people are in terms of arrears and repossessions.

Q3 Mr Fallon: I understand that the problem may well deteriorate quite sharply next year, as Kay has illustrated, Mr Lindley, but you have told us that the number of people falling into mortgage arrears is actually increasing at the moment and the Council of Mortgage Lenders say it is falling; which of you is right?
Mr Lindley: I think we are right. The number of people in mortgage arrears is increasing as unemployment hits them. They thought the total number of people in arrears this year might reach 500,000 and maybe they have revised down that forecast, but mortgage arrears will continue to rise as unemployment hits and as those consumers who are on short-term tracker mortgage deals roll off those deals and revert back onto the standard variable rates and see a rise in their payments. The trick will be what the Government and what the lenders and the regulators can do to prevent repossession.

Q4 Mr Fallon: We will come to policy in a moment. I just want to be clear about the numbers and how they could be 20% out. How do you know the number is increasing at the moment?
Mr Lindley: The FSA has released statistics saying the number of new arrears cases increased in the first quarter of this year.

Q5 Mr Fallon: The end of the year is when the Council of Mortgage Lenders now expects the number three months behind to be 425,000. What do you expect that to be?
Mr Lindley: I expect it to be around that, maybe slightly higher, depending on what happens to interest rates and what happens to lenders' interest rates between now and then.

Q6 Mr Fallon: Why were they so far out? Why did they think it was 500,000?

Mr Lindley: The big uncertainty is the unemployment picture because that is the biggest cause of arrears. When you lose your job you cannot afford to maintain mortgage payments and so a big determinant to your forecast will be what happens to unemployment. The Bank of England has also done some projections and they see arrears continuing to rise, maybe just peaking below the highest level they were in 1991. It also depends on how you measure arrears, whether you measure it in terms of people who are three months behind, six months behind or as a proportion of the loan.

Q7 Mr Fallon: Let us just stick with three months behind. You both now agree that it should be around 425,000 at the end of the year. What about the end of 2011, what will the picture look like then if no policy is changed?
Mr Lindley: If no policy is changed we think that it will continue to rise. One of the effects of some of the government schemes is they are designed to put people into temporary arrears because under the Homeowner Mortgage Support Scheme you make a temporary payment, so technically you go into arrears when you enter the government scheme, but the important point would be to stop those arrears turning into repossession and people losing their homes.

Q8 Mr Fallon: So by the end of 2011 the figure will be what?
Mr Lindley: We think it will continue to rise maybe up to 450,000/500,000, but a big determinant is what happens to interest rates and what happens to unemployment.

Q9 Nick Ainger: Ms Boycott, there is a whole range of measures that have been put in place by the Government including advice measures, the Mortgage Rescue Scheme and so on, both financial, if you like, and advisory. Do you think they are working?
Ms Boycott: We do think that they are working. Firstly, I think all of these measures have helped to raise awareness of the fact that there are things that can help consumers. One of the good things that we would like to acknowledge is that it has driven consumers to seek help earlier. We do know that. We also recognise that things have been put in place quite quickly, certainly versus the last recession. If I take each one because they are quite different. We think that the support for mortgage interest has been effective, especially the reduction from 39 weeks to 13 weeks.I think what we would say is that that was in place before this recession hit and shows that long-term safety nets were not in place. We would like to see more consideration of safety nets going forward. We welcome the principles of the Homeowner Mortgage Support Scheme. We would say there have been some issues with how it has been brought in. It is relatively new, it was brought in in April, and it is still not clear which lenders are in, which lenders are offering equivalent schemes and which ones are not participating. How that works on the ground, our advisers get people calling up and they will say, "This is my lender," and they do not even have a definitive list yet of what each lender is offering. That basically means that there is almost a lender lottery depending on who you had your mortgage with whether you are going to get the HMS or not. That is still very unclear and it is confusing for consumers. We have the schemes announced and people are coming for advice but then it is quite difficult to be signposting them. I think that we would also see that administratively that has made it very difficult. In terms of the Mortgage Rescue Scheme, we welcome the principle. We know there has been very low sign-up and we are looking forward to seeing the figures that are coming out today on numbers of sign-up.

Q10 Nick Ainger: On that point because this is one of the schemes that has been criticised because of the very low take-up and at one stage only one or two people had actually benefited from it. What is your analysis of the problem? Why has it taken so long? Why at this stage is it still a relatively low take-up?
Ms Boycott: What we are seeing first of all is a lack of consumer awareness around all of these schemes. Of course every time an extra scheme is introduced it adds to the consumer confusion about which scheme you are talking about. We think overall there needs to be more publicity around all of these schemes to drive the consumers in. However, there have been administrative difficulties around getting all of the different parties together in order to get a satisfactory agreement and whilst we would not necessarily say this is a benchmark, what we have seen in the private sector sale and lease back schemes is they have been able to process this much quicker than this scheme. It does seem to be administrative difficulties in terms of processing.

Q11 Nick Ainger: I think you say that it does appear to be increasing. Does that mean the administrative glitches have been ironed out or are they still there and more work needs to be done?
Ms Boycott: We would like to see what the figures are today.
Ms Edwards: Certainly Bureaux are reporting that they are now beginning to get their first cases through the Mortgage Rescue Scheme which we are actually seeing, but it does take quite a long time to get through the process.

Q12 Nick Ainger: Do you think it could be made easier and faster?
Ms Edwards: It is slightly too early to say. With Shelter we are undertaking further research this year to pinpoint if there are any problems with the Mortgage Rescue Scheme and with the other government initiatives, so by the end of the year we will be able to say.
Ms Boycott: The final one is the Pre-Action Protocol and I think we would say that that has been welcome in terms of helping consumers.

Q13 Nick Ainger: Okay. Coming back to the Mortgage Rescue Scheme, the budget has been set for approximately assisting 6,000 people. Obviously we are nowhere near that figure yet despite whatever

is being announced shortly. Do you think it is a scheme which has merit? Is 6,000 enough? Once these issues have been resolved and we see it working, is a 6,000 target enough?
Ms Edwards: It is obviously quite a small number. Obviously there were two parts to the scheme, one was equity release and one was basically a social housing sale and rent back scheme. Also that policy was devised before the recession so it does not really address the kind of problems we are seeing now with high numbers of people in mortgage arrears and perhaps having no way they can stay in their home. Reports from Bureaux show that selling the home back to the housing association is much more important to their clients, and that is taking a long time to sort out, and in some cases people do not qualify.

Q14 Nick Ainger: Kay, you said earlier that one of the problems with the Homeowner Mortgage Support Scheme is that a significant proportion of the lenders are not part of the scheme.
Ms Boycott: It is numbers of lenders as opposed to numbers of mortgages. I think where Shelter would be is that if lenders are offering equivalent schemes then that is okay.

Q15 Nick Ainger: But are they? Abbey is not participating for example. Are they offering an alternative?
Ms Boycott: It has been very difficult for us to get hold of data that allows us to do that direct comparison and it is certainly very difficult for us then to communicate it out to our advisers.

Q16 Nick Ainger: Perhaps Sue can help on this one. Abbey, Nationwide, Barclays and HSBC are not participating in the Government scheme. Are you aware whether those four major lenders have got equivalent schemes of their own?
Ms Edwards: Personally I am not aware but then I am not an advice worker so I could not really say.
Mr Lindley: Part of the problem from our point of view is the lenders who are outside the scheme—we think it is about 20% of mortgages who are outside the scheme—are disproportionately the sub-prime lenders and those who securitised people's mortgages and sold them on. We know that arrears rates among people whose mortgages have been securitised are twice those amongst those for whom they were not securitised, so there is big segment of the market outside the scheme where people are in arrears. What we wanted the FSA and the Government to look at is whether there are some terms in the securitisation agreements which are actually preventing lenders from joining the scheme or from setting up an equivalent scheme. We raised this back in January and now the FSA have said some of these securitisation agreement place limits and restrict lenders' ability to defer interest or to move from a repayment mortgage to an interest-only mortgage. We think that is unfair. It is important that people are treated fairly regardless of what a 200-page legal document that they might never have seen says. In the US they have taken action on this and they passed a bill giving the people administering these mortgages the right to modify the mortgages without being at risk of lawsuits from investors.

Q17 Nick Ainger: So this scheme definitely does need seriously tweaking? Is that what you are saying, particularly in the sub-prime sector?
Mr Lindley: Yes, it definitely needs extending towards the sub-prime lenders and the people amongst the lenders who sold on the mortgages and we need to check that there are no legal barriers to lenders participating in these securitisation agreements, and if there are then the FSA needs to take similar action to what they have done in the US where they passed a bill.

Q18 Nick Ainger: Do CAB and Shelter agree with that view?
Ms Boycott: There were two points there. In terms of would we want to see the scheme tweaked, we would like to see all lenders signing up or providing equivalent schemes. What we would also like is that that is done in one wave so that then all of the advisers—if you think about the thousands of people that are giving advice out there—are told about it, it is all transparent, as opposed to lots of small changes which are very difficult. One of the concerns we have got about the schemes going forward is lots of incremental changes that make it extremely confusing for the consumer.

Q19 Jim Cousins: Just a quickie on the Mortgage Support Scheme. I have discovered because of my constituency work that there are regional caps on the value of the property so that in the north-east of England only a property of a lesser value than £125,000 can be considered for this scheme and that the person taking advantage of it has to demonstrate that they have the need and the size of house that they are in. This of course is related to the conversion to rent aspect and the present situation with housing benefit and local housing allowance. Do you consider that a scheme as complex as that with these hurdles is likely to be of widespread benefit?
Ms Boycott: Can I check whether you mean the Homeowner Mortgage Support Scheme or the Mortgage Rescue Scheme?

Q20 Jim Cousins: The Mortgage Rescue Scheme.
Ms Boycott: I think you said Mortgage Support Scheme and that is one of the issues with this that they are very complex to the consumer and they are not quite sure. I think we would say that there are lots of complexities about it. What we cannot say is there is one specific thing that will help to suddenly get rid of all the problems. Yes, it is very complex for our clients.
Ms Edwards: We would certainly like to look at whether any changes to the rules are necessary.

Q21 Ms Keeble: Just a couple of very quick questions first for Kay or Sue. Have you come across examples of people having difficulty getting support for mortgage interest because they are on

contribution-based JSA and there is someone else working in the household and they run into real difficulties?
Ms Edwards: Yes we certainly have seen cases like that.

Q22 Ms Keeble: Do you think it might be sensible to look at linking support for mortgage interest to the tax credit system rather than to JSA?
Ms Edwards: We would certainly like to see an equivalent to housing benefit for homeowners because at the moment people who are renting can get housing benefit if they are in low-paid work or if they are on contributory benefits rather than means-tested benefits but that is not the same for homeowners.

Q23 Ms Keeble: Do you think that that linkage might be more useful in terms of looking at the pressure on family incomes?
Ms Edwards: It could be.

Q24 Ms Keeble: Thank you. Really for Kay and Sue, do you think that mortgage lenders are exercising sufficient forbearance when dealing with households in mortgage arrears?
Ms Edwards: We undertook some research in April this year with Shelter, the Money Advice Trust and Advice UK and it was two pieces of research, one was asking advisers of those organisations what their experience was, particularly since the Pre-Action Protocol came in, of helping people with mortgage and secured loan arrears. What we asked them was whether there was any difference between the way high street lenders treated their borrowers and sub-prime second charge lenders and overwhelmingly they said that generally mainstream lenders were much better at offering forbearance than sub-prime and second charge lenders.
Ms Boycott: Some other research that we did showed that one in four said their lender had offered them no help when they had gone in with arrears management and that was across all lenders as well.

Q25 Nick Ainger: I see that the CAB specifically says that negative equity is a factor in forbearance and in a sense forbearance is a polite way of saying it is not worth repossessing. Therefore would you make any predictions at all about what is likely to happen if property prices pick up?
Ms Edwards: I can tell you my own experience. I was a debt adviser in East London during the last recession, so it would have been 1996 or 1997, where you began to see a lot more lenders who had been forbearing during the early part of the 1990s suddenly thinking there is no point in forbearing any more, we are going to go to court to get possession. In 1996-97 as we began to see house prices increase in East London we certainly saw a lot of lenders who had been forbearing for a while suddenly take possession action because house prices were increasing.

Q26 Ms Keeble: To what extent do you think that the whole problem around negative equity has been fuelled—and you must have seen this at the CAB if it has happened at all—by people taking out equity in their property and just chasing the value up and using it for consumer spending?
Ms Edwards: Certainly a lot of the people that we are helping have actually re-mortgaged and re-mortgaged and re-mortgaged again so by the time they come to us, even a few years ago, there was very little equity left.

Q27 Ms Keeble: Given the problems that people are experiencing now, is it worth looking at some different protocols for re-mortgaging?
Ms Edwards: Not just looking at first charge mortgages, also looking at second charge as well. What we are seeing is a lot of people do not just have a main mortgage, they have one or two second charges too.

Q28 Ms Keeble: My constituency has got the unfortunate honour of being the negative equity capital of the UK. Are there any particular measures that you would suggest that we should be pressing the Government on to deal with this problem?
Ms Edwards: Could I provide that in a supplementary memorandum?

Q29 Ms Keeble: Yes. How about Dominic and Kay, have you got anything that you would want us to look at?
Mr Lindley: I think it is partly making sure that lenders pass on interest rate cuts to their standard variable rates because all of your constituents in negative equity will be stuck with their existing mortgage lender and have nowhere else to go. We heard a lot earlier this year when base rates were being cut that the Libor rate, the rate at which banks lend to each other, was still high, but now that has gone down significantly but have not seen any further cuts in standard variable rates. It might also be about asking lenders to offer new deals to these people even though they are in negative equity and they have nowhere else to go.

Q30 Ms Keeble: Do you think that all the mortgage lenders are complying with the FSA Mortgage Conduct of Business rules and, if not, would each of you very quickly like to give an example of what you think is not good practice.
Ms Edwards: We are certainly seeing some cases where lenders are not complying but part of the problem is the rules themselves are a bit vague and they do not deal with some of the problems that we are seeing. For example, what the rules say is that repossession should be a last resort. It does not say that court action for repossession should be a last resort, which is one of the changes we would like to see. Despite the Pre-Action Protocol, despite the CML's excellent guidance, that is why we are still seeing some lenders take possession action as a first rather than a last resort to recover arrears.

Ms Boycott: We are seeing a variation within lenders as well so it may be that not all the people within lenders are given exactly the same treatment and that may be about making sure that policies are put down. We are concerned also that the forbearance will change month-on-month depending on where the market conditions go. That is just very, very confusing.
Mr Lindley: We would agree with Sue that the rules are very principles-based and it is difficult for consumers to know what they actually mean let alone the firms. That is why you need strong monitoring and enforcement by the FSA to find out exactly what is going on on the ground. They themselves admitted last August, and again in June, that there are lenders who are too ready to take court action and do not take enough account of borrowers' circumstances and imposing these arrears charges unfairly in some circumstances. The question is what action are they taking to clamp down on these lenders, and so far they are refusing to disclose the names of the lenders involved.

Q31 Ms Keeble: We have a formidable list of mortgage arrears fees which came from Which? which has got things like £150 for a debt counsellor from West Brom, £300 for fees for instructing solicitors from Barclays and Woolwich. There are some very high charges there. What do you think of these charges because they are not supposed to be higher than the actual cost, are they?
Mr Lindley: Yes, that is right. They are supposed to be a reasonable reflection of the extra administrative cost incurred by lenders as a result of people being in arrears. We do not think they are fair, particularly fees like £35 for missing a payment and having to send a letter. The OFT clamped down on default charges for credit cards and made them be cut to £12 and you have still got lenders imposing a £35 charge when a direct debit is missed. That is going to come on top of an additional fee from the consumer's current account for missing that direct debit. You have got some lenders imposing charges of £50 or £60 a month for people who are in arrears and that is going to damage people and not help them resolve their situation.

Q32 Ms Keeble: Some of these charges are actually from firms and companies in which the Government has got a large stake. The Halifax has £100 for the cost of a debt counsellor, Lloyds TSB has some high charges and Northern Rock is actually very vague. Do you think that organisations in which the Government has got a substantial interest and control should actually be beacons of best practice rather than having excessive or completely unclear charges?
Mr Lindley: Yes, they should be looking for best practice. The first thing is to get the lenders to open their books and justify these charges and provide a full breakdown of what this £35 or £55 a month is actually supposed to cover in terms of administrative cost. We would like to see lower charges and we would also like to see, if a consumer has made an agreement with a lender to repay their arrears, all charges are suspended. When I was reviewing the tariff of charges the only lender which said they did that was Nationwide in their tariff of charges. They said they would charge £20 a month and if you come to an agreement to repay the arrears then the charges are stopped. We would also like to see a 90-day window for people to negotiate with an independent debt counsellor (not a collection agent or a debt counsellor charged by the company) to come to a reasonable agreement on arrears.

Q33 Ms Keeble: CAB you provide debt advice. What do you think the cost of a visit by a debt counsellor should be? What is a realistic charge?
Ms Edwards: Obviously we do not charge for the debt advice that we give and certainly £100 seems to be very steep. It is often charged even though CAB is already negotiating with the lender on the client's behalf, so it does seem very, very steep indeed.

Q34 Ms Keeble: So there is double charging going on as well?
Ms Edwards: Yes. We are also seeing a lot of sub-prime lenders who are charging regular charges for being in arrears even where the borrower has made a repayment arrangement with the lender and is sticking to it. In some cases the amount the borrower has agreed to pay off in arrears is the same or less than the amount the lender is charging.

Q35 Chairman: Is it the case that the consumer is not getting a fair deal here?
Mr Lindley: There is no evidence that the consumer is getting a fair deal. Lenders have not justified these charges in any way. The FSA found one lender trying to recoup its advertising costs against these charges and that is totally against the rules. They are not there to cover overheads. Again, we asked the FSA who this lender was and they refused to say, so they have found lenders levying unfair charges and they refuse to say who they are.

Q36 Chairman: Why are the FSA refusing?
Mr Lindley: We have put in a number of freedom of information requests asking for this information and the FSA says disclosure of the names would undermine their dialogue with firms, they say that disclosure of the names could affect a firm's brand and reputation in the market in which it operates, thereby making it more difficult for the firm to win business. The same disclosure of the names of firms who have been treating people unfairly could lead to an increase in complaints from consumers which may turn out not to be justified so causing additional burdens on firms and disappointing customer expectations. Overall they conclude the commercial interests of firms which are trying unfairly to evict people from their homes and levying unfair charges are more important than the public interest and the interest of consumers in disclosing this information. Until firms see a real penalty from this disclosure, they are not going to change their practices, and the FSA has to immediately name these firms. This poor practice has been going on since last August and over that period thousands of people have been

repossessed and the FSA still refuses to name which firms it has concerns about, which firms it has referred for further enforcement action, and we think it is unacceptable and does not provide a strong enough incentive for the firms to behave themselves. We need naming and shaming and we need much higher fines. We would also like to see the revenue from those fines going to provide independent debt advice rather than what happens at the moment, which is the revenue from the fines is returned to the industry in lower fees for next year.

Q37 Mr Todd: At what point should a company be named and shamed? There is clearly a process here in which the FSA may investigate a complaint which has been received and then may take some enforcement action. Are you saying that as soon as they want to ask questions of a company that should be public knowledge?
Mr Lindley: No. They gather information from a company and then, if they identify a company they have concerns about, they can issue them with a notice saying, "We intend to name you" and then the company may have a few weeks to respond and then the company should be named. This enforcement action should not take months and months. The firms will drag it out; they know the FSA is willing to negotiate on when to name people and whether it names people.

Q38 Mr Todd: Even though this is critical market intelligence for someone choosing a mortgage? That if a particular company has practices which they would not like to encounter themselves, they may choose to take their business somewhere else, so it is partly about informing the market place of a company's practices?
Mr Lindley: Certainly, but they say it is in the company's commercial interests and if they are named they may not be able to gain new business. If people have been evicted from their homes unfairly by companies, they do not deserve to get a lot of new business.

Q39 Mr Todd: Shall we go back to the "mortgage: conduct of business rules" which were drawn up in 2003, when no doubt many thought that these circumstances would not arise? Is there an argument for a review of those rules to make them more robust in circumstances where they are being tried much more severely?
Ms Edwards: Yes, certainly. We argued in our report in 2007, before the crisis started, that the rules needed revision to deal with the arrears problems at that time.

Q40 Mr Todd: And specifically?
Ms Edwards: Specifically in relation to both selling and lending and arrears and repossessions, and particularly in relation to the selling of self-certification mortgages, where we felt there was need to make the rules much tighter.

Q41 Mr Todd: Is there any sign that the FSA has considered reviewing its rules?
Ms Edwards: Yes, it is conducting a mortgage review at the moment, so they are asking us for ideas as to what should be included in that review.
Mr Lindley: We would support a clamp-down on self-certification. The FSA looked at some of those and in 50% of cases they could not see why a self-certification mortgage had been recommended, because the person probably would have been able to prove their income and be eligible for a full status product.

Q42 Mr Todd: I think all of your organisations have been critical of the FSA as being weak in this area to some extent or another, would you care to expand on that? We are seeing them next week I think.
Ms Boycott: What we would mention is the time they have taken to do their thematic mortgage arrears review—they did the first phase in August and the second phase has just come out. It has taken that long, in which time 40,000 homes have been repossessed, and it is an unacceptable length of time. Also I think Dominic has made the point very clearly about the lenders who have been seen to have enforcement action but have not been named, and it is very difficult for consumers to make a choice.

Q43 Mr Todd: I think one of you used the phrase "principles base".
Mr Lindley: Yes.

Q44 Mr Todd: Which is broadly the way in which the FSA seek to act in this and other areas, to be honest. Do you understand why they prefer, as they would characterise it, a principles based approach rather than a very prescriptive, "We will authorise these particular practices and you must not do them until we have checked" approach?
Mr Lindley: The problem with the principles based approach is that it requires strong monitoring and enforcement, and we think that is lacking from the FSA at the moment.
Ms Edwards: It is quite difficult, if you are getting advice for someone and trying to help them with their mortgage arrears problem, to actually apply principle based rules, because your view of what principle means might be very different from the lender's view.
Ms Boycott: We have an example at the moment. If you think that one of the causes of this crisis is the lending to people who, to be honest, could not sustain their borrowing, in the last week one of our employees has been offered a mortgage which is five times her salary and which is two-thirds of her net income, so it is clearly unaffordable and at the moment the principle based regulation does not cover that. So we have seen some of these issues which caused the crisis maybe re-emerging in the market place.

Q45 Mr Todd: Perhaps you are bringing out the point that the FSA approach is not understandable to the ordinary consumer. It may be understandable in terms of the principles of the companies seeking to operate it, but it can provide no assurance to the consumer because they cannot understand what

these principles are and how they might be applied in reality to the products which they are being offered. Is that right?
Mr Lindley: If the FSA published something or if one of the trade associations published something saying, "There are the principles and this is good practice", if the company is not complying with good practice, can you actually do anything about it?

Q46 Mr Todd: So is part of what you are asking from the FSA a much more robust, consumer information package which goes to someone who is offered a mortgage saying exactly how they are protected in these circumstances and what the company ought to be complying with in offering this product and then monitoring the loan through to its eventual repayment?
Ms Boycott: If you imagine being a consumer at this point, we know 6.5 million households are saying they have stress and depression because of their housing costs. If you are in trouble, at the moment you might not know what fees you are going to be charged, you do not know what will happen if you come off your fixed rate mortgage, you may not know what the forbearance is going to be from your particular lender. The current schemes are very complicated so it is difficult to know what would qualify. It is incredibly confusing. I am fairly new to Shelter and just getting my head around this has been very, very hard and it is my full-time job, so if this is a consumer who is already struggling emotionally, maybe struggling with employment, it is very, very difficult, and we would call for much more transparency.

Q47 Mr Todd: So a very clear, simple leaflet given to a consumer which says, "This is how this product is supposed to be compliant with these rules, this is how your loan will be monitored into the future and the compliance of this company with those rules, and this is how you deal with any problems which arise", that sort of offering from the FSA is a critical part of what we are after, is that right?
Ms Edwards: I think the FSA already do that but I would like to see much more information about the requirements on lenders to do something. For example, the rules require lenders to have a responsible lending policy, it does not have to be public, so you do not actually know what that lending policy says, you cannot challenge it at all.

Q48 Chairman: Can I come back to the issue of not naming the companies, because there is a term here, "enforcement", and if I am correct in reading the submissions I have, the FSA can begin enforcement against firms without naming them, is that correct?
Mr Lindley: Yes, can begin enforcement.

Q49 Chairman: Tell me what enforcement means. Explain that for the public record here.
Mr Lindley: Being referred to enforcement means the firm gets referred to the enforcement division of the FSA and will then start discussions about what the problems are and what might be done.

Q50 Chairman: So the FSA by that stage will have had a clear idea that the company are contravening their advice and procedures?
Mr Lindley: They will have specific concerns about that company. Sometimes you hear firms being referred to enforcement and the FSA will put out a press release saying, "Two firms have been referred to enforcement" and you will not hear anything again about those firms. Sometimes you might get a fine rather later on, six months, nine months, a year later. When the firm has been referred to enforcement, the FSA can name who they are because judges will be hearing these repossession cases over the next few months and the FSA should be sharing that information. We do not think there are any particular legal barriers to the FSA sharing this information with the judges and with consumers, it is a matter of their practice and their unwillingness to do it.

Q51 Chairman: Do you think the FSA are out of line and seemingly the only institution which identifies wrong-doers but provides them with anonymity?
Mr Lindley: Yes, we think they are out of line, and it is possible to name firms which have been referred to enforcement and which you have concerns about and that would alert everyone about the concerns about those firms. If you are finding poor practice then you should release that information as soon as possible, particularly in such time-limited issues as mortgage arrears. If the FSA finds a problem with a company one day, we do not expect it to name it the next day, but surely there must be a procedure they can go through to get the names of these companies out into the public domain.
Chairman: This seems to be an issue we will come back to.

Q52 Sir Peter Viggers: By the process of sale and rent-back a householder can sell a property and rent it back from the person to whom he or she has sold it, and of course apart from releasing cash this can give the opportunity of receiving housing benefit, yet Shelter has perceived problems here. Would you like to outline the problems you perceive, Kay?
Ms Boycott: We have seen lots of problems. We think there are about 50,000 transactions to date and some of those people have lost quite a lot of equity in their home. These people are desperate. I met a woman who had four children who had gone through sale and lease-back of her home, the company had bought it and she was on an assured short-hold tenancy and she lost her home within six months. She is with her children now living in temporary accommodation and, to be honest, she is very, very desperate and is very open about that. There is an interim regime which comes into force from 1 July from the FSA and we very much welcome that because this was an industry which really did need regulating, but what we want to see is that that regulation has teeth and they move to enforcement very quickly where companies are not complying. What we do not want to see is the slow progress we have seen elsewhere because we have many, many cases of people who in good faith have thought this

was a way out of their arrears crisis and being repossessed and then have found it has turned into a nightmare as they have lost a huge amount of value. We are quite disappointed that the interim regime does not require independent valuations, therefore people are in danger of losing some of that equity, and also making sure they have secured tenancies going forward.

Q53 Sir Peter Viggers: What has the framework been for monitoring these transactions? Has there been a statutory framework at all?
Ms Edwards: No, there has not at all; they have been completely unregulated, until tomorrow when they will be regulated for the first time under the interim regime. We have seen many clients who have come to us because they thought this was the best way out of their mortgage arrears problem and are now often facing repossession for the second time, either because they fell into rent arrears because they could not get housing benefit or because the landlord who bought the house is in mortgage arrears themselves.

Q54 Sir Peter Viggers: Will the interim regime require an independent adviser to comment on any transaction?
Ms Edwards: I am not familiar with the contents of the interim regime.

Q55 Sir Peter Viggers: Do you know, Kay?
Ms Boycott: No, but we can come back to you with a note on that.

Q56 Sir Peter Viggers: Is the allegation there has been some kind of fraud, or is the agreement which is reached by the person who is selling the property clear, written and transparent and they simply do not understand the implications of it?
Ms Boycott: The OFT report in 2008 estimated there were upwards of a thousand private firms plus individuals getting involved in these sorts of schemes, so you can imagine the variation we have seen in terms of practice; it has been very, very difficult.

Q57 Sir Peter Viggers: Do you think the size of the market is likely to increase as a result of the economic downturn?
Ms Edwards: It is certainly possible. We have seen a lot of scams coming because of the economic downturn in employment, in other consumer areas, in credit, and it could happen this will increase too. It may also decrease because there is now regulation in place.

Q58 Sir Peter Viggers: Will the FSA, assuming responsibility for this market from 1 July, under the interim provisions, put an end to the shoddy practices?
Ms Edwards: We hope so, and we hope the FSA will work with us to make sure that happens.

Q59 Sir Peter Viggers: Is there a case for introducing a temporary moratorium on sale and rent-back activities during the downturn, given the expected increase in vulnerable households?
Ms Boycott: We have seen so many examples of poor practice over the last year, we would be very, very nervous about that.
Ms Edwards: In every sort of market there are some companies which are trying to do best practice and some sale and rent-back companies have spoken to us about statutory and voluntary regulations. We would not want to stop those firms which are offering a good product and offering a good security of tenure.

Q60 Sir Peter Viggers: What is your overall comment on the response of Government through the Office of Fair Trading and the FSA to this problem? Are you satisfied they now have a proper handle on it and will solve the problem in the longer term?
Ms Edwards: What has been really welcome about this is the very swift action by the FSA, the OFT and the Government to bring in regulation. If you compare it with the regulation of bailiffs, which has been talked about for 20 years and will not be in place until 2012, the Government acted within a couple of years of concerns being raised by ourselves, Shelter and the Council of Mortgage Lenders.

Q61 Sir Peter Viggers: Are you satisfied that the FSA now has a handle on the whole thing?
Ms Edwards: We hope so.
Ms Boycott: We hope so.

Q62 Chairman: The BBC *Watchdog* programme contacted me quite a time ago, maybe a year ago, on this issue and I promised to take it up with the Government, which I did. It is nice to see there is regulation now. The type of practices which were being described to me at the time were some landlords taking over property and giving people a commitment of a level of rent for a few months but then after six months the rent going up three or four fold and the person finding themselves out on the street. There is documentary evidence from BBC *Watchdog* on that issue. Are we certain now that with regulation that type of practice is a thing of the past?
Ms Boycott: I think we would say we will monitor the situation very carefully. We cannot say it is going to be a thing of the past. We welcome the regulation and we will keep a very close eye on it over the coming months. The other concern I would like to raise about this is that sale and lease-back is one option and what we want consumers to do is make sure they are aware of all the different options, that they are not being pushed down one route with that provider, so it is very important that consumers take independent advice before going down any of these routes. One of the issues is that at the moment advice capacity, certainly in terms of phone advice, is quite limited just because of the demand that is coming through. The other thing generally is that overall on

all of these schemes consumers have somewhere to go, where somebody can signpost them through the multiple options and define what is best for them, as well as encouraging them to contact their lender and understand what their lender can do for them as well. The difficulty with all these schemes is that they can get pushed down one route and that may not be the best option for them.

Q63 Chairman: One of the issues at the time, I remember, was the advertising, and I took this up with the Advertising Standards Authority. What about the level of advertising now? Is there still some misleading advertising out there?
Ms Boycott: We will have to come back to you on that.
Chairman: I think it is worth looking at that and keeping in touch with the FSA on that issue, because it is most certainly the case that the advertising at that time was rather appealing to people and then they find themselves, six months later, with the whole ground under their feet having changed.

Q64 Mr Fallon: Can we just come back to the two Government schemes—I know we have touched on them earlier. I want to be clear about the facts and numbers again. The target for the Mortgage Rescue Scheme was 6,000, what is the actual information at the moment as to the number who have benefited from that so far? Does anybody have that number?
Ms Boycott: The number which has come out this morning is that on the Mortgage Rescue Scheme it is now six households in total.

Q65 Chairman: How many? 6,000?
Ms Boycott: Six.
Chairman: Three zeros missing?

Q66 Mr Fallon: It was launched in January, the target was 6,000 and you suspect that only six—
Ms Boycott: Those are the figures which have literally just come out this morning.

Q67 Chairman: Can you name them!
Ms Boycott: It would be fair to say we are quite disappointed in that number.
Jim Cousins: You cannot be surprised?

Q68 Ms Keeble: Is that one of the ones where negative equity is an issue?
Ms Boycott: The negative equity issue was addressed in the Budget and that is fairly recently. I think it is the complexity. First, do consumers know about these schemes, because they seem to be going to private sale and lease-back in quite high numbers, so they are aware there is an alternative, so we would ask for more marketing. Secondly, are all these administration difficulties and is the energy put into sorting those out, because obviously you do have to get all the lenders together, and local authorities; there are quite a lot of conversations which need to take place. We are looking at those glitches. There is no one easy answer.

Q69 Mr Fallon: Where did the target of 6,000 come from? Was that advice from any of you?
Ms Edwards: No, that was the Government's estimate.

Q70 Mr Fallon: I know it was the Government's estimate, but where did it come from?
Ms Edwards: I do not know where it came from.

Q71 Mr Fallon: How many people do you think should be benefiting from this scheme over the year given that you told us earlier the total in arrears may reach over 400,000?
Ms Edwards: Certainly we would like to see many more than six people helped and would like it to be more like 6,000. We are dealing with quite a number of enquiries about Mortgage Rescue but obviously it does take a long time for them to go through the process and some people of course are not eligible.

Q72 Mr Fallon: But the scheme was announced in January, so if they have only got six in six months, it does not sound like a very well designed scheme, does it?
Ms Edwards: No. It is certainly very welcome that it is now eligible for people who are in negative equity; that was one of the big stumbling blocks in the early months of the scheme.

Q73 Mr Fallon: Can we turn to the second scheme, the Homeowners Mortgage Support scheme. How many have signed up for that?
Ms Edwards: We have dealt with 900 enquiries since the inception of the scheme but I do not know how many of those we have helped get on the scheme.
Ms Boycott: The analysis that we did of the first few weeks of it was that a proportion of people were eligible for support for mortgage interest, so our advice has signposted them there. There were a number who were not eligible because their lenders had offered equivalent schemes and there were a number who were not eligible because there were no schemes by their lenders. We would still welcome the fact that people came and got independent advice and were signposted to the right area, but I do not have the actual numbers who have signed up so far.

Q74 Mr Fallon: This scheme has been running two months now. Nobody knows how many people have signed up? In what form is that information supposed to be made available?
Ms Boycott: Communities & Local Government will have the information.

Q75 Mr Fallon: You have not got the second month's figures yet?
Ms Boycott: I do not think so. The numbers we have got are our internal number of people we think are going to be helped. C&LG are going to come out with the numbers later. You may wish to ask them next week if they are giving evidence.

Q76 Mr Fallon: But you do not know?
Ms Boycott: No.

Q77 Mr Fallon: What do you think the target was?
Ms Boycott: I am not sure.
Ms Edwards: We are not sure there is a target. We will come back to you on that one.
Ms Boycott: One thing to say is that there is a target for the scheme but there are also equivalent schemes and they are not going to be tracked. What we would say is that the equivalent scheme we welcome, whether people are getting help through the Homeowners Mortgage Support scheme or directly through their lender, as long as they are getting that help, that is okay. So we do need to think about both of those when we think about the figures.

Q78 Mr Fallon: Are you expecting all lenders to sign up to this scheme?
Ms Boycott: No, because some lenders have said they will offer equivalent, if not better schemes. The difficulty is getting the transparency of that information and we have asked repeatedly to get the list of who signed up and with what and who is offering an equivalent and who is offering nothing.

Q79 Mr Fallon: Is it your expectation that all lenders should either be in this scheme or offering a better individual scheme?
Ms Boycott: Absolutely, or equivalent, yes.

Q80 Chairman: We will probably get more answers on the Homeowners Support scheme in the second session, but why do you think that lenders have not signed up to the Homeowners Support scheme in the numbers that perhaps the Government expected?
Ms Boycott: Obviously lenders can answer for themselves but I think they would say that if they are offering equivalent schemes which may fit more easily with their administration systems, that is better, and they can also offer different options to their customers. I think the complexity of the administration has been quite a barrier for lenders as this scheme was brought in.

Q81 Chairman: I hear that some of those schemes could comprise about 200 pages for the lender to fill in. Is that correct?
Ms Boycott: I think it has been very difficult to get the entire industry to adopt a scheme which is quite administratively complex.

Q82 Jim Cousins: I wonder if I could ask something which comes out of this which is a slightly broader policy point. We are seeing a great reduction in the number of high loan-to-value and high loan-to-income mortgage offers. Should we regard that as being a necessary return to prudence, to sound lending in the Gladstonian traditions, or should we say that that carries the implication that the offer of home ownership to large numbers of people on low and fragile incomes who do not have access to the Bank of Mum and Dad is now a delusion and we must find a completely different route to offer those people decent homes?
Ms Boycott: I think that we would say is that sustainable home ownership is going to be one of the key issues going forward. We have seen the first wave of repossessions, we think we saw those marginal borrowers, those on a knife edge of affordability, and those were probably the first people to fail, and that will have been driven by the high loan-to-income and high loan-to-value. The example I gave earlier of people being offered five and a half times their income is very worrying for us, and whether that is a return to some of this unaffordability. What we would welcome is sustainable home ownership, not unsustainable home ownership, and that is what seems to have happened with some of the deals which were around in the last few years.

Q83 Jim Cousins: But sustainable home ownership going forward means guessing about the level of unemployment and guessing about the security of employment and guessing about the future pattern of mortgage interest rates. You cannot arrive at a concept of sustainable home ownership unless you have taken all of that into account. Is not the implication of what you have said that we need a much simpler scheme that is quite all-embracing which provides for an orderly exit from home ownership for quite large numbers of people?
Ms Boycott: I think we would probably say that one scheme was unlikely to cover the number of circumstances that people find themselves in, and an orderly exit is something we really would like to see because we see months of worry for a lot of our clients as they ask if they are eligible for one scheme, are they eligible for another and they sort of bounce between options, so an orderly exit, yes. Whether that is going to be through one scheme or another, I think we would doubt, because there are different options for different people and where they are.

Q84 Jim Cousins: Mr Lindley, do you have any figures which might indicate to us the number of borrowers who in the course of, let us say, the next 12 or 18 months, when unemployment is likely to be rising, are going to face a shift from fixed rate mortgages to variable mortgages?
Mr Lindley: It is normally about 1.5 to 2 million borrowers coming off short-term deals each year. Some of those will be fixed rate mortgages so they might see a small reduction in payments on the standard variable rate, others will have been mortgages which tracked the base rate. Two years ago you could get mortgages which would track at 0.5% below the base rate for two years and then would revert back to the standard variable rate, so those borrowers who have been paying very little interest for the past two years will now suddenly go back on the standard variable rate. The key determinate will be when interest rates start to rise, because in many cases over half the banks' customers will simply have nowhere else to go and will be stuck with their existing lender, and that is why banks have almost taken advantage of their captive customers by not passing on cuts because there is no competitive pressure in the mortgage market.

Q85 Sir Peter Viggers: Is not the implication of the figures that you have given us that if we were thinking about an orderly exit from home ownership then the numbers of people we ought to be considering might be in that frame are far larger than the 6,000 in the Government's Mortgage Rescue Scheme with its such complex regionally variable rules that only six people so far have taken advantage of it?
Mr Lindley: What we do need to get first is a better supply of mortgage finance because all the existing lenders are concentrating on people who have got 40% equity or 25% equity. I share your concern that it is going to be very hard for first-time buyers to gather that amount of deposit without external help. What we need is mortgages up to 90% loan-to-value available. We do not want to see a return to the 125% Northern Rock Together mortgage, but we do want to see good value mortgages. With NatWest at the moment, if you have got a 75% loan-to-value mortgage then you are paying an interest rate of 3.69, but if you need a 90% mortgage you would be paying interest of 6.59, almost 3 percentage points higher. We cannot really see how those higher interest rates are justified based on the increased risk, but you are going to lock a lot of first-time buyers out of the housing market if you are saying to them, "You have to come up with a 40% or 25% deposit before you can get on the ladder".

Q86 Ms Keeble: I just wanted to ask one quick question on sale and rent-back values. Do you not think it is important that the public is aware of the difference between sale and rent-back values offered sometimes by the mortgage providers or, indeed, sometimes the local council do this as well, and the complete rip-off companies who under-price a property, mislead on the capital value, overcharge on the rent and then they lose their homes? Who should provide that advice so people can choose carefully between which options they go for?
Ms Edwards: People do need to understand the difference and what their rights are. They are probably best getting that from an independent advice agency like Shelter or Citizen's Advice Bureau.

Q87 Ms Keeble: That needs a lot of signposting though.
Ms Edwards: It does.

Q88 Ms Keeble: Most people think that advice costs as well.
Ms Boycott: There also need to be advisers there to do it. There has been signposting. Our helpline can only currently meet 30% of its call volume, so even if people are doing the right thing looking for advice, there is an issue with capacity in terms of telephone advice in particular.
Chairman: Thank you very much, that has been very helpful to us. We have a second session in which we will be putting some of the points you made. Thank you for your help and no doubt we will keep in touch on this issue which will have significance in the months ahead.

Witnesses: **Ms Jackie Bennett**, Head of Policy, Council of Mortgage Lenders, **Mr Eric Leenders**, Executive Director—Retail Banking, British Bankers' Association, **Mr Adrian Coles**, Director-General, Building Societies Association, **Mr Peter Williams**, Deputy Director-General, Intermediary Mortgage Lenders Association and **Mr John Socha**, Vice-Chairman, National Landlords Association, gave evidence.

Q89 Chairman: Welcome to the second part of our session. Can you introduce yourselves for the shorthand writer, please?
Ms Bennett: I am Jackie Bennett. I am Head of Policy at the Council of Mortgage Lenders.
Mr Coles: I am Adrian Coles, Director-General of the Building Societies Association.
Mr Leenders: Eric Leenders, the Executive Director responsible for retail banking at the British Bankers' Association.
Mr Socha: John Socha, Vice-Chairman of the National Landlords Association.
Mr Williams: Peter Williams, Executive Director of the Intermediary Mortgage Lenders Association. That is the trade body for lenders who lend through intermediaries.

Q90 Chairman: Welcome. I will put my first question to the Council of Mortgage Lenders. We heard in the first session about the forecast by the economist, Ian Shepherdson that repossessions will hit 100,000 to 120,000 by 2011. Are your figures at variance with that?
Ms Bennett: We have only put out a forecast for 2009, we have not predicted forward, partly because we think it is too uncertain in terms of what happens in the economy, what happens with unemployment, for us to be able to make that forward prediction. Would you like me just to run through that?

Q91 Chairman: Yes, sure.
Ms Bennett: In terms of our forecast for 2009 we originally had a figure of 75,000 possessions for this year but we have actually revised that downwards to 65,000 for this year as a result of lower interest rates which is enabling people to be able to work with their lenders to stay in their homes. Also, as a result of lender forbearance, which is increasing, lenders are keeping more people in their homes, and as a result of Government initiatives which are encouraging more people to engage with their lenders or with money advice which, again, is enabling people to work together to be able to stay in their homes. As I say, we have revised that forecast down this year.

Q92 Chairman: I have got a couple of points from that. Unemployment is predicted to rise sharply over the next few months, say, and some people are talking about three million unemployed and, indeed, the departing MPC member, Danny Blanchflower, is saying by 2012 it could be four million unemployed. What would be the impact of an increase in unemployment, say first of all to three million, on the number of households in mortgage arrears and being repossessed?
Ms Bennett: We have not done that calculation. As I say, we restricted ourselves to looking at what might happen this year. We have indicated in our forecast document that if unemployment does continue to rise as predicted that will have a knock-on impact on arrears and possessions potentially going forward effectively worsening the position. There are obviously other factors at play here and we have not done that "If you get three million unemployed, what number of possessions would that equate to?" We simply have not done that calculation.

Q93 Chairman: Are there any comments about how sensitive the levels of repossessions will be to the interest rates?
Ms Bennett: We believe that it will be a combination of factors. Unemployment is clearly a key driver, and we believe not just unemployment but other factors around things like people will not get the overtime or the bonuses that they are expecting, perhaps will not get the pay rises they are expecting, and that will all feed through into that. Interest rates is clearly a factor. Lenders are telling us that because of the lower interest rates people are more able to make their payments. Moving people to something like interest-only is a much more realistic option at the moment because interest rates are so low. Again, a combination of higher unemployment, reduced unemployment and higher interest rates would have a serious effect potentially on arrears and possessions.
Mr Williams: If I may, Chairman, all of us would take the view that lower interest rates have been an absolutely key factor in keeping the lid on arrears and possessions. If interest rates begin to rise that is clearly a factor alongside unemployment, and I think in all the submissions that have been put in to the Committee there is a general view that next year it is possible that numbers will go up, it all depends on sets of circumstances. The most important factor going forward is restoring a normal mortgage market, a normal housing market, which allows households to trade out of their difficulties. In reality, of all the schemes that have come into play, the one that is most effective for most people is simply trading in the market.

Q94 Ms Keeble: I wanted to ask about mortgage lenders' behaviour. You heard the comments in the first half about the level of fees which are being charged for managing arrears. What is your comment on them because some of the levels are quite outrageous?
Mr Coles: Someone mentioned that Nationwide ended charges as soon as an agreement had been reached with the borrower and, in fact, that is general policy across the entire building society sector. I would argue that building societies especially are not guilty of the crime that is being suggested. I suspect most mainstream lenders would also come into that category, not just building societies.

Q95 Ms Keeble: Let us hear from CML and then look at some of the evidence.
Ms Bennett: In terms of the wider mortgage market it is certainly included in our industry guidance that it is good practice if somebody is in an arrangement to pay that they should not be charged a fee for that arrangement. There is a case that lenders are allowed under the same rules to charge a fee for the additional work that having somebody in arrears can cause. There is a balance to be struck because if that cost is not borne by those people who are in arrears it has to be passed on to the wider population, so everybody's mortgages would be more expensive.

Q96 Ms Keeble: Some of the evidence that was given earlier was that one firm was actually recouping its advertising fees through these charges, so it was not the case that what was being recouped were costs that would have otherwise gone to the general population.
Ms Bennett: That is something which the FSA is investigating.

Q97 Ms Keeble: Is the FSA investigating that currently?
Ms Bennett: Yes.

Q98 Ms Keeble: Do you know which organisation that is?
Ms Bennett: No, I do not.

Q99 Ms Keeble: It is a bank presumably, is it?
Ms Bennett: We do not know. They have not said. They have simply said it is four firms they are looking at for enforcement action and one of the issues they are considering is the charges that lenders make for people in arrears.

Q100 Ms Keeble: You must know which some of the four are?
Ms Bennett: I do not. I honestly do not know.

Q101 Ms Keeble: Let us have a look at the actual breakdown. Nationwide has got half of its headquarters in my patch and I am used to Nationwide doing quite well, although I do see they charge £95 for a visit of the debt counsellor. If we look at Skipton Building Society, which I think is still a building society, it charges arrears of up to a maximum of £100 a month, eg if you are in arrears for £1,500 the charge would be £30 a month. That is quite a hefty whack for an arrears charge, is it not? I do not see how you can say that building societies are following best practice.

Mr Coles: Does it make that charge when an arrangement has been made with the borrower?

Q102 Ms Keeble: It says 2% of the amount of the arrears each month up to a maximum of £100 a month. One of the banks, for example HSBC, is charging 0.5% of the amount of the arrears, so it is four times what HSBC is charging.
Mr Coles: I would need to go back to the Skipton and see whether that is a protective clause that they have put in and they might use in very rare circumstances if they are not getting engaged with the borrower, or whether that is a normal course of events that they pursue.

Q103 Ms Keeble: Certainly some of the organisations, and I want to come back to sub-prime, are charging very large amounts and it is simply not the case that the more reputable, the lower the charges. Certainly the banks where the Government has got prime shareholding are either not providing information or charging high charges. What is your evidence for your assertion that the banks or large mortgage providers are following better practice?
Ms Bennett: I did not make that assertion. It is the case that lenders are allowed to make a reasonable charge for the work that is—

Q104 Ms Keeble: They are allowed to cover their administration costs.
Ms Bennett: Yes. If there is a suggestion that is not the case that can be investigated by the FSA. It is the FSA who set the rules around this and the FSA can make those investigations. That has been part of the work that has recently been concluded by the FSA and they have said as part of the Mortgage Market Review later in the year that they will look again at arrears charges and handling.

Q105 Ms Keeble: Do you think that £100-£150 is fair and a reflection of the administrative costs for the visit of a debt counsellor?
Ms Bennett: It would depend on how that cost was made up. In the case of debt counsellors, again it is good practice and included in our industry guidance, a debt counsellor should only be sent when you are not able to engage with the borrower. Again, the customer should be allowed the opportunity to refuse that visit and take free debt advice which, of course, is available.

Q106 Ms Keeble: For Northern Rock it says on the visit of a debt counsellor that the charge varies "depending on the level of help you need". Do you think it would be right that if people need more help they should be charged more because presumably they are more in debt?
Ms Bennett: Again, people should be given the opportunity to refuse that visit from a debt counsellor and take their own free debt advice. As I say, lenders quite often will only use debt advisers when they cannot actually make contact with the borrower and the borrower will not engage.

Q107 Ms Keeble: Why should *Which?*, and it might be down to the BBA actually, have to go to the extent of submitting FoI requests to get information about things that should be open to the public and easily available, which is charges for the various aspects of mortgage arrears?
Mr Leenders: I would be surprised if it was necessary to go to the FSA with an FoI request to get details of charges. The point that was being drawn out in the previous evidence session was around some supervisory enforcement action which I think, quite rightly, should remain confidential until that is concluded. Thereafter, typically the FSA will publish its findings if it has found that it needed to uphold against a firm.

Q108 Ms Keeble: It has not been possible for *Which?* to find out some of these costs. Do you not think that those charges should be readily available so that people can see what the charges are and understand and make decisions?
Mr Leenders: I think it comes back to the first principle, which is where a borrower has engaged with the lender, typically the lender has discretion to wave or shade these fees, and that has not necessarily come out of the stark table that you have got before you. That is a consideration that would be taken into account depending on the extent to which the borrower has come forward to discuss their financial difficulties. It is not for me to say that it is not very difficult for some consumers to come forward because actually I think it is very difficult, but at the same time all the while a lender needs to chase to engage with the borrower to make sure they are discussing arrears there is a cost attached, unfortunately.

Q109 Ms Keeble: Clearly some of the charges have been quite at variance with the admin costs and that is why they are being looked at. Why should people not know which mortgage providers are being investigated by the FSA because people might want to think twice about taking out a mortgage with a mortgage provider who is currently under investigation?
Mr Leenders: I think I would hold the view that where there is an investigation there is not necessarily guilt. There are also degrees of crimes and misdemeanours. Where a minor issue has been resolved to the satisfaction of the regulator, that is probably something that could be dealt with in-house. We have seen plenty of examples where the FSA has named and shamed, has fined, and, equally, the Banking Code Standards Board has named and shamed as well. Where there have been significant breaches of rules or codes, we do see the names published in the public domain.

Q110 Ms Keeble: Why should people not know at the time that there is a complaint made and investigation taking place? That is not going to prejudice the investigation, it is simply saying that it is being looked at.

Mr Leenders: For me, I think there needs to be a distinction between perhaps an unfounded complaint and a complaint that has some grounds. I would side more with the Financial Services Authority in this circumstance where they would like to have the opportunity to investigate the issue before they make public whatever findings they might reach.

Q111 Ms Keeble: I wanted to ask about forbearance, which you might want to comment more about, Adrian and Jackie, and in particular the relationship between forbearance and negative equity that was raised in the first session. Who would like to comment on that?
Mr Coles: Just because you go into negative equity does not mean that your ability to repay the loan is endangered. Clearly it is more difficult to move if you are in negative equity, but as long as you are still in employment, you have got an affordable mortgage, there is not necessarily a link between negative equity and the development of arrears and moving into repossession.

Q112 Ms Keeble: In Northampton I think it is estimated that about 15% of properties are in negative equity according to the report that was published in the *FT* and *The Independent* as well. Where unemployment has doubled over the past year, where you have got increased unemployment, people losing income through lost shifts, they cannot keep up the mortgage payments and they cannot sell the property either. Is it not a real pressure for homeowners?
Mr Leenders: It is a real pressure for homeowners and that is why those homeowners should go and talk to their lenders as soon as they possibly can to see what rescue mechanisms can be put in place and what assistance can be given, both by the lender and any money advice agency they might go to.

Q113 Ms Keeble: Is it also causing any problems for the mortgage providers because of the difficulty of organising their financing because of the need to ensure that they have got real security for their financing in general
Mr Coles: In that situation, what a mortgage lender will do is bend over backwards not to take possession because that crystallises the loss. If the likelihood is that if the borrower can rescue the situation, if it looks as though they might return to full-time employment if there is an opportunity to get a job then they are less likely to take possession at a time and place of very high negative equity.

Q114 Ms Keeble: Do you see any problem down the line for the mortgage providers if they have not got proper security for their members?
Mr Coles: Yes, clearly. There is the potential there for the loss to be crystallised and you could record a loss in the books, and lenders do not want to do that but clearly there is a potential problem.
Ms Bennett: As a precaution you have got to remember that the number of arrears and possessions are still very, very small as a proportion. Of course it is significant for those people going through that problem, and I would endorse what Adrian was saying in terms of negative equity. If somebody really wants to give up and sell the property they can work with the lender and do something called an Assisted Voluntary Sale, so the borrower actually stays in their home and sells the property themselves, so they do not have to go through the courtroom with all the additional cost that might bring. They can get a value for the property and they can talk to the lender about how they deal with that shortfall there. Other lenders have negative equity products where they allow people to move on to another property if they need to move for work and things like that, so there are options available for borrowers, but absolutely talking to the lender is the first thing that people should do.

Q115 Ms Keeble: Do either of you see the development of a sort of sub-prime product in the UK? We have sort of accepted that we do not have that problem here but do you see any risks of that developing because throughout the previous session a number of people referred to sub-prime out there.
Mr Coles: You have to remember that it is the case that obviously sub-prime borrowers, adverse credit borrowers, have come to lenders with a history of problems, so in that sense they are more risky borrowers and do have a greater propensity to default so, yes, there is a greater risk. I have to say the problems we have here in relation to the borrowers are unlike those in the States.
Mr Leenders: I think there is a further point and that is as a consequence of an individual's financial circumstances there might be a movement to sub-prime. The individual might have incurred an adverse credit history. That touches on another point that I would like to return to on unemployment, which is that we are starting to look quite deeply at who it is that is becoming unemployed. For example, the record increases in the 39s-45s typically are family homeowners which is something we need to think through. At the same time and in the context of unemployment we need to think a little bit about the return to work period. A couple of years ago that was maybe three months or so, but now it is stretching out and that means the redundancy payments and the savings need to be eked out longer and that will probably mean more arrears as a consequence of the limited opportunities in the job market which is something, again, we need to be alive to.

Q116 Ms Keeble: I also want to develop the two-tier structure where you have got sub-prime.
Mr Williams: It is a point we make in our submission that many householders are sustaining their position rather than curing their position, and in a sense that is true of forbearance generally, that lenders, with borrowers, are managing through the current circumstances but people are not necessarily recovering them, which is why I think there is a nervousness on this side that unless the wider contextual situation improves borrowers will face

difficulties because increased forbearance ultimately puts up the amount of interest charged against the property and there comes a point where the situation for that household is very, very difficult. That is particularly true in the non-prime market at present because the non-prime market has effectively ceased the lock rate, there is no effective lending into the non-prime market simply because the mortgage lenders do not have any funds to lend and that market is largely inactive. That is making it very difficult for householders in that market to trade through, to move, to re-mortgage, and it is also making it difficult for individual lenders to manage those processes in ways that other lenders who have access to more finance in the market are better able to do. The two-tier system you were referring to is certainly there because of the way the mortgage market is frozen in certain parts of the UK.

Q117 Ms Keeble: Just one more question, which is on the comments that were made previously about the FSA Code of Business for Mortgages and whether it is too vague and enforcement both of that and the procedure for dealing with arrears, the charges and so on.
Mr Williams: Can I just make one quick comment. The CML's guidance on that, which is trying to bring together the regulatory focus on arrears in terms of the principles—MCOB 13—and the practice guidance issued by the CML, which is widely used across the industry, brings together, if you like, principles and practice in a very, very creative way. That has been an effective way forward by trying to marry the high level with actually what people do.
Ms Bennett: Thank you, Peter, for quoting our guidance. We did that that because we felt that the high level principles that were set out by the FSA were not detailed enough for lenders to be able to understand exactly what sections meant. We also had conversations with the advice sector who could not understand what lenders would be doing on a day-to-day basis from the high level principles. That was why we published the guidance. We would like to see the FSA working with lenders. Whilst I do not think any of us on this side of the table believe there is any systemic failure within lenders of the arrears and possessions processes, it is clear that there are probably individual cases where it does not work as well as it should. We would like to see the FSA working with lenders to resolve their problems almost before they become problems. In some ways, enforcement in itself is a failure because those problems have not been addressed. We do not want a regulator to fear. In some ways that is perhaps not a constructive way forward if you want lenders to be able to work with the rules, that is not something we would like to see.
Mr Coles: There is always a balance to be drawn between principles which are vague and no-one can tell whether anybody is following them, and rules which are so detailed that the lender cannot step outside of the rules and give a tailor-made service to people's particular circumstances. You have got to get that balance right and probably the CML approach has got that balance right.

Q118 Chairman: In terms of the propensity of companies to be more open and transparent, Mr Leenders, do you not think the industry has got a little bit to go on that yet? If a company is not treating customers fairly it is important. I am reminded of our previous experience with the Banking Code Standards Board when they indicated to us that with regard to the basic bank accounts, banks that were falling behind would not be named and it took a letter from me—HBOS was the first to agree—to agree that they were going to expose the progress of basic bank accounts and then every bank followed. I think it has done the industry good at the end of the day. The propensity to be more open still has a bit to go. Do you not agree?
Mr Leenders: There probably will be some way to go, it depends in which context you look at that propensity to be more open. There are winds of change and we would look to be more open. If we are looking specifically to the point I discussed with your colleague, I do hold quite strongly that there are investigations that need to take place and those should remain confidential because, of course, the groundings of the complaint need to be looked at quite thoroughly.

Q119 Chairman: If people have been affected at that time and the propensity is for other people to be badly affected in a situation there has got to be a judgment made and I think the FSA has got a bit to go in that area yet.
Mr Leenders: I would like to think that part of the internal discussions is that judgment call by the FSA.

Q120 Mr Todd: I think most of you heard the discussion about the FSA's Mortgage Conduct of Business Rules which were drawn up in rather happier times. Do you feel that those now need to be urgently reviewed and, indeed, should have been reviewed already reflecting the circumstances that we are now in?
Ms Bennett: No. We do believe they are fit for purpose. As we have been talking about this, we do believe MCOB 13, which is the chapter which regulates arrears and possessions, is fit for purpose. Combined with our industry guidance, which puts a lot more colour around what lenders should be doing on a day-to-day basis, we do believe they are fit for purpose. The FSA has said as part of its Mortgage Market Review later this year it will look again at whether they are appropriate. The thematic inspections that the FSA has done, as I say, have not found a systemic failure of those rules.

Q121 Mr Todd: If those rules are fit for purpose, why did the Government see fit to change the guidance to courts on dealing with repossession processes which indicates that perhaps they did not think these rules were robust enough?

Ms Bennett: I think there was some confusion, if I may be so bold, within the court system in terms of MCOB 13 and what it required. We had been through a period where there were fewer arrears and possessions coming to court, so we needed to find a way to make the judiciary very familiar with what MCOB actually requires, and what the pre-action protocol does is ensure that the lender has been through all the steps that they can and that repossession really is a last resort before it is taken to court.

Q122 Mr Todd: So this was an educative process for the judges and not an attempt to deal with perhaps failures in the industry itself. That is your argument, is it?
Ms Bennett: Approaching possession in a consistent manner and ensuring that all the steps had been gone through before the case was taken to court.
Mr Coles: And it is consistent with MCOB. There were no new rules introduced as a result of that.

Q123 Mr Todd: What I am trying to draw out is that perhaps MCOB was not being followed properly, perhaps because it is not as crystal clear as all that, and the change in the pre-action protocol was an attempt to produce a longstop to deal with the likelihood that companies would continue to take their chances in court without having gone through proper due process.
Mr Williams: I think it probably just meant there was a more coordinated approach between the legal system and practice in the industry and it was an appropriate upgrade for them. The Mortgage Market Review is an opportunity to bring all of those things together. There have been a lot of new developments, as you rightly say, and the Mortgage Market Review is an opportunity to tidy all of those strands up.
Mr Leenders: If we were to take a step back there is probably room for some regulatory review because it strikes me as slightly incongruous that, for example, second charges are dealt with under the Consumer Credit Act or, indeed, not regulated, which is enforced by the Office of Fair Trading, not the FSA. Buy-to-let mortgages do not really fit under any regulatory regime. There is probably some further work to do about sale and lease-back. Looking at the totality of credit provision, secured and unsecured, our view would be that perhaps the discussion should go beyond MCOB and a review of MCOB to a consideration of whether—where we sit as licensed deposit-takers—that regulation of all credit should fall within the remit of the Financial Services Authority.

Q124 Mr Todd: That is very helpful. Can I just clarify with Mr Williams, what is the difference between sub-prime and non-prime?
Mr Williams: Non-prime is the term used to describe the general spectrum within which sub prime and other categories of non prime lending sit. Forgive me, I will attempt an explanation and no doubt just make it worse now! You have to go through pain to get to pleasure!

Q125 Mr Todd: I will watch you digging. Go on.
Mr Williams: In terms of the spectrum, somebody who has only missed a payment, let us imagine, would be categorised as near-prime through to somebody who has had a county court judgment that might be categorised as heavy sub-prime. It is a spectrum, a continuum of non-prime lending –Jackie Bennett referred to it as adverse credit—a term in my view that is equally negative—running from near-prime to sub-prime.

Q126 Mr Todd: Can I ask you whether your members are focused on dealing with, however you define this sector, that particular sector of borrowers? I noted the description of yourselves as the mortgage trade body for lenders who distribute mortgages via intermediaries.
Mr Williams: Correct.

Q127 Mr Todd: It did not tell me exactly who these bodies were, except looking through it appeared to be the non-traditional sectors to some extent which raise money through the capital market.
Mr Williams: It is a broad church. It includes all the major banks and building societies, so members of the BSA, the CML and the BBA are members of IMLA as well, because of the intermediary focus. Virtually all of our members are members of other trade bodies. Because they are intermediary-focused it includes a lot of specialist lenders who only sell through intermediaries rather than through branches. They do not have a branch network, they are not deposit-based, by and large they are capital market based using securitisation. There is a focus there around intermediary sales and specialist lending.

Q128 Mr Todd: They have been focused on the more specialist area, if you like?
Mr Williams: Yes. A lot of IMLA members would have been active across the non-prime spectrum.

Q129 Mr Todd: From my limited exposure as a constituency MP those people I have come across who are having difficulty have tended to be those who have borrowed money from the non-traditional sector which I imagine would have had a product sold to them by an intermediary.
Mr Williams: Yes. Again, this is a very, very wide spectrum of lenders. Eric has already referred to second charge lenders who are not in the IMLA membership and there will be a large number of other lenders who are not as well. There is a very wide network of lenders who operate in the market for people with difficulties.

Q130 Mr Todd: How active are the FSA in addressing this sector? To some extent the big boys who are represented down the table everyone knows about, but a lot of these smaller operators are not household names, so if you get into difficulty and someone offers you a way of solving it funded by this—

Mr Williams: Many of these smaller names are, in fact, subsidiaries of major lenders. GMAC, for example, is a subsidiary of General Motors and became the 10th largest lender in the UK. I think the characterisation of the non-prime market as somehow backstreet and sordid is—

Q131 Mr Todd: That was not what I said.
Mr Williams: No. It is where people go in their thinking and I think it is inappropriate.
Ms Bennett: It is the case as well, as Peter said, they are our members as well and the FSA's rules apply equally across the whole range of lenders.

Q132 Mr Todd: Let me just turn to the FSA's rules and how they are understood by the public. Adrian, you were talking about this base being perhaps so vague that people did not necessarily understand what they were getting. You may have heard what I was suggesting was a rather more robust and clear communication of what the protection meant and when you have got a mortgage what is it that is being looked after here and how is the governance of this mortgage going to operate and how are you protected should something go wrong. Do we not need something much more clearly written than that so that the consumer understands what is being done? To some extent the industry has attempted to fill this space themselves.
Mr Coles: I think the FSA has made big steps forward with its *Money Made Clear* website as well which gives general advice, not clearly on individual specific mortgages, and the BSA, CML and other trade bodies' websites have improved tremendously over the last few years to give that clearer understanding of what the whole mortgage process is about.

Q133 Mr Todd: Is not this aversion from the specific by the FSA perhaps the enemy of consumers in some circumstances? Ms Keeble was asking about the offer of debt advice, but should it not be a straightforward obligation of an advert that when they approach a customer offering to provide debt advice for £100 or whatever, they should be obliged to say "You can, of course, go to . . . "
Ms Bennett: And they do.

Q134 Mr Todd: Is there an obligation as opposed to the good practice?
Ms Bennett: There is. FSA rules actually require lenders to tell—

Q135 Mr Todd: To make it absolutely clear?
Ms Bennett: Yes. The pre-action protocol reinforces that point.

Q136 Mr Todd: That is true of a number of the offers of assistance of various kinds which you referred to as alternatives. You have to say many of the customers you are dealing with are perhaps not as well-tuned into their rights so how that is conveyed is a rather important element to this.
Ms Bennett: Absolutely. We know lenders who have been working very hard on this and they try a number of different methods to engage with customers: they will write to them; they will phone them. We have heard of things like texts. I can assure you that by the time a debt counsellor is being sent there have probably been three or four attempts to try and make contact.

Q137 Mr Todd: We have had the discussion over the FSA reporting process. Do I take it that none of you have an objection to public exposure of a company when that enforcement is concluded and the FSA has the freedom to judge and say while there is process and discussion going on over enforcement no publicity should be drawn to the company involved?
Mr Coles: So do not run the risk of naming and shaming the innocent; go through the proper process and find them guilty.

Q138 Chairman: How long can that enforcement process take?
Mr Coles: You should put that question to the FSA. It depends how complex the issue is.

Q139 Chairman: The thing that worries us is you can be talking about a year as normal.
Mr Coles: That sounds a long time.

Q140 Chairman: But the company in question could still be going along with its bad practice and people are affected. How do we deal with that, Adrian?
Mr Coles: It depends on the complexity of the case, how difficult it is for the FSA to understand what the firm is doing and the firm needs time to prepare its defence against allegations that might not be correct. Without knowing what the details of these cases are it is difficult to state and I think you should press the FSA on that. A year sounds a long time but there may be complexities that we do not understand.

Q141 Chairman: There is a suspicion that the consumer may be getting a bad deal and new consumers may be getting bad deals.
Mr Williams: The only reassurance I can give you on that is in the case of the latest enforcement orders I believe all those lenders are inactive in the market at present and, therefore, in that sense your concern about ongoing consumers is slightly minimised. There are a number of lenders having very close relationships with people like the Consumer Credit Counselling Service and their IT systems are set up to provide a hot key link to those agencies, so free advice is almost automatically given rather than fee-based.
Ms Bennett: If FSA supervisors are working with their lenders, and we know following the review the FSA had last year that they are doing what they call close and continuous supervision, hopefully, as I said, that means that those processes can be improved on a day-to-day basis and if there is some underlying problem around enforcement then that should be dealt with by reviewing policies.

Q142 Chairman: From our point of view the worry is that consumers will be continuing to get a bad deal. Also, there is a passive element from the industry here, it has been passed over to the FSA, it is nothing to do with it but if you get good self-regulation and the gamekeeper turned poacher approach then the ones that are committing that bad practice can get kicked out more quickly and consumers will have better deals. There is a lot that can be done on that.
Mr Williams: I am sure there is. It is worth saying that supervisors from the FSA working with individual firms are very active on these issues, they are not pushed on the backburner.
Chairman: There is work to be done.

Q143 Sir Peter Viggers: There have been some disturbing stories about practice in the sale and rent-back sector. Are these landlords your members in the National Landlords Association?
Mr Socha: I can say almost categorically no, but definitely there have been cases where there has been quite appalling loss of value to the person who owns the house. That is definitely going on and that is why we welcome the FSA's novel approach of introducing an interim regime straight away rather than waiting a year for the actual legislation to pass through Parliament.

Q144 Sir Peter Viggers: Perhaps I can ask all of you who wish to contribute, do you think that the sale and rent-back sector has a useful and respectable part to play in the future of housing and finance?
Mr Coles: I would say yes, if it is run properly. Clearly the sorts of abuses we heard about earlier that have hit the newspaper headlines you would like to see regulated out of existence, but to say under no circumstances whatsoever can a homeowner ever sell their home to a future landlord and then rent it, if that deal is done transparently and fairly that is what we want. We should not outlaw all practice, it can work very well. We should certainly outlaw the sorts of practices that we have heard described today and in the media.
Mr Williams: I would agree with that. If you look into the different markets, it is the base for the home reversion scheme. Home reversion schemes are where people sell their homes to another company and then rent them back effectively. If done properly it is a sensible device.

Q145 Sir Peter Viggers: Do you think that the FSA now has a clear handle on the market and the proposals it put forward both for its interim regime and its later regime to come into effect in about a year's time will deal with the scandals?
Mr Socha: Yes, we feel that it will limit the number of operators in the market simply because the nature of FSA regulation is quite arduous. It is not just a case of filling in a couple of forms. I think that will remove a lot of the players from the market simply because of the amount of paperwork they are going to have to do to be compliant and continue to be compliant.

Q146 Sir Peter Viggers: Will the regime, when implemented, ensure that each individual who wishes to enter into such a scheme has independent advice?
Mr Socha: The old phrase "you can take a horse to water but you can't make it drink" applies here. Yes, certainly the whole thing is set up so that there is independent advice available though some of the actual operators do not use a valuation that perhaps we would understand as homebuyers ourselves. There is definitely a valuation in there somewhere. The idea behind it was to get the homeowner, who is a person in distress, to see the sense of getting the property valued independently. Even when we looked at this we made that as a fundamental part of it, that there would be independent valuation of the property.
Mr Socha: I think in the context of competition and market forces, mortgage rescue is a derivative or one aspect of the same principle. If we could get that to be perhaps more widely used then there would be alternatives and those considering that type of product might gravitate more to a mortgage rescue product if it is commercially more viable to them.

Q147 Sir Peter Viggers: Do you think that the size of the sale to rent market is likely to increase as a result of the economic downturn?
Mr Williams: Yes.
Mr Coles: That seems likely. If you are a renter you get more support from the state through housing benefit if you are a low income person compared to if you are an owner-occupier, so the incentive for an owner-occupier who suffers a big reduction in income is to look at the possibility of becoming a tenant.
Mr Socha: There is a mistake in that summation. Currently, the Department for Work and Pensions make it quite clear that you may not claim local housing allowance—housing benefit is now defunct—on a house you have owned in the last five years, that is a specific regulation, therefore if you are hoping to claim local housing allowance on a house you have sold and rented back, you cannot do that. There are certain circumstances where local authorities may take the view that re-housing a family would be quite distressing to the family and that is in the ambit of the local authority. Remember, we are dealing with 480 local authorities across Britain who administer local housing allowance. It is down to the officer on the ground, the circumstances and the cost of re-housing that family.
Mr Williams: That is a very important point. It relates to a point Mr Cousins raised earlier about the shape of home ownership going forward. Sale and lease-back does have a role. Mortgage Rescue, unfortunately named in my view, is not really about mortgage rescue but achieves an end with families preserved in their homes. All of those things require a degree of flexibility around the system. Some of the structures around housing benefit, the role of local authorities in terms of buying back property and facilitating those moves, are all constrained. We need to think about how the world of home ownership is

now, how it might be in the future and how we manage that transition. Sale and lease-back is part of that process.

Q148 Chairman: I took this up in September 2007 with the BBC, as was mentioned earlier, on *Watchdog*. I contacted the CAB and they are seeing some companies advertising more prominently in newspapers and radio and leafleting in some areas, and one of the worst cases the CAB reported was one that involved an individual who sold his house for 40,000 less than the market value. The BBC 5 Live investigation team reported typically that the sale and rent-back companies offer 75% of the market value and in some cases they have heard as low as 40%. In one case, the BBC 5 Live report said a woman was said to have had dozens of offers of 50% of her home's value, her mortgage repayments were £325 and she was being asked to pay rental rates ranging from £474 to £500 a month. This has put people in jeopardy and they are finding themselves without any roof at all over their heads within a few short months of such a deal being completed. Are you confident that such scandalous examples are a thing of the past now?
Mr Socha: They will be once the system comes in.

Q149 Chairman: When will the system come in?
Mr Socha: Tomorrow. The start of registration is 1 July 2009.

Q150 Chairman: So it is a thing of the past from tomorrow?
Mr Socha: No, from the end of the month. They have one month to register.

Q151 Chairman: The end of the month is actually just a couple of days away.
Mr Socha: 31 July, my apologies. They only have one month to register with the FSA to operate sale and rent-back. If you are not registered after 31 July and doing sale and rent-back then you will be committing an offence under the Financial Services Authority.

Q152 Chairman: So those unacceptable schemes will no longer take place?
Mr Socha: We are hoping that there will be some publicity put behind this.

Q153 Chairman: When you say you are hoping, it does not seem as if it is as firm as we would like.
Mr Socha: We are asking people like the FSA to advertise to the consumers that they should look for somebody who is registered with the FSA. It is quite straightforward.

Q154 Chairman: If you see such schemes taking place after 1 July, or whenever, as an industry will you ensure that the FSA gets to know about it so that we get rid of these scams?
Mr Socha: We have already talked to the FSA and they are doing peripheral monitoring, I think that is the technical term, which is looking for these types of people. As a little example, I actually took the liberty of buying two of the redtops this morning at the train station here and there were about four in *The Sun* and three in *The Mirror* advertising sale and rent-back schemes.

Q155 Chairman: So we need to get rid of that.
Mr Socha: I would have thought so.

Q156 Chairman: How good has the FSA been on that? Is everything as good as it should have been?
Mr Socha: They will have to make sure that they are FSA registered and that will be clear-cut from the end of July.

Q157 Chairman: I think what you are telling us is that whilst regulation is taking place, there is real work in progress to ensure that these scandals are a thing of the past?
Mr Socha: Indeed.

Q158 Chairman: Before we move on, CML have spoken about the industry guidance on MCOB 13 and treating customers in arrears fairly. What force does this guidance have and what evidence do you have that your members adhere to this guidance?
Ms Bennett: We, as a trade association, do not have any regulatory powers. As I said, we produced the industry guidance to try and help the industry but, ultimately, if the FSA believes that lenders are not complying with their rules, which we believe are added to by our guidance, then it is the FSA who can take that action. Borrowers also have the opportunity to complain to the Ombudsman's Service. If they believe they have been treated unfairly by their lender they can take the complaint first to their lender and then, if they are not satisfied with that response, they can take that to the Ombudsman. What we do know is that a large number of members, and I cannot tell you how many because we have not been through the process but we know from talking to members, have actually done a gap analysis against their own policy and practice using our industry guidance and have made amendments as a result of that. I know the FSA also did a chief executive officer letter last November asking all lenders to review their processes against MCOB 13. We are not privy to the results of that exercise but all lenders were asked to write to the FSA saying what steps they had taken to review their processes and policies as a result of re-looking at those.
Mr Coles: Last year, Chairman, the FSA did say in a press release: "Mainstream lenders were largely compliant with FSA requirements in this area of arrears administration and have policies and practices that should ensure that customers are generally treated fairly". We have taken the FSA at their word there and that is the statement they have made.

Q159 Mr Fallon: We were told this morning that the Mortgage Rescue Scheme has now only helped six people instead of 6,000. Why is that? Is the scheme simply badly designed?

Mr Williams: No, it is a complicated scheme. The six who have been helped as opposed to 6,000 planned but you have to recognise that regardless of the numbers that come out at one end there is still an enormous amount of interaction in that process which means that final output number could massively mis under-represent the total impact that scheme is having. It is early days and it is complicated. It does take time to negotiate these difficult circumstances for the households to deal with. The reality is that in that process quite a lot of reconciliation is then arrived at between lender and borrowers, so the output of six people having their homes saved, or whatever the number is, is only the tip of the iceberg of the benefits that are coming through.

Q160 Mr Fallon: How do we measure the iceberg? How can we be sure the scheme is working if we only see six people today being helped by it in six months?
Mr Williams: There are a lot of other people interacting within the system.

Q161 Mr Fallon: Yes, but how can we be sure that they are interacting positively?
Ms Bennett: The figures that were released this morning suggested that over 5,000 householders have actually been in touch with their local authorities. We know from talking to lenders and the Communities and Local Government Department that a lot of those people are being helped by lenders, but through their normal forbearance processes, and that is right because that is not using taxpayers' money to help them. Quite often these are people who have not been in touch with their lender before. This is another way of getting people to engage with lenders and money advisers and we think it is a very positive thing from that perspective.

Q162 Mr Fallon: So the purpose of the scheme is to encourage people to talk to their lenders, is that right?
Mr Williams: It is to avoid unnecessary homelessness and in that process clearly a conversation with lenders has to take place on a sustained basis. For many people that is a very difficult thing to come to terms with for all sorts of reasons. In the circumstances of losing your home there is a great deal of difficulty people have facing up to that and we should not underestimate that in any way.
Ms Bennett: For some people it may be simply receiving some budgetary advice, debt advice, making sure they are maximising the benefits they can be claiming, and sometimes people are more prepared to talk about that with local authorities than they are with their lenders.

Q163 Mr Fallon: How many people do you expect to benefit from the scheme by the end of this year?
Ms Bennett: I think that is a very difficult figure to give.
Mr Williams: Again, I agree with Jackie. I think the benefit is 5,000 have already been in touch and you can expect that number to continue to rise and you can expect that to be at least 10,000, and that is a lot of people who are benefiting. In terms of people who finally come out of the other end as "rescued", it will be small numbers I suspect.

Q164 Mr Fallon: Let us turn to the other scheme then, the Homeowners Mortgage Support Scheme. How should we measure the success of that?
Mr Williams: That has been a matter of much argument and debate for all of us who participated in the negotiations with the Government on the Homeowners Mortgage Support Scheme. There was a lot of discussion about the scale and ambition of it: was it 100,000 households, was it 40,000? The numbers that we understand have come through at present are relatively small but the system is complex. One of the reasons it is complex is that you have to set up a major reporting system between CLG and lenders to track the progress of the individual cases coming through. That has inhibited quite a lot of lenders early on from participating. It has taken a number of lenders time to align their IT systems with the CLG reporting system which means, to go back to the non-prime market, a number of specialist non-prime lenders are about to sign up to the scheme but it has taken a long time to get everything in a row to make effective reporting. Once you start reporting it is in the public domain.

Q165 Mr Fallon: But this scheme was announced two months ago.
Mr Williams: Yes.

Q166 Mr Fallon: Why has it taken two months?
Mr Williams: I think two months is nothing in the scheme of trying to set up a very complex reporting scheme.

Q167 Mr Fallon: I thought some lenders were refusing to join the scheme on the grounds that they were offering better arrangements themselves. Is that still the case?
Mr Coles: Certainly that has been the case for building societies. One building society has formally signed up to the HMS Scheme.

Q168 Mr Fallon: One out of how many?
Mr Coles: Out of 53. The other 52 have all signed up to a BSA document that, broadly speaking, gives the same guarantees to borrowers as HMS does. It goes back to the point I was making earlier that if you are not constrained by HMS you can give more tailored solutions and can react more accurately to the precise needs of individual borrowers rather than go down the very specific, rules-based route of HMS. The other point that follows from Peter's point is that it is very complex. If you look at a medium-sized building society, they might have one or two people who qualify for this scheme and to set up the detailed IT systems, which cost a lot of money to set up, at a time when there is not much spare cash around in the mortgage lending industry is just not cost-effective. It is far more sensible for you to employ an extra member of staff to give arrears advice to customers

rather than employ an extra IT member of staff to set yourself up for a scheme that might help two of your customers.

Q169 Mr Fallon: So the HMS is really pretty pointless alongside the BSA Scheme?
Mr Coles: I do not think it is pointless at all.

Q170 Mr Fallon: But only one of 50-odd members has participated.
Mr Coles: There are two points. First of all, the publicity engendered by the announcement of the scheme has created an environment in which customers will approach their lenders more to discuss their problems and, as we have always said, that is the key to helping people get over their difficulties. Secondly, HMS has emphasised the role of money advisers and the Money Advice Trust and other providers of debt advice. We worked to produce a leaflet with Money Advice Trust on what to do if you cannot pay your mortgage. I think it has brought the advisers and the industry closer together and that has been another benefit of the scheme. We very much support the sentiment behind the scheme and in publicity terms it has had some useful outputs, but I think you have to look wider than just the numbers who are not, as Peter was saying.

Q171 Mr Fallon: The net benefit of both these schemes really is they have just got people to talk to their lenders more?
Mr Coles: The publicity effect has been much greater than the precise effect of helping specific numbers of people so far.
Mr Leenders: I do not think that contact can be underestimated because at the end of the day that is the entry point for any form of support for someone in financial difficulty. You have to establish that communication and that dialogue. Whilst you are absolutely right that it seems particularly frustrating that there is a small number of beneficiaries from the direct objectives of the scheme, in the context of the number of inquiries that have commenced a dialogue in some circumstances where there might not have been a dialogue at all, that is very beneficial.
Ms Bennett: We can see that coming through in the numbers now. Lenders are being more forbearant for longer. The number of possession orders made by courts in the first quarter of this year was much reduced and had actually gone down from the last quarter of last year. All of these things are demonstrating forebearance, and I know it is very difficult to find the true evidence of exactly what is happening, that all of these things taken together are having an impact and helping more people stay in their homes.

Q172 Mr Fallon: They need to have an impact if you believe the figures we were given this morning, that the number of people three months behind will continue to rise this year and well into next year.
Mr Williams: Yes, we accept that.

Q173 Chairman: If I could come back to the Homeowners Mortgage Support Scheme, from what I can gather there is an IT problem there. The Government came up with this scheme and companies are saying, "It is too complex for us". What we have got to ask as a Committee is how do we end up with situations like that? Why could the Government not have made a simpler scheme so that there would have been a fit between what the Government wants and what companies want. Take us through that.
Mr Williams: I think the Government is between a rock and a hard place on this. Because ultimately Government is offering to cover some of the costs that lenders incur by forbearing, rolling up the interest, there is a public expenditure issue here which clearly has to be tracked and logged very carefully about who comes into that scheme, are they eligible and are they appropriate, right through to finally when they come out of this scheme and there is a bill to be settled, is it the right bill, was it justified and has the lender kept that down. To get that comfortable for those lenders who are racking up arrears through this period on the assumption at the end in the event of default they can reclaim it, the lenders have to be utterly confident about that and the Government has to be utterly confident that is the right figure at the end. All of that is quite a complex process.

Q174 Chairman: Adrian, there must be some way we could make it better?
Mr Coles: The problem is that the legal requirements behind the scheme are extremely complex. It is not just the IT. The legal document governing lenders' participation in the scheme was 187 pages and understanding that when it is written in legal jargon and getting your head round it is very complex indeed. On the other hand, as Peter has said, the Government was very concerned to protect taxpayers' interests, to make sure that money was not paid out in circumstances other than it intended. We would very much like to see a simpler scheme and had the scheme been simpler I am sure more building societies would have signed up. You have got this distinction between the Government very concerned to protect the taxpayers' interests and building societies essentially wanting a simple, straightforward scheme to administer. I do not know in the days of modern bureaucracy how you bring those two things together easily.

Q175 Chairman: There has been quite a bit of talk about irresponsible lending, but how much of a problem in terms of arrears and repossessions has there been as a result of irresponsible borrowing?
Ms Bennett: Reporting that we get back from members suggests that a number of people who are in trouble are in trouble because they have second and other unsecured charges against their properties. This comes back to a point that we were discussing earlier in terms of having an overall approach to regulation of a number of these different

parts of the financial system because borrowers can get different amounts of money from different types of lenders—not those represented here today—and that can be the thing that actually tips them over the edge. It is not necessarily the first charge mortgage, it is sometimes the other borrowing that they have taken out to support that that is actually causing them the problems, particularly if their income is reduced by some other means, whether through unemployment or some other factor.

Mr Coles: I think that is the key point. These problems are not caused generally in most cases by irresponsible lending or irresponsible borrowing, they are caused by a significant change in circumstances after the loan is taken out: relationship breakdown, loss of income, growth in unemployment. That was what the research showed in the early 1990s and I suspect that is what the research will show when this recession is over as well. You cannot foretell the future. Some people will take on loans in good faith and some lenders will lend in good faith where it turns out two years later that people cannot cope.

Q176 Jim Cousins: I wonder if I could just ask the Council of Mortgage Lenders, is GMAC one of your members?

Ms Bennett: They are.

Q177 Jim Cousins: They are. Have they always been?

Ms Bennett: Yes.

Q178 Jim Cousins: We were given some figures by *Which?* for the number of borrowers who were likely to shift off fixed rate mortgages over the next 18 months. I think the figure was roughly 1.5 million. Does that fit with your own understanding of the situation?

Ms Bennett: We have not done any recent research. I can go back and check whether we have got up-to-date figures, I am not sure whether we have or not, but if we have then I will submit them to the Committee.[1] That sounds in the right sort of ballpark figure.

Q179 Jim Cousins: Is it not entirely possible, although perhaps rather difficult to predict precisely, that we will be faced with large numbers of people who will find themselves in an unsustainable home ownership situation?

Ms Bennett: We would like to think not. If we remain in a low interest rate environment then those people are likely to be coming off fixed rates on to a lower rate than they are currently on. I know that from talking to some of our members, who are also members of Peter Williams' organisation as well, where they are saying, "We know if we can keep borrowers at their fixed rate for the next few months they will be coming off and paying a lower amount because of the lower interest rate environment at the moment". We also know that lenders are working very hard across the board in talking to people about what might happen when they come to the end of the fixed rate if they are going to be facing some sort of payment shock, but I have to say the discussions we are having in the industry at the moment are not about worrying quite so much about that big upward payment shock that we were looking at perhaps a year or 18 months or so ago when broader interest rates were much higher.

Q180 Jim Cousins: Have you raised with Government as part of the early stages of this Mortgage Market Review the need to consider perhaps a simpler and broader menu of exit strategies from home ownership?

Ms Bennett: We are talking to the Financial Services Authority about a whole range of issues that might be covered in their Mortgage Market Review and certainly looking at higher risk products, whether that be for people who have adverse credit histories, higher loan-to-value, higher loan-to-income, all of those areas are being explored at the moment.

Mr Williams: I think there is no doubt that if you put together the whole package of the safety net underneath home ownership it is full of holes. The Mortgage Rescue Scheme, for example, has major weaknesses. It has been tinkered with and has problems with it. Lots of the other schemes are partial. We have a non-operational non-prime market. We have a mortgage market which is not fully funded or competitive at the moment. There are a lot of very difficult issues out there which certainly do need to be brought together. I think Government is beginning to see it in the round but it certainly does need to be seen in the round because there are some major issues.

Mr Leenders: A lot of that debate has been taken forward under the Homeowner Finance Forum. As an industry we feel that has been a very effective vehicle for the sorts of discussions that we are summarising in the conversation this morning.

Q181 Jim Cousins: Coming to that directly, clearly we have seen a considerable reduction in the number of mortgage offers at the high loan-to-value, high loan-to-income end of the spectrum. Should we be breathing a deep sigh of relief about that and saying, "We are not sending more people charging straight into Mervyn King's heavy artillery", or should we be saying that we need a different kind of offer that would keep the dream of mass home ownership alive?

Mr Leenders: I think that is the trick, it is how to outflank the artillery, to continue your analogy, because there will be those who a couple of years ago took a homeowner at say 80% LTV, say, who might find themselves slightly under water now looking to perhaps move for a job opportunity or what have you and is it right that we restrict that opportunity through the instrument that is LTV or do we need to

[1] *Note by Witness:* While we have not modelled this closely or published any figures recently, we estimate that approximately 1.2 million fixed rate mortgage loans will be maturing in 2009. The number of maturing deals is likely to trail off later this year, and this would suggest a figure of roughly 1.6 million for the 18 month period to mid-2010. And so, broadly consistent, I think, with the estimate attributed to *Which?*.

work through some of those scenarios. That is probably a lot of what the CML are discussing with the FSA just now.

Q182 Jim Cousins: So what is the answer?
Mr Leenders: The answer is that it would be very easy, would it not, to suggest that we could have a blanket LTV and that would provide a cushion of equity. However, we are where we are and for some people who took out mortgages a couple of years ago, to impose that now might be quite restrictive and have an unintended consequence, a negative consequence, both for those individuals and for the broader functioning of the housing market. We need to work that through before we land on a solution that might be simply, "Let's have a prescribed LTI and LTV", even though it has been applied in other countries.

Q183 Jim Cousins: If we had a prescribed LTI and LTV, large numbers of people who in the past would have been homeowners and at present maybe considering becoming homeowners will not be able to do it, in which case we will have to turn to Mr Socha and his members to provide the solution in terms of decent homes.
Mr Williams: But you can already see that in the rise of the under-30 year olds who are renting not owning. There has been a complete shift in the balance between owning and renting of households under age 30 and that process will continue. Clearly we do have a constrained mortgage market and in the future I think the lending industry view is that higher LTV mortgages will come back slowly but we have yet to put in place the regulatory responses both at the FSA and EU level in terms of what the controls might be. There is a general view, and the experience in other countries would suggest, that an imposed LTV limit is not effective, there are ways round it, and in other countries a more common solution is to use a mortgage indemnity guarantee—Canada would be an example—which allows higher LTV lending with the protection of an insurance programme. There is no appetite in this country to go there, both on the part of the industry who experienced problems in the past with those policies not actually paying out or Government who seem to have little appetite for it as well. There is a very rich debate about LTV and LTI cut-offs. Most of the industry has migrated to affordability calculations which are much richer and more complicated than that. Our view would be that product prescription would be damaging ultimately to innovation and the mortgage market and we would learn to regret it. Our general collective view across all the trade bodies, if I understand it rightly, would be LTV prescription would not be welcomed.

Q184 Mr Brady: In looking at either new lending or re-mortgaging, what assumptions are you making about house values?
Ms Bennett: I think it will be for individual lenders to take their own views about where they think house prices are going. It almost depends which index you look at as to what you think house prices are going to do. Each lender will take its own view about that. I suspect that is part of the reason why we are seeing very little high LTV lending at the moment.
Mr Leenders: For us, we would see some stability in parts of the market but I think there is regionality and different geographies seem to have suffered more with negative equity, and your constituency is one that was mentioned earlier. Also, the type of housing is quite significant insofar as perhaps the three-bed semi near to a good school has held value far better than the luxury two-bed executive apartment near to the railway station. There are moving parts which will continue to move. Overall, I think we do see there is some stability and as that stability continues then we will see an increase in LTVs as that spectre of negative equity starts to recede.
Mr Coles: Lenders do have to take account of the views of outside agencies, so Moody's for example, when they credit-rated building societies recently had a central forecast of minus 40% on house prices peak to trough, and they are down 20% so far, and a stressed environment, as they call it, of minus 60%. If you are a lender who has done a fair amount of higher LTV lending and then you are exposed to a credit rating agency saying, "What happens if house prices fall by 50%?", you will be embarrassed. It is not sensible business to get into from a credit-rating agency's point of view. If you are downgraded by the credit-rating agencies it will cost you more to raise funds in the wholesale market and you will have to put your mortgage rates up. It is the same with the FSA. The FSA on its stress testing is assuming a very severe reduction in house prices. If you have got too high a proportion of your lending in high loan-to-value ratio lending the FSA will take some pretty severe action against you. The regulatory and credit-rating agency incentives are to keep your loan-to-value ratios pretty low at the moment.
Mr Williams: The FSA is working on a 50% down stress test.
Mr Coles: Peak to trough.
Mr Williams: And obviously when you put alongside that high LTV lending attracts a higher capital charge there are major disincentives to do high LTV lending.
Mr Coles: You have got to be pretty brave to do a significant amount of LTV lending.
Mr Williams: I think what you will find is there are a number of products in the market, and it has picked up a little bit, but the volume of lending behind that is quite small. It is as much a symbolic gesture of the market rather than a mass return to high LTV lending.
Mr Coles: The price saving that was suggested by one of the earlier witnesses sounded very sensible, not at all outrageous for that 90% LTV given the very significant risks that you run taking that sort of lending both from the regulators, the credit-rating agencies and the market itself, of course.

Q185 Mr Brady: Can I ask you, Mr Leenders, are the banks less concerned than the building societies about those threats to credit-rating because it is a smaller part of their business?

Mr Leenders: I do not think they would be less concerned, they would have the same regard for the conditions in the marketplace generally. Of course, they are regulated in the same way by the Financial Services Authority. Perhaps where you have a smaller, less diverse suite of products the impact that a rating agency evaluation might have will be more significant than on a broadly based diversified bank, so perhaps that is a lesser consideration, but otherwise it would be wrong to surmise that the banks have less regard for those things.

Q186 Jim Cousins: Following up your reference to the stress testing exercise, Mr Coles. One building society, West Brom, has already come up with some fairly radical proposals. How long are you expecting this stress testing exercise on the building societies that are involved to take because this is clearly quite an unsettling business potentially?
Mr Coles: Yes. I think that is a question you would have to put to the FSA. They are doing the stress testing and my organisation is not involved in that, so you must ask them. I understand the stress testing in a number of societies is occurring now but I do not think it is a finite process and if the recession continues, if unemployment carries on rising and house prices keep falling, I dare say the FSA will see that as a continuous process rather than just a one-off. You really must ask them, I think, they would have much more detail than me.

Q187 Chairman: Jackie, you said in answer to a question that you do not have any projections of arrears and repossessions in 2010 or 2011.
Ms Bennett: No.

Q188 Chairman: Why not?
Ms Bennett: Because the environment is uncertain, the economic position is uncertain and we still do face a lack of mortgage finance, we believe all of those factors make it unrealistic to try and do a projection at this point.

Q189 Chairman: There are always variables in the economy and you are forever coming out with projections on this, that and the next thing. I am fed up reading in my national newspapers about projections on A, B, C, D and E, so why do you not join the band?
Ms Bennett: I think that is exactly why we do not want to join that bandwagon. If we do we are going to be putting a number into the public domain that we cannot have any confidence in.
Mr Williams: The shortfall in mortgage finance is utterly unprecedented. There were instances in the 1970s when HM Government lent building societies £500 million but the shortfall in overall mortgage supply has been dramatic and is continuing. Until some of those markets reopen it is very difficult, as Jackie is saying, to take it forward.

Q190 Chairman: So we will not see the CML make projections for 2010 or 2011, or 2012 or 2013?
Ms Bennett: We may do, but certainly not at this point.

Q191 Chairman: If we do get those projections then we will say, "These people really know what is going to happen in 2013", is that right?
Ms Bennett: That is very difficult to answer.
Chairman: Thank you very much for your time, it has been very helpful to us.

Tuesday 7 July 2009

Members present

Mr John McFall, in the Chair

Nick Ainger
Mr Graham Brady
Mr Colin Breed
Jim Cousins
Mr Michael Fallon
Ms Sally Keeble
John Mann
John Thurso
Mr Mark Todd
Mr Andrew Tyrie
Sir Peter Viggers

Witnesses: **Mr Jon Pain**, Managing Director, Retail Markets and **Ms Lesley Titcomb**, Sector Leader, Retail Intermediaries and Mortgages, Financial Services Authority, gave evidence.

Q192 Chairman: Good morning, welcome to this mortgage arrears and access to mortgage finance inquiry. Can you introduce yourselves for the shorthand writer, please?
Mr Pain: Certainly, Chairman. My name is Jon Pain, Managing Director of the Retail Markets at the FSA. I joined the FSA in September last year.
Ms Titcomb: My name is Lesley Titcomb, I am the Director of the Small Firms and Contact Division, and I have sectoral responsibility at the FSA for mortgages and for retail intermediaries.

Q193 Chairman: Welcome. *Which?*, in their submission to us highlighted the issue of securitisation and covenants which restrict the scope for the lender to exercise flexibility and forbearance towards households in mortgage arrears. What is the FSA doing to ensure that the securitisation business model does not inhibit lenders from offering support to homeowners in mortgage difficulties?
Mr Pain: Yes, Chairman, we are aware of that issue, and we are looking to address that as part of our mortgage market review that we are completing later this year. It is worth pointing out to the Committee that in a lot of cases the third-party administrators look after the mortgage administration of those accounts on behalf of some of those firms, and they are bound by our rules in respect of the Mortgage Code and treatment of customers in arrears.

Q194 Chairman: You also released a statement recently which stated: "We do not expect to see future securitisations that contain provisions that could potentially lead to the less fair treatment of borrowers, for example, by restricting or preventing the use of any commonly available arrears tool where it would achieve the right outcome for customers." What are you doing to ensure that happens?
Mr Pain: As I say, Chairman, that will be the issue that we address as part of the mortgage review.

Q195 Chairman: What is the timescale for that?
Mr Pain: We have been out to industry and are engaged with industry now; we are planning to issue a discussion paper in the autumn and then, subject to the feedback on that discussion paper, we will be issuing a consultation paper in the first quarter of next year.

Q196 Chairman: So the consultation paper—probably over a year before it ends.
Mr Pain: No, I hope not, Chairman, because there are some big issues to address in that context. We would expect the consultation paper would be, probably, three months, so I would hope that by the first half of next year we would start to make some changes that we need to address on mortgages.

Q197 Chairman: So a year from now?
Mr Pain: A year from now, Chairman, yes.

Q198 John Thurso: What is your current estimate of the number of households in mortgage arrears, at the moment, and what level of increase do you expect over the next 12 to 18 months?
Mr Pain: Mr Thurso, you are probably aware that we produce a quarterly report on the mortgage data we obtain from firms, and the last quarterly report actually shows that the total number of mortgage arrears (our report talks about numbers of accounts as opposed to individuals) was just below 400,000—399,000. That represents about 3.6% of the total number of mortgage accounts in existence today; the other side of that, of course, is that about 96% of mortgage accounts are performing in line with their mortgage account plans and repayment schedules. What we have seen, though, over the last 12 months, is that that level of outstanding arrears cases has been increasing, so that number is up about a third from this time last year.

Q199 John Thurso: You would expect that to continue for the next 12 to 18 months as the level of increase?
Mr Pain: There are, obviously, a number of economic factors that impact on the mortgage market and on consumers' arrears. Clearly, some of those trends and issues—unemployment and so on—have yet to play out, so we would expect that to actually still have an impact that needs to be worked through in respect of those numbers of mortgage arrears, yes.

Q200 John Thurso: Why has the gap between possession orders and actual possessions widened in recent years?

Mr Pain: I will comment and, by all means, let Lesley add to that. Of course, the one thing to remember in terms of the relationship between arrears cases, first and foremost, and repossessions is that not all arrears cases actually migrate to being repossession cases. The relationship is somewhere in the order of about one-in-eight of arrears cases.

Q201 John Thurso: This is the difference between actual possession orders granted and actual possessions taking place; the gap has widened quite significantly. Is it a coincidence that that divergence coincides with the introduction of the Mortgage Conduct of Business rules, for example?
Ms Titcomb: To be frank, I do not think we have done analysis that demonstrates that. There are a number of reasons why people do go and seek repossession orders and they do not necessarily progress through. It could be that the issue gets resolved before the actual possession takes place, but we have not done any specific analysis on that point.

Q202 John Thurso: It would be interesting if you do some analysis because, obviously, having a repossession order against you is a pretty hairy thing for somebody to go through, and if it is never going to be executed then it is a lot of grief for not a lot of attainment, at the end.
Ms Titcomb: This is why we emphasise that people should only move to repossession as a last resort and that, wherever possible, they should find another means of resolving the problem between them and the borrower.

Q203 John Thurso: In your written evidence it is stated that mortgage arrears and repossession levels are likely to reach similar levels as those in the early 1990s. Why do you think the cycle will repeat, as it did then, given there are very significant differences in the monetary policy environment?
Mr Pain: There are a number of different factors, if you compare the 1990s to today, so, obviously, the issue in terms of unemployment levels had a big bearing in respect of arrears and repossessions. The issue in terms of interest rates prevailing at that time—you will recall interest rates at that time were 14-15% compared to the relatively low levels now—but the shape of the mortgage market has changed quite dramatically as well, so you have a bigger segment of specialised lending; you have a bigger segment of the buy-to-let mortgage market. Those markets were not at that level in any significant way in terms of the 1990s, and they will have a bearing in terms of how the mortgage market—

Q204 John Thurso: That is an argument for the cycle not repeating itself; your evidence said it would repeat itself.
Mr Pain: Buy-to-let, for instance, has never been through a recessionary climate, in that respect, so the impact that has on arrears and repossessions might well be different. It is very difficult to have a straightforward apples-and-apples comparison between now and the 1990s because, quite frankly, the mortgage market is different and the economic prevailing circumstances are different as well.

Q205 Mr Fallon: You said the number of arrears would increase beyond the 400,000. What is the peak you forecast?
Mr Pain: Mr Fallon, we do not actually make a forecast as such; we obviously do, through our financial risk outlook, give some idea in terms of what the consensus of other forecasters are predicting in that respect. The CML, you might recall, from evidence to you last week, said the numbers might rise to 500,000 in total.

Q206 Sir Peter Viggers: Your Conduct of Business rules were introduced in 2003, which was a much more benign period. How are they standing up to the present climate?
Mr Pain: They were actually introduced at the end of 2004 so they really became effective in 2005. We spent the first year or 18 months of the new mortgage regime (which, if you recall, replaced a voluntary code—so this was then both principle and specific rules addressing all aspects of the mortgage market) carrying out a series of investigations into the mortgage market to make sure our regime had bedded down properly and that lenders were adhering to our practices and our requirements. That ranged from responsible lending through to mortgage advice, the financial promotions of mortgages and the disclosure regime. In respect of arrears, per se, which is obviously the focus of this Committee today, we carried out two phases of work looking at the arrears issues in the mortgage market and the adherence to MCOB rules in respect of arrears. Phase One, which looked across the marketplace as a whole showed that, in the main, mainstream mortgage lenders were adhering to our arrears policy and the treatment of customers in arrears. There were some specific issues in terms of specialised lenders, and that became the focus of our work in Phase Two, when we looked at that part of the marketplace in some detail.

Q207 Sir Peter Viggers: What additional work are you doing in that specific area—sub-prime or specific mortgages?
Ms Titcomb: We have just completed our second phase of work in terms of the mortgage arrears practices, focusing specifically on specialist lenders and the third-party administrators that they use. We are following up on a number of things. Every firm that we saw we are discussing remedial action with, where that is appropriate. Four of the firms have been referred for enforcement investigation with a view to possible sanctions, and so on. We are also, then, feeding a number of the lessons that we have learned from that into our mortgage market review. This started off originally as a traditional, post-implementation review of the Mortgage Conduct of Business rules but has now been increased in scope to cover the whole of the regulatory arena around mortgages because we feel it is very important to look at how the tools work in combination with each

other, and we are very conscious that we can change something, for example, on the Conduct of Business side and it could have an effect on, say, access to the market, or whatever. So we have to look at the combination of all the tools available to us—prudential conduct of business, approved persons and Gateway-type regimes—and that is what the mortgage market review is covering, so it now goes wider than Conduct of Business.

Q208 Sir Peter Viggers: When you carry out a special study and you name four or five companies, do you publish their names?
Mr Pain: As part of that, if we refer them to enforcement action we wait for the enforcement action to conclude. It is our usual practice that, once we have concluded that, we do publish the outcome of those enforcement cases if it has actually resulted in us fining the firm and finding them in breach of the issues. That we do make public.

Q209 Nick Ainger: Coming back to the Conduct of Business rules, in terms of arrears, it says in those rules: ". . . a charge for arrears on a customer except where that charge is a reasonable estimate of the cost of the additional administration . . ."—so no charges that are unreasonable, basically. Could you explain why there is such a variation in the so-called administration charges between different mortgage lenders for those people that are in arrears?
Mr Pain: You are quite right. (I will make a first comment and then let Lesley add some of the detail.) Our rules are fairly specific about this particular issue; there can only be a recovery of the costs borne by the firm; they are not designed to allow the firm to generate a profit from handling arrears cases. One of the issues that is worth bearing in mind, one of the important aspects of arrears management, is you do treat the customers as individuals. Therefore, we do not want a highly automated process; you do want the case management of individual circumstances to be part of that process, so that the consumer is understood in terms of their financial position and treated accordingly. Of course, our rules allow, then, for some charges to recover some of those costs and the handling of an arrears case, but we do expect it to be proportionate to the costs involved. Lesley referred earlier on to some of the work we have done with the specialist mortgage market. We have found in some instances there those charges were inappropriate and were excessive, and that has formed part of our enforcement action with those firms.

Q210 Nick Ainger: We have had a large amount of evidence complaining about these high charges—again, claiming that they are to cover administrative costs. We have got complaints about GMAC and Kensington charging a standard £50 a month if you are in arrears, and we have other evidence of going up as high as £60 and £70 a month. When you hear these instances, what is the FSA doing? Clearly, these are covering a hell of a lot more than administration costs, are they not, at those sorts of rates per month?
Mr Pain: As I have already referred, we have, when we looked at the specialist mortgage market, taken enforcement action against a number of firms (four or five firms) with several under review as well. Some of those enforcement cases relate to those charges that you have referred to. So where it is brought to our attention that there are issues in those charges we do take action.

Q211 Nick Ainger: Do you wait for a complaint to come in and then take action, or are you monitoring the charges that are being made by mortgage lenders?
Ms Titcomb: All our Conduct of Business rules, including this one, are part of our ongoing supervisory approach with firms. Our supervisors, who go out and have the relationship with these firms, will be looking at a range of things that those firms engage in, in terms of whether or not they are treating their customers fairly, and this would form part of that work. Obviously, if they found particularly egregious examples during that work we would expect them to follow up. In addition, we then do the thematic type of work that we have talked about here today, and, as Jon has said, that has picked up a number of issues with charges—not only, I may say, about absolute amounts but, also, in particular, about the way charges are applied in some cases; for example, repeat presentation of direct debits—that kind of thing—or charging regular arrangement fees even when an arrangement has been come to between the lender and the borrower. We are following up on a number of those. The whole area of arrears charges is one that, again, we will be examining within our mortgage market review to see whether the rules need amending.

Q212 Nick Ainger: I was going to say, as there seems to be almost a systemic breach on a regular basis by a number of mortgage lenders of these rules, is it not time that you actually issued very clear guidance about what can and cannot be charged in terms of these arrears charges?
Ms Titcomb: We have already, first of all, emphasised what our rules say to people; we publish examples of good and poor practice already, and we will continue to emphasise those. We will continue to pursue it through the regular supervision and we will then do the policy work to look at whether we should change the framework. So we feel we have covered all the angles.

Q213 John Mann: What are you doing about the buy-and-let-back market?
Mr Pain: The sale-and-rent-back market? Yes, as you will probably recall, there was an OFT inquiry into that marketplace at the end of last year. In October last year the OFT recommended that the FSA should take over regulation of that marketplace, and the necessary indication of that was passed by Government—Treasury—by the spring of this year. So, in July, we have issued an interim framework to take over regulation of that marketplace, with a full regime of regulating that marketplace taking effect from June next year.

Q214 John Mann: Will that be retrospective in looking at problems?
Mr Pain: We cannot, obviously, make our regulations retrospective in that sense, but what I think we will see is, even with the interim arrangements, we expect a particularly hard shake-out of firms in that marketplace, and so a lot of firms, we are expecting, will not apply for authorisation by the FSA as a consequence of that interim regime.

Q215 John Mann: What about the scam of doorstep lending in order to persuade people to buy council houses followed up by second, and even third, secured and unsecured loans all linked to the same lender? What evidence is there of that going on?
Mr Pain: I am not aware of any particular instances of the doorstep lending you have referred to, in that sense, Mr Mann, but, of course, you will be aware that we only regulate first-charge mortgages in the mortgage market; we are not responsible for regulating second-charge mortgage lending. Neither are we responsible, at this moment in time, for regulating buy-to-let mortgages.

Q216 John Mann: But that has to be part of your investigation if you are investigating these four companies. If those practices are going on that has to be part of it.
Mr Pain: Certainly, the regulatory regime, in terms of when that comes into effect, will, obviously, set rules and regulations in terms of how that process should—

Q217 John Mann: You are already regulating it. Let me give you an example: when I complained to you in detail about Kensington Mortgages 18 months ago, why have I heard nothing back?
Mr Pain: I have got to be honest, Mr Mann, I am not aware of that. I am happy to have a look at that.

Q218 John Mann: It is a fairly fundamental issue. You are provided with a lot of detailed information on a specific complaint, I meet yourselves. If that was the Law Society and it was a complaint about a solicitor there is a set process in place that is open and above board, I am kept informed and my constituents are kept informed and that is either resolved or it is not resolved. If it is not resolved there is an ability to challenge that to an Ombudsman. With yourselves it disappears into the ether, does it not?
Mr Pain: I do not entirely accept that, Mr Mann. I treat any complaints that we get, whether it be from yourselves or from other trade bodies or anybody else, very seriously and we investigate those issues and try and respond in a very fulsome manner. If we have not, in this particular instance, then I apologise for that fact, but that is not our usual process; we do look and treat all complaints that we get about firms that we regulate very seriously.

Q219 John Mann: No, you do not. I meet your senior officials, I provide a full dossier, with individual complaints of a major, serious nature but, also, suggesting to you that this is a major problem in the market, not just an aberrance in a particular case, citing other examples, bringing in doorstep lending, bringing in second-charges and then up to third unsecured loans, suggesting that the same agency linkage is there, and your rules are being bypassed by people using a set of agents. It is a major issue to investigate. It may be that there are perfectly reasonable answers for all of that. But then we find others complaining about the same company. You have not got back to me. Why not?
Ms Titcomb: Mr Mann, as you know, first of all, if a consumer with a particular company has an issue they can take it up with the firm itself and, if they are not satisfied, with the Ombudsman. Secondly, we do not, as a matter of course, comment on whether or not we are investigating a particular firm. We recognise that that makes it extremely difficult for us to keep people like yourself and individual consumers updated as to what is happening, but we do take the information that is provided to us very seriously. Thirdly, I would say, again, our remit only extends to first-charge mortgages so, whether we like it or not, we cannot take action against people around types of lending which are outside our remit. It is just not within our power to do so.

Q220 Chairman: Mr Pain, why do you not have a meeting with Mr Mann?
Mr Pain: Indeed, Chairman.

Q221 John Mann: Finally, should your remit be extended to go beyond first mortgages?
Mr Pain: As we have alluded to, we have already been given the remit to extend that into the sale-and-rent-back arena, and as part of the mortgage review we will look at that and the case for extending that to the buy-to-let and second-charge market. That is, obviously, a matter for Treasury.

Q222 Chairman: Let us discuss it at the meeting. I have got you a meeting. You have taken out enforcement action against four firms. Is that correct?
Mr Pain: Four firms are in the process of enforcement action in respect of the specialised lending we have referred to, Chairman, yes.

Q223 Chairman: Can you tell us how many homes these four lenders you have just referred for enforcement are repossessing every month?
Mr Pain: No, I am afraid I do not have those details. That process and that management of arrears will form part of that enforcement.

Q224 Chairman: Are you likely to refer more lenders for enforcement?
Ms Titcomb: It is possible that we are considering a number of other firms for referral to enforcement.

Q225 Chairman: Why have you not named the four firms which you have referred for enforcement action for failing to treat customers fairly?

Mr Pain: As I have already tried to allude to, Chairman, it is our usual practice, once the enforcement process is complete and we have found there is a case for taking action—

Q226 Chairman: The reason I am asking that, Mr Pain, is that whilst these have been referred to enforcement they could be treating quite a number of customers unfairly at the moment.
Mr Pain: As part of that enforcement action, obviously, we are taking a very close look in terms of their treatment of customers as part of our supervision activities on a daily basis.

Q227 Chairman: What you have stated to us in your evidence is that: "Disclosure to the public of the names of the firms with whom we had discussions . . . would be likely to undermine theirs and other firms' willingness to engage in a dialogue with us and to provide us with information." That goes completely against Hector Sants' proposition that these firms should be scared of the FSA. This seems pretty mealy-mouthed. They will not engage in dialogue with you if you name them? You are in charge, not them.
Mr Pain: Indeed, Chairman. Our enforcement action is very decisive and we will take that action through to its conclusion. Quite frankly, until the full enforcement process is complete, it would be unjust to say they are guilty before they are proven guilty.

Q228 Chairman: How long will it take for it to be complete?
Mr Pain: Enforcement cases depend, in terms of their level of complexity, but three to six months is a normal part of that process.
Ms Titcomb: We may get to it earlier than that if they choose to settle with us.

Q229 Chairman: Meanwhile, they could be treating customers unfairly.
Mr Pain: Obviously, having got them into enforcement, we are taking a very close interest in our supervision of their activities.
Mr Fallon: How do the customers know?

Q230 Chairman: Exactly. How do the customers know, as Mr Fallon says?
Mr Pain: Those customers are already with those firms. It is our role then to make sure they are treated carefully.

Q231 Chairman: Exactly. They are in ignorance of what is happening. This is the thing: you have a bias towards the industry here, in the sense of giving them the benefit of the doubt, but the customer does not get the benefit of the doubt. We are looking for you to change that attitude.
Ms Titcomb: Can I emphasise that just because somebody has moved into being referred to enforcement action does not mean we stop making them try and make it better in the short term. Indeed, their co-operation with us and their desire to put it right is an important factor in determining what sanction they get.

Chairman: Lesley, you have not convinced any of us here.

Q232 Mr Tyrie: Could I just ask a couple of follow-up questions to that? The question here is what happens to new customers who join businesses during the period in which you may have some reason to suppose that there is something amiss? What protection do they get? You have said, Mr Pain, that you monitor carefully the way they are treated. Have you taken advice on whether failure to protect those customers adequately might constitute maladministration for the purposes of the work of the Financial Ombudsman?
Mr Pain: Those customers, if they are still active in the mortgage market, because some of those lenders might not be active in mortgage markets (so this might be a "closed book", so to speak, in terms of those cases), that are moving as part of that would be protected by our Mortgage Conduct regime, but you would also hope that those new customers are not going to go immediately into arrears, but if they were to go into arrears in the future then they would be subject to the same safeguards that we put in place by our regime and framework.

Q233 Mr Tyrie: The point I am trying to get at is: is it the pressure that may come from referrals to the Financial Ombudsman for cases of administration the main pressure leading you to decide where the balance should be struck between treating firms fairly and treating customers fairly?
Mr Pain: I am very conscious (and the Chairman has made it very clear, in terms of the Committee's views), in terms of them taking decisive action, but I would point out we fined a record number of firms last year in terms of our enforcement activity. That was up from £4 million to £28 million. We have set out today, and it is recorded in the press today, a very clear regime of toughening up our enforcement fines and the likely—

Q234 Mr Tyrie: Can I ask this question about the Financial Ombudsman's role?
Ms Titcomb: We, obviously, use information, in terms of what we see at the Ombudsman, to inform our decision making, both on policy terms and we are particularly interested if it shows issues with a particular firm, but it is only a small factor that we take into account.

Q235 Mr Tyrie: Looking at it from the point of view of treating firms fairly and customers fairly, you are exempt from being sued for gross negligence, in law, are you not, but you are not exempt from being sued for acting in bad faith? Do you think it is possible that putting out information into the public domain which could seriously damage a firm and, therefore, the value of that firm to shareholders, could, in certain circumstances, constitute bad faith—something going beyond gross negligence or recklessness?
Mr Pain: We, obviously, very carefully balance those issues out, Mr Tyrie, but we are very clear: if we have taken enforcement action against a firm and that has

resulted in us fining the firm for breaches of our rules, we think that is quite rightly a matter that should be made public. That is the process we have adopted. In the case of firms being fined, that is part of our publication process after the event has been concluded.

Q236 Mr Tyrie: I am asking a different question, again. I am sorry I have to ask the same questions twice. The question I am asking is: what is the legal constraint on your acting on firms? Is it the fact that eventually there is a level of behaviour by you on which the firm themselves could take action?
Ms Titcomb: I am not an expert on the immunity provisions which cover the FSA. We tend to think about it in terms of—

Q237 Mr Tyrie: That is, in itself, significant, if I may say so. It means that you do not feel constrained by that.
Ms Titcomb: Indeed. What we are looking at is how we can secure the best outcome for consumers in this, but, equally well, balancing it, as you might put it, with natural justice to the firm. So we have to balance the process between the desired outcome, and that is why we come to the view we do that it is not wise for us to disclose the names of firms that we are investigating.

Q238 Chairman: That is good because I get the feeling from your answers that there is work in progress here. If you can work on that then I think we can achieve a situation where firms are named—they are not shamed, they are named—where there is going to be an investigation, so that people understand that that process is going on. It is good for the FSA, it is good for consumers. In fact, it is good for the industry as well. So if you look at that and write back to me on that, we will engage in this dialogue.
Mr Pain: Certainly, Chairman.

Q239 Mr Breed: Following on slightly from that, are you taking any sort of action with the OFT in respect of excessive charges and all those sorts of things? What involvement do you have, what action do you take, with OFT?
Mr Pain: Obviously, the OFT's remit is, largely, in the second-charge marketplace. That is a separate regulatory regime. We work very closely with the OFT in terms of a number of issues where they overlap, so the whole question of affordability and the whole question of responsible lending. We have regular dialogue with them in terms of how we address those issues, but that particular regime, in terms of the second-charge mortgage market, is part of their remit.

Q240 Mr Breed: Those rules do not impinge on your efforts, and you can assist them in actions that they may want to take as well, presumably?
Mr Pain: We have never found it necessary to directly get involved in action the OFT is taking in respect of second-charge lending, but, as I say, we do have a close and effective working relationship with the OFT.

Q241 Mr Breed: There are two separate issues here, in this whole area. There are those excessive charges and arrears, and everything else—admin charges, penalty charges—which have already been charged and then—willingly or unwillingly—have been paid by consumers, so they feel they have been unfairly dealt with. Then there is the ongoing work, and we know that is because they are trying to build their profitability from very low current interest rates and everything else, by adding those. Can you tell us what actions separately you are taking in respect of those arrears, if you like—those ones that have already been charged where consumers come to us (and they come to all of us, I suspect) and we really want some action there—and what are you doing to prevent the same thing from happening with the new facilities, where yes, there is a bit of lending taking place but it is really at amazingly high rates and charges and everything else?
Ms Titcomb: You mean in terms of the cost of that lending?

Q242 Mr Breed: Somebody will say: "Yes, I can get a mortgage", but, quite frankly, the costs related to the arrangement fee, the administrative charges, the charge for looking at the property—it just goes on and on. They are all very happy, of course, to add it to the advance, but it is a very expensive piece of borrowing.
Ms Titcomb: As you know, we are not a price regulator in ourselves. What we are looking at as part of the mortgage market review, for example, is the area around disclosure to consumers. As I have previously said, in terms of things like arrears charges—that type of thing—we will be looking at our Conduct of Business rules in relation to those, again, as part of the mortgage market review to see whether we need to change those in any way.

Q243 Mr Breed: If you then decide that, yes, they have been there, will you ensure that those excessive charges—whether consumers have complained or not—are actually refunded?
Ms Titcomb: Individual consumers, for example, can go to the Financial Ombudsman if they are not satisfied with the answer they get from the firm. So they have that safety net. If you look at the Ombudsman's annual report, they have actually reported that they have been dealing with a number of cases like that and have secured restitution. Equally well, as well as announcing yesterday about the importance of increasing fines on firms who misbehave, we have also emphasised the importance of them providing restitution to customers where that is necessary.

Q244 Mr Breed: So, if the practice of charging a particular fee or charge, whatever it is, has been complained about by 20, 30, 50 consumers and it is

then found that that is excessive, it is inappropriate, do you ensure that the firm then repays all of that to all of the borrowers that have been caught under that particular charge?
Ms Titcomb: Restitution is a very important part of any enforcement action that we take.

Q245 Mr Breed: Even if they have not complained?
Ms Titcomb: Usually. It varies in extent and how we do it, but we always look at that particular issue about redress and restitution, yes.
Mr Pain: One of the most significant things, and it is a very important point, in terms of taking enforcement action is not the fine per se, but it is the cost of restitution for them putting right all those consumers and that is a cost that is not always visible, but is extremely costly to firms that say that—
Mr Breed: And you ensure that that is done.

Q246 Mr Brady: You said that you are reluctant to make it publicly available if you are taking action against firms or have concerns about firms. What information though do you share with the courts if repossession action is being taken?
Ms Titcomb: Well, as you know and I think probably this Committee may be aware, there is now a pre-action protocol in place. What we found, and we were informed, for example, in discussions with the Ministry of Justice, was that the courts did not well understand the FSA Rules and their status and all the rest of it, so we worked with them to turn it into a pre-action protocol which is something the courts recognise and they are familiar with. It reflects the vast bulk of our Conduct of Business Rules so that effectively a lender has to demonstrate to the court, if they wish to secure a repossession order, that they have followed the Conduct of Business Rules and have made every effort, for example, to come to an agreement with them.

Q247 Mr Brady: So, even though you do not tell the court that you have concerns or are taking enforcement action, it should be readily apparent to the court that the firm is in default of those requirements?
Ms Titcomb: Precisely, yes.

Q248 Mr Brady: Since that has been the case, have you seen any evidence of a change in behaviour of the courts, a change in the outcomes?
Ms Titcomb: Well, we have seen that there is a decrease in the level at which the rate of repossessions is increasing. We cannot yet attribute that causally to the pre-action protocol. It has only been in effect since the end of last year, so an awful lot of the cases that are going through the courts at the moment would have been started before the pre-action protocol came in, so we cannot attribute that slowing down in the rate of increase to the pre-action protocol yet.

Q249 Mr Brady: How soon would you hope to be able to identify whether that is a causal effect?
Ms Titcomb: Well, the general time-lag between an arrears and someone becoming a repossession would be 12 months or so, so it would probably be at least a year, and of course there are many other factors in play as well, such as the general plea for forbearance on the part of lenders.

Q250 Mr Brady: But you are confident that the courts effectively, albeit through a different route, have all of the information they need about the conduct of lenders now?
Ms Titcomb: Thus far, we have had positive feedback that the pre-action protocol has certainly helped, yes.

Q251 Mr Todd: Would it be better if the FSA published its own analysis of the sorts of charges and practices that lenders were involved in in this marketplace and made those available to the court process so that they can make their own judgments on what is an appropriate process that has been followed prior to seeking repossession?
Ms Titcomb: My understanding is that the issues in the courts rarely centre around charges, and I think it would be fair to say that consumers who have issues with charges would be better placed going to the Financial Ombudsman if they have an issue.

Q252 Mr Todd: English law relies a huge amount on the test of reasonableness, reasonable actions by a lender to work with a borrower prior to repossession. I would have thought, but perhaps you are more expert on these matters than I, that one of the tests of reasonableness would be to show the sorts of behaviour and charging regimes on a comparative basis that various companies were involved in so that, where a company appeared before a bench seeking repossession, the bench had some information on which it could base a judgment as to reasonableness.
Mr Pain: I take the sense of it and I understand the point you are making, but I think it probably would be difficult to say that you can compare on a like-for-like basis all lenders, in terms of their costs, for reasonableness. What the court process does have and what our protocol and Arrears Rules actually do spell out is a very clear transparency of what those charges are and how the consumer should be informed about what their rights are, and that obviously is part of the protocol arrangements that Lesley has referred to. The courts are very well aware of that fact. They do not have, I agree with you, the explicit comparisons of one charging tariff compared to another.

Q253 Mr Todd: Well, would that not be a valuable supplement and, following the Chairman's helpful suggestion that you might be considering some movement on the enforcement process, one mechanism of movement might be transparency from an FSA perspective as to the comparative performance of various companies in some detail? If you feel that natural justice is not being served by open disclosure that a company may be in enforcement, it might be helpful to have the wider

public having more available some of the core data which would suggest that enforcement might be taking place because of substantial variances in that company's practice from the norm within the industry.
Mr Pain: Yes, I understand the point.

Q254 Mr Todd: Do you understand where I am going?
Mr Pain: Indeed, and I suppose I would say that much of the issue that the court is actually dealing with at that time is whether or not they will allow the repossession to take place, not the absolute level of charges. I think it is probably our responsibility to make sure that those charges are appropriate and, if they are in breach, that we take specific action against that firm itself.

Q255 Mr Todd: I am perhaps being too subtle for you—
Mr Pain: You might be.

Q256 Mr Todd:—because what I am suggesting is that this might be a rational basis for giving more information about your marketplace which would have a useful adjunct to a court a process because certainly, I think, you would be wrong to suggest that the whole process of the reasonableness of the lender is irrelevant to the court, I do not think that that is at all the case—
Ms Titcomb: Absolutely not.

Q257 Mr Todd:—and this would be a useful context for assessing the reasonableness of that lender's behaviour.
Mr Pain: I think it is a very helpful suggestion. Can I take it away and then reflect in terms of how we might make that work in practice?

Q258 Mr Todd: This would be perhaps a little bit of a departure from the rather more principles-based approach which the FSA has attempted to use in this area, something which links actions to evidence that is in the marketplace and suggests that variances from the norm are something which requires further explanation and at least places the customer in a stronger position to make some judgments and, as I have suggested, the court as well.
Mr Pain: Indeed, and I have acknowledged that.

Q259 Jim Cousins: The specialist lenders have to raise money in the markets and they do not take deposits. Are we now in the business of trying to clean them up so that they continue to play a role in supporting the dream of owner occupation in perhaps riskier areas, or should we simply be thinking of winding them up and closing them down?
Mr Pain: Well, I think you touch on some very important issues in that sense, Mr Cousins, and that is one of the issues that our Mortgage Review is looking to address. You are probably well aware now that specialised lending in the mortgage market today has reduced dramatically to being almost non-existent.

Q260 Jim Cousins: Well, it must be close to zero.
Mr Pain: Yes, non-existent levels, so there are two fundamental questions to address there. One is the mechanism for those lenders raising funds, wholesale funding, to actually participate in the mortgage market, and the second issue to address as part of our Mortgage Review is how we want to see the shape of the mortgage market emerge and give some greater protection to some of those consumers who do require and are in need of specialised mortgage lending, whether that be credit-impaired history lending or particular types of mortgages, so that is one of the central issues of our Mortgage Market Review, to think about how that mortgage market will be shaped in the future as opposed to just allowing it to emerge as it did in the past, but the funding question is central to that.

Q261 Jim Cousins: But there are some very fundamental choices to be made here. Do we think, going forward, that there is a role for these specialist lenders at all, or should we be thinking about winding them up as fast as we can and rescuing the people whom they have been seeking to serve as best we can?
Mr Pain: Yes, I think it is worth bearing in mind that, when I referred back to the Chairman in terms of some of my earlier comments about the overall arrears level in the mortgage market, clearly the arrears level in specialist lending is higher than it is, and you would probably expect that, in the mainstream mortgage market, but it is in the region of 10% or so, which does mean then that 90% of those mortgage customers that have been provided specialist mortgages actually have had access to the mortgage market and are now still sustaining their mortgage account, so I think we have to think very carefully about just eliminating that part of the mortgage market, otherwise you will close off opportunity for consumers to have access to the mortgage market. I think the key for us is affordability, so what we want to see is a sustainable mortgage market where there is clear affordability proven for the consumer on taking that mortgage commitment, and that is the essence and one of the key cornerstones of our Mortgage Review.

Q262 Jim Cousins: Mr Pain, it is all very well to talk about affordability, but incomes at the moment are not rising, a lot of them are not secure and they are not necessarily knowingly insecure well in advance, so how do specialist lenders who do not have access to deposits and all the support that goes with deposit-takers, how do they operate in such a situation?
Mr Pain: Well, as we have already alluded to, Mr Cousins, at this moment in time they are not particularly active in the mortgage market, full stop, because of the issues that you have just raised. I think the issue I am pointing towards is—

Q263 Jim Cousins: Affordability is a cop-out. Do you want this sector to survive or not?

Mr Pain: I am sorry, I disagree, I do not think affordability is a cop-out. I think what is important is that, when consumers enter the mortgage market, they do so with the full knowledge that they can sustain that mortgage over the lifetime of that mortgage. Now, we will, and, you are quite right, there are areas of the mortgage market that our Mortgage Market Review will, decide whether they have worked in the best interests of consumers, but I think it would be wrong to say that the mortgage market en masse, even in some of those areas, has not actually opened up the accessibility of owning your own home to a large number of mortgage customers. There are 12 million mortgage customers in the UK today and a good proportion of those customers would not have had access to the mortgage market if it were not for the opportunities of some of those lenders, and that is not to say that all those lenders have ended up doing a disservice to consumers. Where they have, then we will take decisive enforcement action against those particular lenders, but I think affordability is a key part of the mortgage market and that is one of the issues we want to address, going forward.

Q264 Jim Cousins: On affordability then, what loan to income or loan to value ratios do you recommend?
Mr Pain: One of the issues we will look at in the mortgage market is whether the loan to income ratios or the loan to value ratios are appropriate caps or collars in respect of the mortgage market. I have to say, I think genuine affordability is down to the individual, not at a superficial level of income against the mortgage commitment, but genuine affordability, and what level of disposable income do you have in that particular household to support the mortgage payment is really the key test and there are lots of mortgage players out there at the moment who have very sophisticated tools to assess genuine affordability and even the ability to withstand interest rate changes, going forward. That is what we need to get the whole of the mortgage market adopting as opposed to necessarily a simple income multiple; that is not a true test of affordability.
Ms Titcomb: We are also concerned that using a very blunt tool like, for example, a cap on loan to value could have the effect of denying first-time buyers access to the market, which would be unfortunate.

Q265 Jim Cousins: Yes, but what does the FSA want here in a more fundamental sense? Do we want low exposures by banks and specialist lenders, do we want them to be taking low risks, or do we want them to be keeping the dream of mass owner occupation alive? Which of those things do we want them to do?
Mr Pain: Quite frankly, Mr Cousins, I think it is a judicious mix of all those things. We want a mortgage market that works well for consumers, protects them against some risks in respect of what clearly has been an overheated mortgage market in the past, but at the same time does give choice and sustainability in terms of the mortgage market. We do not set housing policy or tenure policy, that is not our role, but what we do want to see is the mortgage market working well for consumers and sustainable, which is the big issue as well, the sustainability of that mortgage market, and having access for the right consumers properly protected with the right level of affordability so that they understand what they are taking on.

Q266 Chairman: You have mentioned the Mortgage Market Review. When is that going to be completed?
Ms Titcomb: We are due to publish a discussion paper on that in the autumn, the end of September/beginning of October, and we then envisage a discussion period of about three to four months when we engage with all the various stakeholders.
Chairman: Well, we are interested in that, so we will probably have you back at the end of that. Also, on the enforcement issue and publication, if you can keep that dialogue up with me on that, I think it would be very helpful. Thanks very much for your time and no doubt we will see you again, though maybe not before the autumn. Thanks very much.

Witnesses: **Lord Myners CBE**, Financial Services Secretary, HM Treasury and **Rt Hon John Healey MP**, Minister for Housing, Department for Communities and Local Government, gave evidence.

Q267 Chairman: Ministers, welcome to this inquiry into mortgage arrears and access to mortgage finance. Lord Myners, Which?, in their submission, highlighted the issue of securitisation covenants which restrict the scope for the lender to exercise flexibility and forbearance towards households in mortgage arrears. Is this issue on the Government's radar and are you proposing to take action to ensure that the securitisation business model does not inhibit lenders from offering support to homeowners in mortgage difficulties?
Lord Myners: Thank you, Chairman. There are a number of issues around securitisation which need to be addressed. This market at the moment is almost non-existent. We wish to see it come back into practice in a responsible way and the White Paper, which we are announcing tomorrow, on the future of financial markets will say more about regulation, and I am joining you again tomorrow to comment on that White Paper announcement to answer your questions.

Q268 Chairman: I watched *Newsnight* and I have got quite a feel for what is going to happen!
Lord Myners: The FSA has been very clear that in future the securitisation process and documentation should not in any way inhibit the ability of the lender or the lender's agents to enter into negotiations with borrowers to help them cope with distress in terms of servicing their obligations. In practice, even when there is a documentary restriction, there are waiver

processes, and I believe it is appropriate for the agent, on behalf of the securitisation vehicle, to persuade the lenders, the funders of those schemes, that it is in their interests to support borrowers and that to not do so is actually probably to put the market under more pressure which has consequential collateral negative outcomes for them. Therefore, I believe, Chairman, that there has been an issue in the previous form of securitisation documentation and I believe that that could be addressed by constructive engagement, but the FSA is very clear that in future it will not accept forms of securitisation documents which do not allow appropriate forbearance engagement.

Q269 Mr Fallon: Lord Myners, could you persuade us that the Treasury is taking mortgage arrears seriously when the Council of Mortgage Lenders are now forecasting perhaps 500,000 people in arrears and perhaps 65,000 repossessions, yet you have the Mortgage Rescue Scheme for only 6,000 people, which seems somewhat lackadaisical.
Lord Myners: Well, I think, Mr Fallon, the most constructive approach that we can take to dealing with this issue is in the area of macroeconomic management. It is through ensuring through fiscal policy that there is demand in the economy which supports employment and an accommodating monetary stance, and certainly one of the things which is clearly different this time in this mortgage cycle from previous ones is that we have much lower interest rates at the moment than in previous times of increase in arrears and foreclosure, and of course an array of policy initiatives which John Healey will speak to in a moment, if you wish, which, I think, have encouraged a much more positive attitude towards forbearance. I meet regularly with the mortgage lenders at the Home Finance Forum and I can see over recent months a quite fundamental change in their attitudes towards forbearance and towards making every effort to ensure that the safety nets are not required, so I would argue, Mr Fallon, that the fact that somebody does not fall into the safety net does not necessarily mean that the existence of the safety net is not having an important impact on the behaviour of both lenders and borrowers.

Q270 Mr Fallon: Okay, but Kay Boycott from Shelter warned us that lender forbearance would likely decline once conditions in the housing market started to improve again and it becomes in the interests of lenders actually to repossess more quickly, but you still have not quite answered the question. If there are going to be 65,000 repossessions, why is your scheme only targeted at 6,000 people and so far only seems to have helped six?
Lord Myners: Well, firstly, I do not subscribe to the view that a recovery in the housing market would lead to lenders foreclosing in those situations. I think an environment in which people felt more confident about the outlook for house prices, inflation and the performance of the economy would be one in which lenders, who, after all, are at the moment deriving most of their profit from the asset side of their financing model, would not wish to curtail the size of their books as a response to that happening. The quantum of support being provided by various government schemes is probably a better issue for John to speak to.

Q271 Mr Fallon: We are just coming on to the detail of the scheme, but I wanted to be clear as to where the target of 6,000 came from. Was that a Treasury target?
Lord Myners: I think it is a target that evolved through discussions between DCLG and the Treasury.

Q272 Mr Fallon: Shelter told us last week that, for every 10% increase in sustained unemployment, there was likely to be a 30% increase in arrears and repossessions. Is that in line with your estimate of the relationship between unemployment and repossession?
Lord Myners: The Treasury does not make forecasts of either unemployment or repossessions and I would suggest that the Shelter model, which is a single factor adjustment model, is a very crude one, to assume that everything else remains constant but that you have a positive increase in unemployment, and needs to take account in practice of the existence of forbearance, of lower interest rates and many other factors which have a bearing on people's behaviour.

Q273 Mr Fallon: You seem fairly complacent about 65,000 repossessions. Do you understand the social impact of repossession?
Lord Myners: Of course I understand the social impact of repossession.

Q274 Mr Fallon: So why are you only aiming to help 6,000 people instead of the rest of them?
John Healey: Mr Fallon, perhaps I could help on this one because I think that, if that were the only thing the Government had put in place, your criticism and concern would have been well-founded, but it is not. That is a number based on the design and modelling of one particular scheme, the Mortgage Rescue Scheme, but the fact is that every month over 200,000 households are being helped with mortgage interest payments and last year 34,000 households were helped by the government-paid, free advice and representation in court. Even on the Mortgage Rescue Scheme itself, there is a risk of looking at the wrong end of the telescope here. It is a backstop for those who have not been able at any other stage in the process to be able, with their lenders, to renegotiate the terms of their loan. Now, on the Mortgage Rescue Scheme alone, which is the one that you are interested in at this point, over 1,100 people sought help from their local authority and got advice last month alone, half of those, with help from the local authority, were then referred to their lender or specialist money advice and, even of those in the system since it started since January where we have just under 500 going through the case, 200 have now been fully assessed, so, for those who are unable

to avoid the situation where they would lose their homes if this government scheme was not there to help them convert a mortgage into rent to allow them to stay where they and their families are living at present, it is there as a backstop, but it is only part of the picture and simply to look at the numbers at the end of the scheme is to omit its importance much earlier on. Exactly as Lord Myners said, part of this is about making sure that anyone getting into trouble with their mortgage talks as soon as possible to their lender.

Q275 Mr Fallon: I understand that and we took evidence on that last week, but, if the FSA believe that repossessions and arrears will in fact reach 1990 levels, as they have told us, are you ready to extend the existing schemes, either of you?
John Healey: I think everything that we have done so far, both extending and flexing the Mortgage Rescue Scheme, the Homeowner Mortgage Support Scheme and the terms of the mortgage interest, demonstrates that, far from being complacent, it is completely the opposite, Mr Fallon. I have to say, what we have looked to do this time is to draw some of the lessons from the situation people were left in in the early 1990s where there was no system of regulation in place, there was no toughening up of the protection for tenants and there were no special schemes put in place, as we have done this time, but, as the pressures and the market change, including the behaviour of the lenders, then we are ready to adjust the schemes as necessary.

Q276 Mr Breed: Lord Myners, as the Minister for Financial Services, are you concerned at the excessive charges which are being levied on people who unfortunately fall behind with their mortgages and, if so, what do you think you and the Government should be doing about it in conjunction with the FSA?
Lord Myners: Well, I think this should be a major focus of the FSA's work in the review which they have announced that they will carry out starting in September on the mortgage market. There is an overriding requirement for the mortgage lender to treat the customers fairly and clearly not exploit those who find themselves in a situation of considerable distress. That is one of the reasons why, for instance, we place such emphasis on borrowers having access to advice so that they are in a position to be able to form a view on the reasonableness of charges. If a borrower finds themselves subject to charges which they regard as excessive, then they should register that with the FSA and with the Financial Ombudsman Service, but I do have a concern that there is a risk that charges could be excessive and the FSA needs to give that very serious attention in the work they are doing.

Q277 Mr Breed: Do you think the FSA has been tough enough in respect of its investigation into individual firms?
Lord Myners: Well, the FSA is investigating a number of firms at the moment and I think it would be wrong for me to say anything, even if I knew anything, about those investigations, but I think they need to go through their proper process. I think the words from the FSA have been quite strong from Mr Pain in the recent letters to the sub-prime mortgage lenders and administrative agencies about the need to raise standards of conduct.

Q278 Mr Breed: So you are happy that their current stance in the way in which they are investigating is satisfactory and you do not have any plans to insist that they are tougher?
Lord Myners: I believe that the approach of the FSA when an organisation finds itself in enforcement is one which has stood the test of time and I think it is effective, but I think the new review of the mortgage market, which the FSA is due to carry out this autumn, will no doubt, amongst other things, revisit their approach to monitoring and enforcement.

Q279 Mr Breed: Well, for those who have already got mortgages and are falling into arrears those who are now trying to renegotiate or are going to new mortgages, there are some extraordinary charges which are being levied now for renewing mortgages or having a new one completely. It appears that they are trying, through charges, commission, arrangement fees and every other sort of fee you can think of, to increase the profit they are going to get out of that because of the low interest rates at the present time. Do you feel that that is just a market condition and, therefore, whatever the market decides in this area is okay with the Government?
Lord Myners: No, I think we need to be alert to the fact that there may not be a market there in the sense that unfair conditions could be imposed and, therefore, the FSA engages at that point through its "treating customers fairly" principle and then through MCOB13. It is a very short-sighted thing for a lender to do. If they have a borrower who is in a distressed condition, unable to service the mortgage, experiencing negative equity, quite frankly, to pile additional charges on a body which is already finding it difficult to sustain the weight is a very foolish and short-term thing to do. I think that, whilst this problem does exist, Mr Breed, and the FSA are absolutely right to focus their attention on it, it is at the margin of the business, but it is the margin where the mischief is being done.

Q280 Mr Todd: Is it not important to face the fact that repossessions may happen through a variety of circumstances and some of them are going to happen because people have over-extended themselves and that protective schemes may simply defer the evil day when an individual or a family must face the circumstances they are in?
John Healey: I think that is correct, Mr Todd, and, even in the good times, there is a level of repossession in the economy and the average in recent years has been about 35–36,000 a year. Our concern has been to do what we can to help people stay in their homes through this recession. Now, that means, and Lord Myners was quite right to point to this earlier on, that one of the things we wanted is for borrowers to speak to their lenders as soon as they may be getting

into trouble and for lenders to regard repossession as a last resort, and it may be necessary, but as a last resort, and to put in place the sort of rearrangement or forbearance that may be appropriate, given the individual circumstances. Now, not everybody will be able to reschedule their payments or will not be able to sustain, particularly if their change of circumstances is long-term rather than temporary, the mortgage that they may have taken out. Now, in those cases, a certain level of repossessions is inevitable. Our concern with the Mortgage Rescue Scheme, which Mr Fallon had indicated his interest in earlier, was particularly to help those who would otherwise then, without their home, defaulting on their mortgage and in threat of repossession, be in serious housing need and, therefore, require local authority housing as a matter of priority, so our attempt is there to head off the problem where we can, but provide a backstop where necessary.

Q281 Mr Todd: And the backstop has to be to face the fact that some people will have to change their housing tenure in time and will need appropriate advice and support to help them through what is a traumatic process and one which landlords need to be prepared for with a provision available.
John Healey: Indeed, but at every step of the way, from that first month when people may start falling behind with their mortgage payments to their repossession case coming up in court, there are things that we have tried to put in place, there is help and advice available and at each of those stages all is not lost, even when the case is in court.

Q282 Mr Todd: What I am hinting at, John, is that maybe local authority and other advisory support is inadequately resourced to meet the demand of the families we are talking about, and certainly my feel from the voluntary sector is that they are facing increasing burdens, even with the additional support the Government has provided to them, of providing advice to people in these sorts of circumstances. Hold that answer for a second as I want to touch on the private rented sector, because you can find yourself in difficult financial circumstances when renting as well, and the resources that may be available to support people through that process as well of dealing with the fact that they just simply do not have the rent available now to meet a commitment they entered into previously.
John Healey: Mr Todd, if I may say so, you are quite right to point to that area. A lot of the attention has been given to people and families struggling with mortgages and, because of the extra demands, to precisely, which I think you would urge the Government to do, the extra funding that has gone in this year to the CAB service, the extra funding that has gone into the National Debt Line, the extra funding that I put in last month to nearly 80 court desks; it is all there to help those who have their homes threatened because they are either threatened with eviction as tenants or repossession as homeowners.

Q283 Mr Todd: But we are not supporting, through that list of actions, local authority housing departments and those delivering support to those seeking any accommodation within the social housing sector.
John Healey: Indeed, that is not the case on a number of fronts. From the £20 million which within the last few months we have distributed to all local authorities in order that they can help deal with some of the sorts of immediate pressures in the system to the consistent increase in grant to local authorities that has been above inflation every year since 1997 to the additional help that the Prime Minister announced as part of the pledge to build more homes this year and next year—

Q284 Mr Todd: John, I place a marker down for you.
John Healey:—I know local government is moving once more, but on every front, recognising the important role local government has got to play, we have been ready to—

Q285 Mr Todd: Let me just raise one other narrow area, which is where a buy-to-let landlord has run into difficulty and places their tenant in a position where they must rapidly find other accommodation. Are we dealing with that circumstance adequately? What I am exploring is the holes in the safety net that has been drawn up, but, as one person has said, if you put together the safety net, you find it is full of holes. It is a good line and obviously logically true, but what I am looking for is where these holes are and whether we have explored them and justified them properly because, as I have suggested, we have got to face the fact that economic circumstance will deliver unpleasant outcomes sometimes, but, if so, whether we have rationalised the support framework for all the various groups that may be affected.
John Healey: Indeed, Mr Todd, and, if I may say so, that is why both Lord Myners and I work on this inquiry, just like the one that is being conducted by the CLG Select Committee, because we are keen to see where the potential gaps or weaknesses in the support system may be and that, where there are changes, we are ready to try and deal with them. You point to one such case which was drawn to our attention of quite a rising level of repossessions of buy-to-let properties in which the tenants had, in practice, only two weeks' notice, may not have been aware of the repossession in process and, having changed recently the Civil Procedure Rules in court, that has now extended at least to a minimum of seven weeks' notice, but there are still gaps, particularly for private tenants who may not know, understandably, the financial situation of their landlord, may not know that a repossession is under way, may not know that their tenancy is threatened quite suddenly, and we will look to change the legislation as we can and we plan to announce the proposals shortly to consult over this summer to do just that. Where the Committee is able to point in its report to further areas that it believes the

Government should consider, then in general terms let me give the Committee the reassurance that that is exactly what we would be looking to do.

Q286 Ms Keeble: I wanted to ask about the support for mortgage interest and, in particular, whether you are looking to review it. Presently, it is paid on income-related benefits and particularly income-related jobseekers' allowance, whereas most of my constituents and those in many other areas go on to contribution-based, but they still cannot afford their mortgage. Are you looking to change the benefits it is linked to?
John Healey: Not immediately, but monitoring how it is working, monitoring also whether it is meeting the sorts of needs that we have been trying to meet is what we are doing all the time, so, if there is a strong case for considering the terms on which it is available, we have shown before that we are prepared to adjust those, as indeed we have already done.

Q287 Ms Keeble: If you say "Not immediately", would you actually consider linking it, for example, to the tax credit system? If you take a household which has an income, say, of £600 a week and it shrinks, because one person loses their job, to £120, they will get contribution-based JSA of £60 per week, but they still will not be able to pay the mortgage and they have nightmares, absolute nightmares. Those are the people who are most likely, as I see it in my advice surgery, to lose their homes, whereas, if SMI was linked to the working tax credit, there might be a way just to raise their income enough for them to be able to manage to pay their mortgage. Would you look at that?
John Healey: If the Committee includes that in its recommendations, of course the Government will consider that. I have two immediate responses, if you wish, Ms Keeble. The first is that there is an advantage in this being a payment that is linked through the Jobcentre Plus single agency and linked to the process of signing on, so there is a practical advantage in not building in too much complexity. The second is, I think, a question about the purpose of the payment support in the first place and that is essentially to try and deal with short-term help when people may be at risk of losing their jobs, but actively with a prospect of getting back into work and, therefore, facing a temporary period in which they need support to see them through that period now.

Q288 Ms Keeble: The tax credit would do that.
John Healey: That is essentially the purpose of the scheme and, if I may say so, if you want to develop that case for doing it in a different way, I think you would need to make the case that it was consistent with the purpose and the principles with which it was set up in the first place.

Q289 Ms Keeble: The Building Societies Association has argued that, for these families, the support could be in the form of a grant rather than a benefit. Would you accept that case?
John Healey: To be perfectly honest, I have not heard that case. What is the advantage in a grant rather than a benefit?

Q290 Ms Keeble: The other thing is it used to be the case that you had to wait 39 weeks rather than 13 weeks to get SMI and now you only have to wait 13 weeks, but there is a two-year cap on it. Is that right?
John Healey: There is a two-year time limit, and it goes back to the point I made to you a moment ago, which is that the purpose of this scheme is not to provide government support in perpetuity, but the purpose of the support for mortgage interest is to help tide people through what they and we might anticipate is a temporary dip in their earnings based on the risk of not just losing their job, but losing their home at the same time.

Q291 Ms Keeble: There are two problems with that. One is that the people who are most at risk are the people who lose their jobs, go on to contribution-based benefits where there is a track record of working in the family because one partner works as well, so they are on contribution-based benefits for six months and that is a temporary period when they most need support and they cannot get it during that period. That is why I asked about linking it to the tax credit or some other system to support them through those six months.
John Healey: I understand more clearly the argument you are making now.

Q292 Ms Keeble: So you would be sympathetic to some recommendations about looking for different ways to support people through those six months?
John Healey: Well, as I said, if the Committee is making recommendations, then the Government will consider them.

Q293 Ms Keeble: Can I ask about the two-year thing because again in my constituency everybody works and they often work post-retirement. A woman came to me in my advice surgery, she was 58, she had lost her job, she had to wait for six months to get SMI, she then would only get it for two years and she did not think she probably had a realistic chance, given her age and given she is an admin worker, of being able to get another job and she then hit retirement with the risk of losing her home and with no means of supporting her mortgage. Do you not think that the two-year cap is unrealistic, given the age profile of people being made unemployed and the pressures that they face about supporting their homes which is a long-term asset, not a short-term asset?
John Healey: It is obviously difficult for me to comment on an individual case, but it does strike me that perhaps a more pressing concern of someone in your constituent's situation then would have been to see the sorts of changes that we have made, so, instead of having to wait six months, only having to wait 13 weeks—

Q294 Ms Keeble: No, she gets contribution-based JSA, so she does not qualify.

John Healey:—and then also having the capital limit doubled in some areas where clearly the scale of the loans that people have is significant. As far as your own area goes, it is an area where we have been aware, and you have played a part in making us aware, of the sort of pressure that people feel and are under on sustaining their mortgages and in negative equity.

Q295 Ms Keeble: I wanted to ask a bit about negative equity. The point is always made that it is not a problem until people move. However, a lot of people feel, when they are struggling to pay their mortgage in the kinds of circumstances that I have described, that, in a sense, they are throwing good money after bad because they are really struggling to maintain payments on something that they know is a declining asset and they are not sure when and if it is going to come back up again and if it is going to come back up before it gets repossessed or what is going to happen and if they are going to get a job. Do you feel that some policy instrument is needed to look at how to deal with the problem of negative equity?
John Healey: I do not necessarily feel that some specific instrument is required, but I do think we have got to be prepared to take it into account in the support we give or the way that we design our schemes. In fact, that was one of the elements that we adjusted our principal scheme to allow where previously, if someone was in negative equity, they were not eligible. I have to say, the representations from you and from Northampton were part of our thinking in making that Mortgage Rescue Scheme take account of and to not bar anyone simply because they had slipped into negative equity. You may be interested that 83 households in Northampton have now approached for help with mortgage difficulties and most of those have been now referred to lenders or for specific money advice and three are now being considered for the backstop provision under the Mortgage Rescue Scheme where, if the lender is not prepared to forbear, if they are not able to reschedule their interest payments, but nevertheless they would be vulnerable as homeless households, then a housing association may be prepared to step in under the terms of our scheme, allow them to stay in their homes, buy out their mortgage and convert it into a rent.
Lord Myners: If I may add a point to Ms Keeble's question, I meet monthly with the major mortgage lenders, the building societies and the banks, the third-tier lenders, the regulators and organisations, such as the Citizens' Advice Bureau and Which? to discuss what is going on in the residential housing market, and obviously I have a particular focus on issues relating to funding and to financial stability. What is quite clear from the engagements I am having with the lenders and also those who advise people who are experiencing difficulties is that negative equity does not necessarily lead naturally to arrears and repossession. Firstly, negative equity is a subjective element and valuations are difficult at the moment, so I see various estimates that 5% to 10% of domestic mortgages are in negative equity, but I do not think one can be terribly precise because the market is not terribly liquid in property, although it is getting better, but it is people's ability to service the mortgage and I think it is economically rational for people who have negative equity to continue to service the mortgage if the alternative is to lose their home, disrupt their working divisions and sever their relationships with friends and family, so it may not be economically sub-optimal for them and they are not necessarily pouring money into something which has already lost its value.

Q296 Ms Keeble: One thing which I am concerned about is that, according to the FSA figures, the biggest percentage of mortgages at 39%, and it is 35% for buyers and 29% buy-to-let, but the biggest percentage is for equity withdrawal and those mortgages are unlikely to be covered by SMI because that tends to be just on the first mortgage for home purchase. Could you say whether you would be prepared to look at relaxing the scope of SMI to include more and obviously, if people have just done it for consumer spending, then you might say no, but be more generous about taking into account those mortgages for equity withdrawal for SMI?
John Healey: I think you might be asking for quite a difficult subjective judgment about whether or not the particular compounded debt was derived in part from equity withdrawal for consumer spending and I think that is quite a difficult thing to propose.

Q297 Ms Keeble: Well, would you look more carefully?
John Healey: If you are looking to take into account second-charge lending, then the mortgage interest may not be the right one and we have taken it into account in one of the other schemes.

Q298 Sir Peter Viggers: Lenders covering about 80% of the mortgage market are involved in the Homeowners Mortgage Support Scheme or in schemes comparable to it. What are you doing to address the remaining 20%?
Lord Myners: We are actively in discussion with them, Sir Peter, and actually of course that is where the majority of the problems lie.

Q299 Sir Peter Viggers: Exactly.
Lord Myners: Now, this is a sector of the industry which is experiencing very real difficulties because its business model is no longer valid in current market circumstances because these tertiary lenders were almost wholly dependent on wholesale funding or securitisation. Now, as confidence returns to the banking market, they are beginning to access additional funds, but clearly this is an industry with whom we are having to work very, very closely. This is where the FSA has been applying their attention and the most recent report, which the FSA produced on 22 June, was very specifically targeted on the non-mainstream lenders.

Q300 Sir Peter Viggers: Are you contemplating compulsion and do you require legislation for that?

Lord Myners: I think we would study very carefully the advice that the Committee gave in this area.

Q301 Sir Peter Viggers: It is early days of course for the scheme, but how would you judge its success and what would success look like?
Lord Myners: Its success is the existence of a safety net which is giving people confidence that the mechanisms exist to help them, in the case of the scheme to which you refer, cope with a period when there is a temporary shortfall in income when perhaps in a two-earner family one of the earners has lost her or his job or where there has been a serious reduction in overtime or the employers moved to short-time earnings. Now, what we want to do is to work with lenders to ensure in that situation that, if there is a reasonable prospect that this individual or this family can return to previous levels of income, then they should be supported during this period of temporary disturbance to their finances, so I think one would measure success in terms of how many cases we could see whether either the existence of the scheme meant it was being drawn on or the very fact that it was there meant that some alternative or similar arrangement was also being put in place by a lender who had not signed up to the scheme, but nevertheless has assured us that they are offering comparable arrangements to the ones which we are proposing.

Q302 Sir Peter Viggers: You did not directly reply to the question as to whether you are contemplating compulsion. What steps are you taking to encourage the remaining 20%, who are not participating in the scheme, to participate?
Lord Myners: Well, I think compulsion is extraordinarily difficult in this situation to compel a lender not to act appropriately to defend the interest of the lending organisation, so I think it is through engagement, discussion and encouraging these lenders to behave responsibly.
John Healey: I think there is also another element which the Committee might wish to look at which is what is called the "pre-action protocol". This is now implemented in courts and it places certain requirements on lenders, whatever their nature, to have been able to demonstrate at earlier stages that they have been prepared to put in place forbearance for the borrower and that they have been prepared to look at the circumstances of the borrower and whether they could reschedule the debt or come up with any other alternative so that repossession then really does become a last resort. That pre-action protocol bites on the sub-prime lenders just as it does on the high street lenders, and I am interested in looking at the scope which I have discussed with the Chairman of the FSA for making sure that the pre-action protocol is consistent with the terms of the FSA requirements and rules. So, in other words, at the front end and at the back end there is a consistent set of expectations and requirements on lenders. It also means that the borrower, however they come into the system, wherever they are at the various stages of mortgage difficulty, know where they stand and what they can expect from their lender, but also what their responsibilities are as well.

Q303 John Thurso: John Healey, can I ask you these questions. I was listening very carefully to the answers that you gave to Michael Fallon about the Mortgage Rescue Scheme and particularly your comment that we were looking at the wrong end of the telescope. When the Scheme was set up it was time limited to two years and the Government estimated it would help 6,000 families and have a budget of £285 million, which is an average of £47,500 per household. We are now several months in, we have helped six households, which would put on that average of six a month the final spend at around £7 million. Why is there such a discrepancy between the estimate and the reality?
John Healey: Because, if I may say so, Mr Thurso, you are looking at the wrong end of the telescope.

Q304 John Thurso: I thought you might say that.
John Healey: What you are missing is that more than 5,000 households have got advice from the local authorities as a result of this scheme. You are missing the fact that 202 households have now been through a full local authority assessment. In about 40% of those cases with the local authority assistance there has been action with the lenders to divert what were families and households threatened with repossession onto a more sensible footing. You have got half then who are into the final stages of the Mortgage Rescue Scheme, 26 of whom have now had a formal offer from a housing association for help. Although this may not be in evidence given to this Select Committee, I mentioned earlier the DCLG Select Committee and Andy Hayward from the Council of Mortgage Lenders said to that Committee: "There has to be a degree of realism as to how long it takes for the Mortgage Rescue Scheme to build up". That is what we are seeing over these first four or five months that the Scheme has been in place.

Q305 John Thurso: I completely accept that. Would you then expect that estimate that was made at the beginning of the Scheme to be broadly where the Scheme will end up at the end of its two year lifespan or would you expect it to undershoot?
John Healey: So far we have no reason to believe that is not a good working assumption. Clearly the sort of factors that we may see in play from changes in base rates to levels of unemployment to recovery in the economy generally, there are a number of factors which may affect the sort of trend and pressures ultimately in repossessions over the next 18 months or so. We will be in a better position much closer to the two years to be able to judge whether or not our estimates at the outset,—and after all this is an innovative scheme, we tried to put in place something that has not been in place before and certainly was not there in the early 1990s when people were left to struggle on their own to get

through the problems then—those working assumptions which we set the Scheme up on, prove to be correct or not.

Q306 John Thurso: You talked a lot about the pipeline, and there has been much talk about the pipeline, but one would need to see a very dramatic increase in what was in the pipeline to reach even half the numbers that we are looking at there. Would you agree with that? To get anywhere near the numbers that were put forward would be a quantum leap in what is coming through the pipeline.
John Healey: To be perfectly frank with the Committee, if this Scheme is not needed in up to 6,000 cases I will be pleased.

Q307 John Thurso: I agree with that.
John Healey: Because it means that it will have worked at earlier stages to get people onto a more sensible footing, to bring attention to the negotiations we want them to have with their lenders, and it will mean that ultimately what Government is prepared to fund and the arrangements we are prepared to put in place have not been necessary. Sir Peter Viggers asked what success might look like earlier on, and it is difficult to say what success would look like but it is possible to say what some signs of success look like. If you look at the quarter one level of moves for court possession orders, down by over 40%, I think that is a good indication that in different ways the system and lenders are taking seriously this imperative to offer forbearance and deal with borrowers in a way that tries to help them avoid the ultimate default and repossession.

Q308 John Thurso: What difference do you expect the establishment of your new central team to manage and fast track applications will make to the numbers that are going through?
John Healey: Again, if I am honest, it is difficult to say with certainty. We are looking to set up a central team that will be in place this month, as I announced, about 15 to 20 people. Rather than waiting simply for cases to come up through the local authorities or that crop up because individuals have approached their lenders, this is specifically to work with lenders who will trawl through their loan books looking for potential cases which they can see ought to have red flags on. It gives us the opportunity to take the initiative here with cases that may fall into that category, link with the local authority, link the lender to the borrower and say, "Look, rather than leaving this until the borrower might actually be under such pressure that they decide to act for themselves, we can get things going that hopefully will be able to head off repossessions that otherwise would occur". If all else fails and it is required then obviously the terms of the Mortgage Rescue Scheme, that potential for converting mortgage into rent, will exist in those cases as well.

Q309 John Thurso: One last question, if I may. Clearly a great deal around this is dependent on what is happening in the wider economy, both at macro level and every other level. The Scheme is time limited to two years based on broadly the forecasts of when the worst problems might be expected. If what happens in the economy is different from that in the forecast and there is a need which continues beyond that two year time window for another six months or a year, would the Government be content to extend it?
John Healey: Yes, we would certainly consider that.

Q310 Mr Brady: Lord Myners, we have heard that a large number of smaller lenders in particular say that they cannot lend obviously for a number of reasons, but one of them being the cautious capital requirements the Government and regulator are placing upon them. Are you confident that you are striking the right balance between sensible caution and the importance of seeing the housing market come back to life?
Lord Myners: I think the capital requirements undoubtedly needed to be strengthened, and that is one of the lessons which we have learned from the global financial crisis and the absolute amounts of capital the banking institutions have to hold and also that capital allocated against specific risks. There has not been a significant change in the amount of capital required to support residential mortgages. I think the challenge that many smaller lenders are currently facing is much more, as I alluded to earlier, on the deposit side and the competition for retail deposits and the drying up of wholesale deposits into smaller lenders and the complete cessation of the securitisation market has led to the greatest difficulty for smaller lenders.

Q311 Mr Brady: You do not accept that capital requirements are a significant factor in this?
Lord Myners: I think capital requirements have been a factor, but I do not think they are the most significant factor. In fact, we continue to have low capital requirements against mortgages with a low loan-to-value. What we have seen is an increase in capital requirements for mortgages which are at greater risk of default and that is precisely what one would expect to ensure that there was sufficient capital available to sustain losses and that organisations which were inherently more risky, whether it be through their investment banking activities or because they were at the non-conforming end of the residential housing market, would be required to have more capital to reflect the higher risk they were carrying.

Q312 Mr Brady: What we are seeing in the market is a move away from offering 90% mortgages, more likely 60/70% loan-to-value. One of the solutions which has been put forward to us by *Which?* in evidence to us is the suggestion that the Government could insure the additional risk element to make it possible for lenders to offer those 90% mortgages which obviously are particularly important for the first-time buyer. What is your reaction to that?
Lord Myners: I think we will see, Mr Brady, a progressive move towards an increase in the number of offerings of higher loan-to-value mortgages as

confidence begins to return to both the housing market in terms of house price trends and also into the broader economy, although the Prime Minister made it very clear back in January in his request to the FSA that he wants serious investigation as to whether we should introduce some form of ultimate cap on loan-to-value ratios, and we will await the outcome of the FSA's deliberations on that subject. There are some markets where insurance has been used, Canada and Hong Kong being two examples. The question about whether that ultimate risk should be borne by the state and whether there should be an element of subsidy or an attempt to fairly price, and if it is fairly priced what would insurance be adding which a bank would not be able to add, would seem to me to be worthy of quite a lot of debate. It draws me to the conclusion that insuring the top end of private mortgages is not something which is going to add a great deal to risk management unless there is an inbuilt subsidy and then we have to ask ourselves some questions about the reasonableness of people in the broader community subsidising people buying homes with high loan-to-value.

Q313 Mr Brady: There is nothing that could or should reasonably be done to facilitate a greater availability of those higher loan-to-value mortgages?
Lord Myners: I think economic forces will see a return to higher loan-to-value lending. We are seeing this happen from major lenders like HSBC and I think if there is a commercial opportunity there for insurers then insurers will step in and create a product as well. I do not think that it would be incumbent on the Government to specifically encourage a move back to high loan-to-value mortgages which did not have the full support of the judgment of lenders.

Q314 Mr Tyrie: There is strong discouragement out there, is there not, at the moment for borrowing from lenders. I am just reading the House Builders Federation evidence: "Lenders are looking for any reason to refuse a loan. Credit scoring has been tightened. Much more information is sought. Loan refusals can be made on the smallest of details". That is an environment that you recognise, is it?
Lord Myners: Mr Tyrie, no, it is not an environment that I entirely recognise because the data that we are seeing as published by the Bank of England in their monthly lending reports, in the reports that they get from their lending agents and in the information which we are gathering through the Home Finance Forum as part of the lending panel structure suggests that there is an increase in lending activity, there is more available finance and there is a trend towards more property being offered at the higher loan-to-value area. There are pockets of the housing market which are still very, very difficult. Inner city flats, for instance, which were built specifically for the buy-to-let market are still experiencing serious value challenges, but there are other areas of the market which are beginning now to find an equilibrium of value. I think in three of the last four months one of the major property surveys has indicated values increasing. The RICS data is showing, for instance, that the time from advice to sale of a house is shortening which is a sign of improving activity. We are also seeing estate agents now saying that the balance of available property to prospective demand is significantly lower than they would normally expect in an affected market. I think the housebuilders will have a view but there are other views as well, Mr Tyrie, which one needs to be informed about.

Q315 Mr Tyrie: Since the market more or less closed up shop for a while I would expect some improvement in the data. Banks are rebuilding their balance sheets, are they not, by widening their margins, especially on tracker and discount mortgages. Do you not think that what is really going on is that mortgage holders and particularly new buyers are now paying the price for banks' past mistakes?
Lord Myners: I think banks lost the ability to make good and informed judgments about pricing risk, and that was one of the causes of the global banking problem, they simply were not evaluating and pricing risk accordingly. They have now reverted back, they have to rebuild their capital structures, they have to do that with support from their shareholders, they have had to do it with support from the Government and obviously retained earnings is another form of building up capital.

Q316 Mr Tyrie: Using the phrase "retained earnings" is really a polite way of saying, "Yes, mortgage holders and first-time buyers are paying for the mistakes of banks"?
Lord Myners: There is a very competitive market for mortgages.

Q317 Mr Tyrie: But if it is so competitive, if I may interrupt you a second time, why are those margins widening? Is that not a sign of declining competition in the market? Is it not something you should be concerned about?
Lord Myners: The competition market is not synonymous with low or close to zero margins, it clears at a level which appropriately rewards risk and generates an adequate return to equity capital. In the past the banking industry got itself seduced into poor pricing and we are now seeing that adjusted, Mr Tyrie.

Q318 Chairman: "Seduced into poor pricing"?
Lord Myners: Yes.

Q319 Chairman: What does that mean?
Lord Myners: Peer pressure, irrational exuberance was the phrase Mr Alan Greenspan used.

Q320 Chairman: They did crazy things, they did not know what they were doing.
Lord Myners: I think they did things which they would come to regret.

Q321 Chairman: Okay. Which others would think were crazy, yes?
Lord Myners: Yes.

Q322 Jim Cousins: Lord Myners, if it is the Government's policy to rely on market forces for a return to lending based on securitisation and for a return to higher loan-to-value and loan-to-income lending, is it not really unavoidable that young buyers who do not have access to the bank of mum and dad have had it for some years to come?
Lord Myners: The first observation that market forces will ultimately determine the availability of credit and the pricing of credit and the conditions of credit link naturally to the issue about high property values. This is a problem for young people and first-time buyers. This is one of the reasons why the Government is so actively encouraging the availability of new property through new build programmes and other initiatives being pursued by CLG.

Q323 Jim Cousins: Turning to CLG, we have got this rather complex array of homebuyer schemes which have very poor take-up. What are you going to do to soup those schemes up so that they can substitute for the bank of mum and dad?
John Healey: I do not think they can ever act as a substitute but what they can do and are designed to do, and were given a further boost of £300 million in the budget, is to encourage two things. At a time when private sector builders last year made starts on new homes at levels we had not seen since the 1980s recession and dropped by a half from just the year before, this sort of support can, first of all, encourage developers to build and, secondly, it can in part help often first-time buyers, in some cases important public sector workers, to get that first foot into the housing market. I do not accept the general argument that too few people benefited from this over the last 10 years to brand them a failure.

Q324 Jim Cousins: Why are we not facing up to the fact that renting, which for many people is a brief transitional moment in their lives, is now going to become a much longer term 10 year option for very large numbers of people? Why are we not just facing up to that fact?
John Healey: I think, Mr Cousins, we are facing up to that. What the Prime Minister announced last week as part of the housing pledge was not just—

Q325 Jim Cousins: John, I am not talking about council housing because a lot of the people who are going to be in long-term lending are people who would never qualify for social housing.
John Healey: No, indeed, but I was going to start with my response to you to say at a time when public finances are extremely tight we have nevertheless been prepared to switch to reflect the high priority that the Government gives to building new homes, the majority of which are for rent at levels which are affordable to people by both councils and housing associations and through kick-starting some of the private sector developments that will also make these homes available but are stalled at the moment because of the recession, that is a recognition that we need to build more homes, we need to build more homes to rent and at prices people can afford to rent. I think if you look at the attitude surveys of people towards homes, housing and what is now, they would say, their first choice of security and type of tenure, more and more people are looking at rent as their preferred option. They are not looking necessarily at long-term loans and mortgages. The way that we tackle both new build and rights for tenants, including in the private sector, is starting to reflect that and will need to reflect that, I think, and I share your view in this, for the longer term as well.

Q326 Jim Cousins: Are we going to consider now the implications for society as a whole of renting being a much more long-term option with much larger numbers of people than historically it has been and the need to face up to the fact that we may have to rescue large numbers of people on modest and fragile incomes from owner-occupation that is not now sustainable?
John Healey: I think the nature and the scale of the housing need, particularly based on the population and other projections for the next 10 years, require us to consider how we make available homes with a wide range of tenure, including with more emphasis on the rented sector than we have done over the last decade. That is exactly the sort of approach that we are beginning to take in Government.
Lord Myners: Certainly the evidence I have seen, Mr Cousins, suggests there is a generational change here. Young people are now increasingly seeing renting as a desirable option at a time when their lives are subject to more change and we may well be moving to a period when the first purchase is delayed until people are in their thirties rather than an aspirational goal in their twenties.

Q327 Jim Cousins: Lord Myners, is the Government considering the implications of the fact that through the stakes that the Government now has in financial institutions—and I am here thinking particularly of the Bradford & Bingley mortgage book—the Government is probably now the largest provider of buy-to-let mortgages in the country?
Lord Myners: Yes, we recognise that is the consequence of the actions we took to protect Bradford & Bingley, but I think we are going to see the evolution of an increasing buy-to-let market. I think it is going to become more professional. Many people often do own one or two properties, but what is very interesting is we are seeing the emergence of much more professional portfolios here. An interesting feature which we have not seen in the UK is the involvement of institutional funds in residential buy-to-let. There is no obvious reason why that should not occur, it happens elsewhere. Germany, for instance, has a very substantial private rented market in which the properties are owned by pension schemes and insurance companies, and

CLG is going some work in this area to work with institutional investors to see what would need to be done to encourage that as a source of additional funds.

Chairman: Mr Healey, thank you for your attendance. Lord Myners, the same for you, and we have the pleasure of your company again tomorrow. Thank you very much.

Written evidence

Written evidence submitted by Mr and Mrs Peffer

INTRODUCTION

We, Andrew and Julie Peffer are submitting this formal submission with a view to having radical changes in the way repossession is handled, "After the Court Stages of Repossession" when selling a property and the lender made more accountable for all those they instruct in the sale of the property.

Having gone through three repossessions in the space of two weeks during April and May 2008, one of which was an Unregulated Business Mortgage, with three different Mortgage Companies, we feel we are in a very good position to demonstrate that the borrower receives no protection from the lender and all those that they instruct in the sale of their property.

If the lender insists on the borrower paying any shortfall, the borrower must at all times be involved in the sale of the property. With the system we have at present, if there are any problems in the sale of the property and costs are involved, whether it be the fault of the lender or those they employ, the borrower has to bear the brunt of it, this cannot be right.

We have asked one Mortgage Company for the Terms and Conditions which outlines the Legal/Moral Obligations towards the repossessed and most importantly the Duty of Care to be shown, no reply. When a borrower takes a mortgage on, the lender insists all criteria is met and the Terms and Conditions are signed before any money is advanced. After repossession they are free to do just as they please, for the sake of all repossessed in the future, changes have to be made.

We list in numerical order, points we feel the lenders should adhere to. They should be standard for all lenders and produced to the borrower before repossession has taken place.

1. The lenders representative at the 1st Possession Court Hearing should know the case in full before attending, especially if all information has been submitted before any Court case by the borrower before the said date.

2. The lender as well as the borrower(s) must respect the Courts decision in connection with the Possession Order.

Any request refused by the Judge from either the lender or the borrower(s) must be respected or appealed.

3. The Courts, the lender, the lenders Solicitor and the borrower(s) should know exactly what date the Possession Order is for.

If several dates are given, for example, three different dates in Solicitor letters and Court notification, then contact should be made and the borrower not ignored by any of the parties involved.

4. The lender should know exactly what the procedures are if the borrower respects the Courts decision to vacate the property on the said date by the Judge. If the borrower vacates the property on the said date, this should not be deemed as voluntarily handing possession of the property back.

4.1 Where and to whom the keys are to be returned to.

4.2 Demonstration of any security system.

5. The lender must at all times know how to source all utility companies, if the borrower is not in attendance or forthcoming with this information on the day of possession. This can be achieved by telephoning for example, Transco for the Gas etc. At present the lenders do not consider this option.

This should not happen a year down the line and left for the borrower to sort out with the utility companies. Should a forced entry be made, this should also not be for the borrower to sort out three months after it has happened to get the keys returned to the Mortgage Company.

5.1 The lender must be responsible for all utilities. The utility companies will not take the word of the borrower who the name of the lender is and they are under the impression the borrower is no longer responsible. It must be pointed out that letters will obviously not get through due to the letter boxes being sealed.

What the utility companies are not aware of; any costs the lender incurs from the utility companies will be bourn by the borrower, whether it is their fault or not.

Should the utility companies not be able to gain access to read meters etc as they are unaware who has taken responsibility of the property once repossessed and lender has not done their job properly, the utility companies can go to Court to obtain a Warrant to force entry, again the cost is bourn by the borrower.

6. The Authorities should be informed when a property has been repossessed; this should not be left for the borrower to do.

7. The lender must be contactable during the same working hours as their Collections Office; this enables the borrower to make contact with the lender after repossession has taken place to find out the marketing procedures of the property.

8. If the lender is using a Managing Agent, the Managing Agents details should be made available to the borrower and the lender must never advise their Managing Agent/Estate Agents, they are under strict instructions not to speak to the borrower.

8.1 Should the lender use a Managing Agent, what appears to happen is the Estate Agent is left to their own devices and any discrepancies with the marketing etc is only picked up by the borrower who advises the lender. A Managing Agent should never contradict the lender.

08.2 The Managing Agent the lender employs, should be no more than 30 minutes away from the property and the Estate Agent employed by either the lender or Managing Agent should be in the post code area of the property.

Most Estate Agents offer Management Services; therefore there is no excuse for employing someone for example 240 miles away from the property in question.

9. A property should be valued as a property and not for repossession purposes. Having restructured on many occasions, it has been proved threee levels of valuations exist ie private sale, re-mortgage and repossession.

10. When the property has been valued, the lender must make available in writing ie fax, email or post to the borrower so the borrower is given a certain time limit to respond with any input.

10.1 The property should be valued by a professional RICS Qualified Surveyor in the local area, not a subsidiary company of the Managing Agent who could be miles from the property in question and would possibly cause a conflict of interest. Although the Estate Agent gives his/her appraisal on the property, they are not qualified surveyors.

Someone outside the area does not use realistic comparables as they do not have a feel for the area due to the fact they are only using internet based sites.

11. The borrower should not have to remind the lender about a HIPS Pack or it be commissioned some four months following possession of property.

12. The borrower must know where the property is being marketed, for example on the internet, with advertising boards erected and not have to remind the lender this is not being done, for example, after one month or more following repossession.

13. The lender must be fully aware at all times what their Managing Agents and Estate Agents are doing with the marketing of the property and this information should be made available to the borrower. It should not be for the borrower to pick up discrepancies in the marketing and contact the lender direct to correct the situation.

Unless the borrower brings discrepancies to the lenders attention they would carry on and not be picked up.

13.1 Description of property

13.2 Should the lender be using two or more Estate Agents, the sale price should be the same.

Not for example, three different prices.

14. If the lender is to reduce the value of the property, a full explanation should be given to the borrower first, especially if this is done in a short timescale.

For example after three days.

15. The Managing Agent/Estate Agent who the lender employs under no circumstances should ever advertise in the local paper the property as repossessed and never attach a notice on the front of the property stating, the borrower has mortgage debt.

Although the lender disagrees with the property being advertised in the local paper as being repossessed their Managing Agents opinion differs. It is the lender that employs the Managing Agent not the other way around.

If the property is a business premises which has been repossessed, this has nothing to do with the business itself, then the Company name should it be put in the local paper, be blacked out, if the business is still trading at all times.

16. If an offer comes in for the property, the lenders outlay is covered and there is a surplus, the lender should not have the right to refuse it. If they do, a full explanation should be given to the borrower why, not just "we are unable to consider the offer".

16.1 If the lender receives an offer and they are in the middle of changing Agents then the property should still be marketed until Exchange of Contracts in case it falls through and the lender should not respond stating they are awaiting the outcome of the offer.

16.2 Any offer accepted by the lender should be advertised in the local paper by the Managing Agent/ Estate Agent who is marketing the property at that time, not one that has been disinstructed, then puts up for sale boards a week after the notice appears in the paper.

This is when the Managing Agent would also send a letter of confirmation to the prospective buyer.

16.3 If the lender has the opportunity to show a prospective buyer around the property, under no circumstances should they drop the value before inviting the buyer in.

17. The Estate Agents should at all times pass details on of any prospective buyer to the lender (and not ignore their emails/telephone calls) and it should not be the responsibility of the borrower to pass on relevant information so that action can be taken.

18. The Estate Agent, the lender or the Managing Agent employs, should never distribute leaflets in the local area stating the property is sold, when it is not.

18.1 If the Estate Agent has been instructed to have an Open Day leaflets should be distributed to all in the local area and not just their own special clients, it should also appear in the paper.

18.2 If the Lender then decides to have another Open Day due to lack of marketing material distributed by the Estate Agent, the lender must make sure, dates and times tally up with leaflets distributed in the area and in the local paper. The borrower should not have to bring this to the lenders attention.

19. The Estate Agent should not erect a "For Sale Board" which states "Sold, Subject to Contract" and leave it there for five months when a buyer has pulled out, for whatever reason.

20. If an Estate Agent has been disinstructed by the lender they should remove their "For Sale Board" and any marketing material on the net promptly and not at the request of the borrower some weeks/months later which results in the property for example, being marketed at three different sale prices at the same time. This should not take six months to achieve.

21. The weekly checks the Estate Agents are instructed to do by the lender should be documented and made available at the borrowers' request.

22. The property should be marketed properly and not as follows:

22.1 A shop that is described as a studio flat, flat apartment or industrial unit etc.

22.2 Under no circumstances should a picture of a toilet be used as the main photo to advertise a property on the internet.

22.3 Under no circumstances do you only describe the property as overlooking a pretty little green or with just room sizes.

22.4 Details should be checked under the Property Misdescriptions Act 1991, for example stating scope for planning permission when it already exists and of which the lender already knew about before repossession.

23. The lenders state, they have to believe their Agents when information is not uploaded to the internet web sites ie Findaproperty and Rightmove. Agents try to blame these sites when in fact it is them themselves who upload the information.

Proof of this can be produced.

24. Although the lender may be rectifying any issues the borrower has bought to their attention, the lender must never make the borrower pay for the errors whether it be theirs or the companies they employ.

Arrears rising.

25. The lender should never return to an original Estate Agent they have previously disinstructed, especially when that Agent advertised the property as repossessed.

26. There are strict instructions the Agents lenders employ have to follow, which they do not. The Agents should never inform a prospective buyer, the property is a repossession, although sometimes it is obvious.

27. The lender should try to sell property even if they are being investigated by the Financial Ombudsman Service and not state they are awaiting the outcome of the investigation if an offer comes in.

28. When reading the internet, information is given "what to do following repossession". If you have never been through a repossession, how can anybody comment? What should happen and what does happen are completely different.

29. The internet also states about approaching Government bodies ie the Financial Services Authority etc who in effect are no help whatsoever and advise the repossessed to seek independent legal advice—what repossessed person can afford that. Therefore it leaves these companies wide open to do just as they please—they are above the Law.

This has happened in the past, it is happening now and it will happen in the future unless changes are made.

The financial institutions are in a win win situation and it appears even if they do wrong they are not penalised and then carry on.

30. Although the property has been repossessed statements still should be issued along with any interest rate increase/decrease letters which does not happen, they would soon be returned if the post has not been redirected due to the fact Agents seal the property letter boxes.

Any questions that are brought to the attention of the lender by the borrower in connection with any charges that have been added to the Mortgage Account, Insurance Premium, Home Visit (when there has not been any), Rates, Ground Rent Arrears a description used as the lenders system is not able to cope with

what this should really be, a full breakdown of Solicitors costs and also Agents fees which could mean anything should be answered and letters not ignored. When a full breakdown is requested, this should be produced.

Once these companies issue their final responses, they totally ignore any further letters, even though more issues are raised.

CONCLUSION

Taking all the above into consideration, we feel the lender not only should be made more accountable for those they instruct, penalties should be imposed upon them for any errors that are made, whether they or the people they instruct are at fault and the repossessed compensated.

All above points can be proved.

An alternative would be, not to charge the repossessed any shortfall, but to have an Insurance Policy in place in the event of repossession. If the lender was submitting too many shortfalls the Insurance Company would soon come down on the lender to find out what was going on. The present system suits the lender as they can threaten the borrower, claim on any Insurance Policy in force, then pass any balance onto a Debt Agency. They are aware the general public are either frightened of them or have no knowledge what to do.

All we are looking for is fairness for the repossessed, "After the Court Stages of Repossession".

I would reiterate, we have found no Government body to help during these trying times and that is why we had to turn to the press.

We thank you for this opportunity for allowing us to submit this submission.

April 2009

Memorandum from Citizens Advice

INTRODUCTION

1. Citizens Advice welcomes this opportunity to submit evidence to the Treasury Select Committee concerning mortgage and secured loan arrears. The Citizens Advice service is a network of over 400 independent advice centres that provide free, impartial advice from more than 3,000 locations in England, Wales and Northern Ireland.

2. In 2008–09, the Citizens Advice service in England and Wales helped nearly two million clients with about six million problems. Debt and welfare benefits were the two largest topics on which advice was given, with 575,000 clients helped with approximately 1.9 million debt problems, and 95,000 enquiries about mortgage and secured loan arrears in particular.

3. In 2007, Citizens Advice published evidence of rising problems of mortgage and secured loan arrears, particularly amongst low income households, often borrowing from sub-prime lenders.[1] These problems preceded the current economic downturn and were exacerbated by falling house prices.

4. During 2008, mortgage and secured loan repossessions and repossession claims rose sharply, and the government introduced a broad-ranging package of measures in late 2008 designed to help people stay in their homes. As house prices continued to fall and unemployment began to rise with the economic downturn, there is evidence of arrears problems extending across a wider range of the population.

5. During 2009, arrears continued to rise significantly and repossessions also continued to rise strongly.[2] But the number of possessions claims (ie cases being taken to court) fell significantly.[3] This positive evidence suggests that very low interest rates and the government measures introduced in late 2008 and early 2009 have had the overall effect of making court action less likely, though people continue to lose their homes.

6. Citizens Advice, together with the advice charities AdviceUK, the Money Advice Trust and Shelter, carried out attitudinal surveys of advisers in April[4] and found improvements in arrears management practices for mainstream lenders over the last six months. As the policy initiatives are fairly new it is too early to assess fully their impact, but it is of concern that not all lenders appear to be using court action only as a last resort.[5] To assess the full impact of the initiatives, we will repeat this survey in October 2009 and publish results by the end of 2009, along with research on clients seen by advisers who are giving advice at court on repossession days.

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1 *Set up to fail*, December 2007, Citizens Advice.

2 FSA Mortgage Lending statistics show the total number of loan accounts in arrears at Q1 2009 was 399,000, an increase of 6% since Q4 2008 and 33% on a year earlier. Repossessions were 14,825 in Q1 2009, 13% higher than in Q4 2008 and 62% higher than a year earlier.

3 Ministry of Justice statistics show in Q1 2009 that 22,609 mortgage possession claims were issued (seasonally adjusted), 13% lower than Q4 2008 and 42% lower than a year earlier.

4 Mortgage and secured loan arrears: Adviser and Borrower Surveys April 2009, AdviceUK, Citizens Advice, Money Advice Trust, Shelter.

5 51% of advisers report that mainstream lender's arrears collection practices have improved since the pre-action protocol was established, whereas only 20% of advisers report that sub-prime and second charge lenders' arrears collection practices have improved.

7. This submission describes the problems we continue to see amongst clients, and outlines further action which we believe may be needed to complete and sustain the safety net to support the government's housing policy.

What problems are we seeing?

8. The number of enquiries to the CAB service about mortgage or secured loan arrears has continued to rise. The table below records enquiries from 1 April 2005 to 31 March 2009. Overall we have seen an 86% increase in the number of enquiries on mortgage and secured loan arrears during this period.

	Enquiries about mortgage or secured loan arrears	*% increase*
2005–06	51,350	0
2006–07	57,372	12
2007–08	64,053	12
2008–09	95,342	49

Poor arrears collection practices

9. Citizens Advice had published evidence on why mortgage arrears and repossessions were growing even while the housing market and wider economy were still fairly buoyant. Evidence from Citizens Advice Bureaux clients at that time suggested this related partly to problems in the mortgage market itself, including poor lending decisions and overly aggressive arrears management practices.

10. We continue to see evidence of poor arrears collection practices, particularly amongst sub-prime lenders and second charge lenders. For example:

> A Berkshire CAB saw a 39 year old man who had been made redundant in January and had an outstanding mortgage of approximately £230,000 with a monthly repayment of £1,300 per month from a sub-prime lender. When he lost his job he contacted his lender and kept them in the picture. He managed to pay the February and March mortgage instalments but then fell into arrears of around £2,600. The lender wrote stating that they would seek possession of the property if the arrears were not paid in full. The man was in receipt of jobseekers allowance and would receive help with housing costs 13 weeks after signing on. But the mortgage lender was still insisting on the arrears being cleared immediately.
>
> A single woman sought advice from a CAB in Cheshire reported that because she could no longer maintain payments to her non-priority creditors and had fallen into arrears with mortgage and secured loan. The client told the CAB that she had been working 55+ hours per week in an attempt to maintain payments and relying on family contributions. She had a first mortgage of £81,000, and two secured loans, one for £39,000 and the other for £7,600 on a home worth £125,000. Her credit debts totalled £28,000 and had mostly taken out two to three years ago to support her unemployed ex-boyfriend. The client told the CAB that she had experienced severe problems with the secured lender to whom she owed £7,600. Although she told this lender that she was considering bankruptcy as a way of dealing with her debt problems, they continued to call her every day making threats of recovery action. The calls included calls to her workplace, and debt recovery agents for the lender passed messages for the client to her colleagues.

Default charges

11. Citizens Advice evidence suggests that there are many instances of lenders making unfair default charges for mortgage and secured loans which are in arrears. There are problems caused by unreasonably high absolute amounts charged, and of lenders applying regular monthly arrears charges even when borrowers have been to court and are sticking to an agreed repayment plan. Often these charges are called "arrears management fees" or administration charges. Monthly default or administration charges can range from £25 per month to £115 per month. Interest is also added to these charges. These charges can mean that where a consumer can only afford to offer to pay an amount such as £50 per month towards their arrears, this can be wiped out by the application of the "arrears management fee". The level of the fees varies enormously, and seems to bear no relationship to the likely administrative costs to the firm of handling an account that is in arrears, but where the consumer is making payments, albeit at a lower rate.

12. Furthermore, many lenders are making compulsory charges to borrowers for debt advice before they will negotiate over an arrears plan. For example:

> A CAB in South East Wales saw a 42 year old woman who came to bureau for help with her mortgage with a sub-prime lender. Although she was making current repayments, she was still being charged £50 because she was in arrears. This was causing her further financial difficulty. She had informed the lender of the reasons for her arrears. Furthermore, the lender said that they would send around their debt counsellor and charge the client £100 for this.

13. We frequently have cases where lenders have charged £100 for one of their debt counsellors to visit their customer. The same lender has also charged £35 for phone calls and letters—including £35 to write to a customer to advise them of the date their counsellor would meet them—for which there was a charge of £100. Unless the customer pays this they are effectively unable to conduct negotiations with the company. Where these companies have signed up to Codes of Practice to treat customers in arrears sympathetically and positively or are required by the FSA to treat customers fairly, they are effectively charging the customer simply to have a conversation about delivering on that obligation. There are a myriad of other practices deployed to protract negotiations, meanwhile the debt only enlarges. This includes, for example, rigid terms about the period of time during which arrears must be repaid—making the situation unaffordable for our clients and charges to supply information about the account balance—a mortgage lender has asked for £60 just to tell the customer how much they actually owe. Another mortgage lender has asked Citizens Advice Bureaux to pay a £60 charge in order to deal with them.

14. Citizens Advice believes that such high absolute charges are clearly unfair, and that powers exist under the Unfair Terms in Consumer Contracts Regulations 1999 for the FSA and OFT to take action to ban such charges. Both regulators know this is going on, but need to take a view about fairness of these charges—including the prices being charged—and intervene to stop it happening or diminish the detriment. Earlier this year, we provided the FSA with a dossier of our evidence on this issue. In their thematic review published on 22 June, the FSA found that poor practice was still prevalent amongst sub-prime lenders, and third party administrators collecting arrears on their behalf, including imposing arrears related charges unfairly.[6] The FSA press release states that four firms have been referred for enforcement action, but we have not yet seen a clear public statement that would allow consumers to know what charges would be considered unfair.

Support for Mortgage Interest (SMI) and Mortgage Protection Payment Insurance (MPPI/)

15. We believe that the Government's decision to extend SMI help in the 2009 Budget by reducing the waiting times and increasing capital limits is an absolutely necessary part of a package of measures to keep the level of repossessions to a minimum through this recession. Statistics from the Association of British Insurers (ABI) underline the necessity for these changes, showing that only around 22% of the mortgages taken out in the last half of 2008 were covered by mortgage payment protection policies (MPPI), and only around 17% of all outstanding mortgages were covered by MPPI at the end of 2008.

16. The need for an effective mortgage safety net is not limited to managing this recession, however. Citizens Advice saw increasing numbers of households facing possible homelessness because of mortgage arrears well before the credit crunch, and we believe that reform of SMI support must be an essential underpinning of the Government's ongoing strategy to encourage lower income households into homeownership for the long term.

17. In particular, we are extremely concerned about the introduction of a two year maximum period of SMI support for jobseekers allowance (JSA) claimants. We believe that the proper way to deal with claimant responsibilities and work incentives is through the requirement for people claiming JSA to ensure they are doing all they can to look for work, rather than through an arbitrary limit on housing costs. We believe that the two year limit on housing costs for JSA claimants should be removed immediately.

18. Citizens Advice also warmly welcomed the decision announced in the pre budget report to hold the SMI standard interest rate at 6.08% for six months. This has provided much needed assistance to borrowers on fixed rate mortgage deals. However some borrowers are likely to remain on fixed rate deals for some time after this six month period expires and would fall into significant arrears if the standard interest rate were to revert to 1.58% above base rate (currently 2.08%). Indeed some of these borrowers are paying at rates even above the frozen 6.08% rate as the following case shows:

> A CAB in Derbyshire saw a 56 year old man who had terminal cancer of the oesophagus. He had palliative chemotherapy and was in receipt of disability living allowance under the special rules for people who are terminally ill. He lived alone and had been on incapacity benefit and income support for over two years. He had an interest only mortgage with a sub-prime lender of £120,000 with little or no equity in the house. His mortgage payments were around £650 per month based on an interest rate of 6.54% that was fixed until October 2009. However SMI paid only around £550, the shortfall being due to the standard interest rate of 6.08% and the fact that SMI was paid four weekly rather than monthly. If the SMI standard rate were to drop to 2.08%, the four weekly payments would fall to around £190 and the shortfall on the monthly mortgage payment would grow to around £460 per month.

Landlord mortgage arrears

19. Another serious impact of the recession is that some private tenants are facing the loss of their home, even though they are up to date with the rent, because their landlord is in mortgage arrears. Tenants have very little protection if the lender repossesses the property, and we have seen a 20% increase in homelessness enquiries to bureaux on this issue in the last year. For example:

[6] FSA press release, 22 June 2009.

> A Surrey CAB reported the case of a lone parent with two children who had been renting a property for 10 months. She came back from a holiday to find that the locks had been changed and there was a notice announcing that a possession order had been made. After a two hour wait, a representative from the lenders turned up and let her in under supervision for 10 minutes to collect a few necessary possessions, including her son's GCSE work. The client and her children had been left very upset. She had to make repeated visits to the lender asking for access and for information about when she would be allowed to collect the rest of her possessions. They proved unhelpful and told her they were "unable to contact the necessary person".

20. Citizens Advice and partners have called for changes to give tenants basic protection from eviction when their landlord has defaulted on the mortgage and the lender is seeking possession.[7] We welcome the Housing Minister's statement on 13 May that the Government will legislate "at the earliest opportunity to provide proper and adequate two months notice of eviction for tenants of any necessary move when their landlord is repossessed". We believe it is crucial that this legislation is introduced in the autumn.

The powers of the court to deal with mortgage arrears

21. Over the last 35 years, the percentage of UK homes which are owner-occupied has risen from just under 50% to over 70%. The expansion of home ownership and the current recession means that more people could be exposed to the risks of arrears and repossession. The legislation which protects home owners with mortgage arrears from losing their home, however, has not been updated since 1970. There are also a number of anomalies in the current legislation relating to first and second charge mortgages.

22. For example, borrowers with second charge mortgages which are regulated by the Consumer Credit Act 1974 can apply for a time order which allows the court to reopen the whole agreement, and reduce the interest on the loan to allow the borrower to pay less than the contractual monthly instalment. In comparison, the court has no clear power to let the borrower remain in their home where they are in arrears with a first charge mortgage, but cannot afford to pay the current instalment plus £x off the arrears.

23. These have been further complicated by the interaction between the Financial Services and Markets Act 2000 and the Consumer Credit Act 1974 (as amended by the 2006 Act). It is not clear whether first charge mortgages which are FSA-regulated are subject to the new unfair credit relationship test in the Consumer Credit Act 2006. If the unfair credit relationships test were to apply to all mortgages and secured loans, it would provide a method of tackling some of the detriment borrowers experience such as irresponsible lending, high interest rates, default charges, harsh collection practices, and mis-selling payment protection insurance.

Buy-to-let mortgages

24. For the first time, bureaux are seeing some "amateur" landlords who need advice about mortgages on buy-to-let properties they had bought as an investment. Even though buy-to-let mortgages are arguably an investment product with a potentially open liability, they are not currently regulated by the FSA, and so lenders marketing these loans have not been subject to the FSA's detailed selling and arrears rules. In many of the cases seen by bureaux, it appears that lenders and investment companies have done little to ensure that these landlords understood the risks of the loans they were taking on and to lend responsibly:

> A Berkshire CAB reported that a man had bought two buy-to-let properties as an investment in North-West England. The properties were overvalued, and rent estimates were over-optimistic. One property had never had a tenant, and the client was more than three months behind with mortgage payments, and the lender was seeking possession. The other property was guaranteed to provide a rent of £600 pm for a year, against a mortgage payment of £650, which he had thought he could manage. The client subsequently discovered that the tenant was in receipt of housing benefit totalling £450 per month, and that this was the going rate for rent. There is now a £200 pm gap. The mortgage is fixed for two years, and the fix has one year to run.

> A CAB in London saw a couple who had bought 23 buy-to-let properties with mortgages from eight different lenders, although their income was no more than £1,500 per month. They were buying their own home via a shared ownership scheme. They were finding it impossible to continue to make all the payments to the mortgages, particularly because the interest rate charged on the mortgages were so high, and the properties were empty at times. Two of the properties had now been repossessed, and the remaining 21 had been taken into receivership. The clients had had to leave their own home, which was in negative equity. They were feeling extremely stressed and were considering petitioning for bankruptcy.

[7] A Private Matter? , Crisis, Citizens Advice, Shelter, Chartered Institute of Housing, March 2009.

Charging orders

25. A charging order is a way of enforcing a previously unsecured debt by securing it against the debtor's property. A creditor with a charging order can then apply to the court for an order for sale to recover the debt by forcing sale of the property.

26. Since 2000 there has been a staggering 722% increase in the number of charging order applications by unsecured creditors. Around 74% of the 132,000 applications in 2007 resulted in charging orders being made.[8]

27. But Citizens Advice Bureaux evidence shows that some creditors are using the threat of court action followed by a charging order to intimidate people in financial difficulties to pay more than they can reasonably afford. The growing ease with which creditors are obtaining charging orders is undermining good debt collection practices. It rewards lenders who will not accept reasonable repayment offers from people in financial difficulties who are doing everything they can to deal with their debt problems. For example:

> A Hampshire CAB reported that a 68 year old man sought help with debts totalling £46,000. The bureau helped him make offers to all his creditors on an equitable basis. One of his creditors, a major credit card company, rejected the offer of £99.04 which would clear the debt in nine years. They insisted that they would only accept contractual repayments. If this was not possible, they would take recovery action. The bureau felt that as the client was a homeowner, it was a policy decision to try and get unsecured borrowing secured.

28. On Thursday 25 June, Citizens Advice published its evidence and recommendations concerning the growing use of charging orders by creditors.[9]

Initiatives to tackle mortgage and secured loan arrears

29. We commend the coordinated action of Her Majesty's Treasury (HMT), the Ministry of Justice (MoJ) the Department for Communities and Local Government (CLG) and the Department for Business Innovation and Skills (BIS) in the autumn of 2008 to introduce measures to support people to avoid losing their homes, as well as the active cooperation of the Financial Services Authority (FSA) and the Office of Fair Trading (OFT) and industry bodies including the Council of Mortgage Lenders (CML) to implement complementary rules and guidance.

30. We also welcome consultations on improvements to regulation of secured lending and to ensure responsible lending by the OFT, and believe these should retain and extend current vital protections for consumers in the Consumer Credit Act.

31. Overall, initial indications suggest that the package of measures introduced in late 2008 and early 2009 are making a difference, though there remain some specific features which need to be improved.

32. The most significant factor keeping people in their own homes at the moment is very low interest rates. Negative equity is also likely to have reduced the incentives for lenders to claim possession before trying other avenues.

33. It is too soon after their introduction to say how the individual measures are working and the extent of any remaining gaps in the safety net. Our further research through court desk advisers in July will provide more information on the actions of particular lenders before coming to court, how far particular courts are taking account of lender compliance with the pre-action protocol, and whether there are gaps in the safety net for particular types of people or circumstances.

34. We have made some specific comments on aspects of each scheme below, and we believe that the government's stated intention to review the mortgage safety net when this period of crisis is over remains necessary.

Sale and rent back

35. Citizens Advice has been concerned for some time about the growth of completely unregulated sale and rent back schemes. These allow the borrower to sell their home to a private landlord at a discount and allow them to remain there paying rent as a tenant. CAB evidence suggests that homeowners in a financially and emotionally vulnerable situation end up selling their homes for much less than they are worth, in return for a tenancy that offers little security of tenure. One of the attractions of the schemes for homeowners in mortgage arrears is help with the rent via housing benefit. However, housing benefit rules are complex, and there is evidence showing how scheme providers can overstate the rules of entitlement and the amount of benefit the new tenant will receive:

> A Cheshire CAB reported that a severely disabled man living on benefits sold his home to a sale and rent back company when he fell into financial difficulties. He received about £22,000 for his property, which he used to pay off his debts. The company told him that housing benefit would be available, but the council refused his application. As a result, the client was in an even worse financial predicament than previously and was facing possible homelessness.

[8] Ministry of Justice, *Judicial Statistics 2007*.
[9] Out of order—Citizens Advice evidence on the use of charging orders and orders for sale in debt collection, June 2009.

36. It is very welcome that the Government have taken swift action on our concerns about sale and rent back schemes. Interim statutory regulation of the sector by the FSA will come into force on 1 July 2009, with the full regime coming into effect during 2010.

Homeowner Mortgage Support Scheme (HMSS)

37. We believe that implementation of the HMSS by CLG has been carried out very effectively. Press coverage has highlighted the very small numbers of households helped to date. Nevertheless, bureaux have had over 900 enquiries about the scheme during April and May (its first two months of operation).

38. Evidence from these enquiries suggests that, while interest rates are at such low levels, other aspects of the overall package of lender forbearance measures, requiring lenders to offer a switch to an interest-only mortgage and/or extending the term of the mortgage, may be sufficient for many borrowers. This may not remain the case if interest rates rise, and as unemployment continues to rise.

39. It is early days to judge the success of the scheme, and we believe it remains a good scheme which may well be more widely taken up as the economic climate changes.

Mortgage Rescue Scheme (MRS)

40. Recent headlines have highlighted that only very small numbers of households have been helped by the mortgage rescue scheme, but bureaux received around 800 enquiries about MRS during April and May, and there is evidence that the existence of the scheme is buying time for more bureau clients. For example:

> A West Midlands CAB saw a 34 year old man living with his partner and two children aged two and six years. He had recently become unemployed and was in receipt of jobseekers allowance. Payments towards mortgage interest had not yet commenced. From all sources their total household income was £973 per month. The man had other debts and had seen a CAB debt adviser. He had been referred to his local authority housing department as a candidate for the Government backed mortgage rescue scheme. He was facing eviction because of the mortgage arrears and applied for the warrant to be suspended resulting in a court hearing on the day the eviction was due to take place. The mortgage lender agreed for the eviction to be postponed to give time for the option of the mortgage rescue scheme to be explored.

41. Our survey of advisers in April showed that initial implementation has been mixed overall, with many advisers reporting problems getting clients accepted onto the scheme. In view of these problems, we welcome the Government's announcement in the Budget that the mortgage to rent scheme will apply to those in negative equity.

42. It appears that the sale and rent-back option rather than the equity option is the one being taken up, and this makes the scheme very expensive. So, while we believe it is necessary to have such a scheme in order to have a comprehensive safety net at this crucial time, we believe it is a particularly expensive approach to supporting people and is not a good long-term solution.

Pre-action protocol (PAP)

43. As noted in the introduction, the overall number of possession claims has dropped significantly, though arrears and actual repossessions continue to rise. So the combined effect of lower interest rates, negative equity and the pre-action protocol appears to have been to encourage lenders to take court action as a last resort.

44. There is evidence, however, that the protocol is not generally being observed by sub-prime and second charge lenders, and bureaux continue to see cases where the protocol has not been observed. For example:

> A Yorkshire CAB saw a 53 year old woman who, with her partner, had a reduced income since her partner became unemployed. Their sub-prime lender had agreed that they could pay back just the interest for a period of months. They also had arrears on this mortgage and had an agreement with the lender for £80 repayments per month. But the lender stated in their correspondence that they would be taking court action and were seeking a suspended possession order on this basis. This appeared to go against the mortgage arrears protocol to keep cases out of court. It also appeared to put further pressure on the client. Lastly, it could also be argued that it was against the mortgage conduct of business rules (MCOB) issued by the FSA.
>
> A CAB in Bedfordshire saw a 58 year old married woman who, due to the recession, had suffered a major reduction in her household income. Arrears of £1,997 had built up on her mortgage with a sub-prime lender. The lender had issued a possession claim which stated that they had followed the requirements of the mortgage arrears pre-action protocol. In particular, the claim form stated that they had not been approached by the client offering any repayment plan, and that they did not know anything about the client's circumstances or employment history. The client had looked up the pre action protocol and felt extremely frustrated as she felt the lender had not followed it at all. The client told the CAB that she had been constantly in contact with the lender and they knew all her and her husband's employment history and has explained and sent supporting documentation that she would be able to pay the arrears in the near future from a legacy and three month's backdated pension credit.

45. We also need to be alert to the possibility that the slow-down in possession claims is temporary, as lenders take time to assess the implications of the pre-action protocol, and that possession claims may recover.

Conclusions and recommendations

46. We support the decisive and coordinated approach which the government has taken to put in place a mortgage safety net to help people stay in their homes. The evidence so far suggests that the measures are making a difference overall, though it is too early to judge their impact fully.

47. But people are still losing their homes, and many are still falling through the gaps. Our initial evidence suggest areas in which the package is not yet working well, and court procedures and regulatory rules need to be tightened up. The government's stated intention to review the mortgage safety net when this period of crisis is over remains necessary.

48. We believe it is necessary to improve regulation of secured lending, while retaining and extending current vital protections for consumers in the Consumer Credit Act, and to ensure responsible lending.

49. We believe that court should have the same powers to protect homeowners whether or not the loan is a first or a subsequent charge. These should include:

— Giving the court the power to make Time Orders on all mortgages or secured loans. This would allow the borrower to ask the court to reopen all mortgage agreements and reduce the interest rate for temporary periods of financial difficulty to allow the borrower to pay below the contractual amount.

— Extension of the Unfair Credit Transaction test in sections 140A and B of the Consumer Credit Act 1974 to all mortgages and secured loans to ensure that the court can look into unfair treatment by the lender and take this into account in their decision.

50. Our evidence shows that sub-prime and second charge lenders, in particular, are not complying with existing FSA and OFT rules, and FSA and OFT rules should be more specific about what constitutes unfair practice and irresponsible lending to enable effective challenge of lender practices by consumers and advisers such at Citizens Advice.

51. We also believe it is necessary to improve protections for debtors facing court action for charging orders and orders for sale. The Government should:

— introduce new measures to set minimum financial thresholds for charging order applications and prevent lenders from obtaining orders for sale on consumer credit agreements except in exceptional circumstances;

— make the law clear that orders for sale should only be granted in cases where the debtor wilfully refuses or culpably neglects to pay, or where the judgment creditor would suffer undue personal hardship from non-enforcement of the debt, and bankruptcy legislation should be amended so that creditors can only petition for bankruptcy where the borrower has willfully or culpably neglected to engage with a creditor's demands for payment;

— bring the common financial statement method (or something similar) into the debt collection guidance issued by the OFT under section 25 of the Consumer Credit Act 1974; and,

— implement the debt management scheme provisions of the Tribunals Courts, and Enforcement Act 2007, which would enable debtors to make affordable repayments to their creditors which are binding and would restrict creditors' rights to enforcement action.

52. There is clear evidence of unfair default charges being levied, and we believe regulators should consider firmer action against companies which act in this way. We believe that firms who make these charges should be named and shamed. Firms within groups of banks with a large public interest shareholding should be expected to lead the way. In addition, both regulators should rule decisively that no customer in debt should be charged for having a conversation or correspondence with a company representative with a view to coming to an affordable payment arrangement which avoids the customer losing their home.

53. We believe that the Government should consider extending mortgage regulation to buy-to-let mortgages.

54. Overall, Citizens Advice believes that the policy response from Government and the majority of the mortgage industry to the growing number of households in arrears has been positive and effective. However the current conditions of low interest rates and widespread negative equity give lenders the ability and incentive to provide a wider and deeper range of forbearance options for borrowers in arrears. These conditions may change in the future and unemployment may remain at a high level if job losses continue through the remainder of this year. In which case lenders may have less immediate incentive to show forbearance. We believe that the Government will need to keep a very close watch on mortgage repossessions over the next two to three years and be prepared to intervene to help borrowers again if necessary.

55. So we believe that it is essential for the Government to continue with the current package of measures while mortgage arrears levels remain high, while reviewing the effectiveness of the package as a whole and the individual elements. In the longer term we believe that the system of safety nets for borrowers in arrears needs a fundamental review to ensure that borrowers, and more vulnerable borrowers in particular, will be better protected to deal with a future economic and housing market downturn.

June 2009

Written evidence submitted by the Building Societies Association (BSA)

The Building Societies Association (BSA) represents all 53 building societies in the United Kingdom. Building societies have total assets of £395 billion and, together with their subsidiaries, hold residential mortgages of almost £250 billion, more than 20% of the total outstanding in the UK. Societies hold over £240 billion of retail deposits, accounting for more than 20% of all such deposits in the UK. Building societies also account for about 37% of all cash ISA balances. Building societies employ over 51,500 full and part-time staff and operate through more than 2,000 branches.

Executive Summary

- The current level of interest rates has resulted in lower mortgage payments for many borrowers making it more manageable for borrowers facing temporary financial difficulties, to stabilise their situation.
- Building societies, including subsidiaries, have lower arrears proportionally than the rest of the industry
- The impact of the current unemployment levels has not yet fully fed through into the arrears and repossessions figures. We anticipate a lag effect, with customers likely to experience difficulties in 2010 once they have exhausted redundancy payments and/or savings.
- Building societies are committed to working closely with borrowers in financial difficulty, to help borrowers who are willing to resolve their situation, to stay in their home.
- The preliminary results from BSA consumer research of those in arrears, indicate that a significant percentage of those surveyed managed to repay, or remain in the process of repaying, their arrears. These early results are encouraging and indicate that most borrowers can work successfully with their lender and remain in their home.
- The BSA would call for the Financial Services Authority (FSA) to be clear and concise with the requirements upon firms in relation to arrears and possessions.
- The BSA recognises the very significant financial harm that sale and lease back schemes can cause homeowners, and as such we welcome the intention for them to be regulated by the FSA.
- The BSA would welcome an overhaul to Support for Mortgage Interest (SMI), including an expansion of the criteria to make it available to all loans secured on the property and to be payable at a rate of interest due under the terms of the mortgage contract.
- The BSA believes that a major benefit from all the Government initiatives is that more customers are seeking money advice and/or contacting their lender much sooner in an effort to resolve their situation.
- If house prices continue to stabilise over the coming months, the BSA expects the number of products available at a higher loan to value (LTV) to increase, increasing the number of first time buyers able to gain access to a mortgage.

Report

The current number of homeowners in mortgage arrears and forecasts for the trend in mortgage arrears over the medium term

1. The current economic environment has led to a rise in the number of arrears and repossessions, with numerous forecasts predicting further rises during 2009 and 2010.

2. There have recently been signs of a stabilising arrears environment. Figures from the FSA[1] for Q1 2009, show that new arrears cases[2] fell to 60,000 from 68,000 in Q4 2008.

3. Building societies, including subsidiaries, have lower arrears proportionally than the rest of the industry, as shown in figures compiled by the FSA.[3]

4. The current low level of interest rates has resulted in much lower monthly mortgage payments for many borrowers, making it more manageable for borrowers facing temporary repayment problems, to resolve or stabilise their situation. However, if interest rates start to rise, this could result in an increase in the number of customers in arrears, especially if unemployment remains high.

5. The impact of the current unemployment levels have not yet fully fed through into the arrears and repossessions figures. We anticipate a lag effect, with customers likely to experience difficulties in 2010, once they have exhausted redundancy payments and/or savings. If the labour market remains subdued we would expect to see a higher number of borrowers with arrears in 2010.

The number and characteristics of homeowners who have had their properties repossessed, the number in the process of having their homes repossessed, as well as forecasts for the trend in repossession levels over the medium term

6. The figures released from the FSA also show that the number of repossessions increased by 13% in Q1. More positively, the rate at which repossessions are increasing has slowed over the last two quarters. This could be explained by the impact of the Mortgage Pre-Action Protocol introduced in November 2008 and by lenders offering greater forbearance to customers with payment difficulties.

7. Taking these factors into account, the Council of Mortgage lenders (CML) revised their housing market forecast[4] for 2009 in relation to repossessions, from 75,000 to 65,000. The BSA agrees with the revised forecast.

8. In the building society sector, the general characteristics of customers who are repossessed, are those unwilling to make a realistic arrangement based upon their circumstances and those borrowers that do not contact their lender until their situation has become too serious to resolve. There are also a small proportion of customers who are in a situation where repossession is the most appropriate solution. These are likely to be customers in, or in danger of moving into, significant negative equity, with a significant long term reduction in income. Many societies are also reporting an increase the number of voluntary possessions, which is also reflected in the FSA figures for Q1 2009.[5]

The treatment by and approaches taken, by mortgage lenders towards homeowners in arrears and/or at risk of repossession, including issues relating to the treatment of homeowners by financial institutions specialising in mortgage lending to sub prime borrowers

9. Building societies are committed to working closely with borrowers in financial difficulty, to help those who are willing to resolve their situation, to stay in their home. They also provide support which best meets the individual circumstances of the borrower rather than adopting a 'one size fits all' approach to arrears management.

10. Earlier this year the BSA, working in conjunction with Money Advice Trust (MAT), produced a consumer leaflet,[6] giving straightforward advice on mortgage repayment difficulties. The leaflet provides detailed information about what happens when a customer contacts their lender, with the aim of dispelling some of the urban myths, in particular that making contact with your lender will only accelerate repossession.

11. The BSA were delighted to work with MAT, to ensure that customers with payment difficulties obtain the correct information, to allow them to handle their situation with confidence and come to an arrangement with their lender.

12. Building societies will often agree bespoke payment arrangements with borrowers, based upon their individual circumstances, with the aim of stabilising the arrears position over a sustainable period. Examples of the range of options already being used by building societies include:

— Amending the repayment terms of the mortgage to interest only

— Extending the term of the mortgage

— Reduced payments

— Payment holidays/zero payments

— An arrangement to clear the arrears in addition to the normal monthly payment

— Capitalising the arrears

— Change of payment method

— Change to the date the payment is made

13. The BSA is currently in the process of conducting consumer research, to understand the customer experience in relation to arrears and possessions, across the industry. The preliminary results indicate that the vast majority of those surveyed were offered at least one of the payment arrangements detailed above and a significant percentage of those surveyed also managed to repay, or remain in the process of repaying, their arrears. These early results are encouraging and indicate that most borrowers can work successfully with their lender and remain in their home. The full results from the research are due to be published shortly.

14. Several societies will also have strategies in place to contact customers prior to mortgage payment difficulties arising, by using behavioural scoring analysis and other similar analytical tools. This allows both the lender and the borrower to agree payment arrangements before the situation becomes serious.

15. Building societies have a good relationship with borrowers, especially via their branch networks. They will use that relationship to identify potential repayment difficulties and to develop bespoke repayment solutions that reflect the specific circumstances of the borrower. Many regional societies will also maintain links with major regional employers, so they are able to work with their borrowers who may be at risk of redundancy or reduction in income, on a proactive basis.

Adherence to and the effectiveness of Financial Services Authority (FSA) rules and guidance for mortgage lenders on repossession policy and treatment of consumers in arrears as well as the FSA's regulatory approach in this area

16. The BSA believe that MCOB 13 is broadly sufficient. However, the FSA should integrate the good and poor practice examples into MCOB 13 to ensure that expectations of firms are clear and unambiguous.

17. The good and poor practice examples were released following the Arrears and Possessions Thematic Review in August 2008. Following Part two of the review in June 2009, the FSA released updated examples in relation to fees and charges.

18. The good and poor practice examples are intended as a helpful tool to aid compliance with MCOB 13. However, in some instances the examples create uncertainty as to whether a firm is fully compliant. For example, the good practice examples state that a firm should record telephone conversations with customers who are in arrears. However, no mention is made of this requirement in MCOB 13, or MCOB 2.8 (Record Keeping).

19. The BSA would call for the FSA to be clear and concise with the requirements upon firms in relation to arrears and possessions, with the aim of making existing rules clearer and not by adding additional requirements to MCOB.

20. The regulatory approach to arrears and possessions has been via thematic reviews, as well as a written request to all Chief Executives, to ensure that customers in arrears are treated fairly. The announcement on 22 June 2009, that four firms have been referred for enforcement, with several others under investigation, is disappointing for the industry, but it is positive that the FSA is taking action against firms which have been identified as not fulfilling their regulatory requirements.

Adherence to and the effectiveness of, codes of conduct, protocols and statements of good practice issued by industry bodies in this area

21. The Mortgage Pre-Action Protocol (MPAP) was introduced on 19 November 2008. The protocol aims to ensure:

— the lender and customer act fairly and reasonably with each other, when attempting to resolve arrears

— greater contact between the lender and the customer, in an effort to reach an agreement without the involvement of the court.

22. The protocol does not result in additional requirements for building societies to adhere to, as much of the protocol reflects the existing requirements of MCOB 13. The main impact of the protocol is in relation to evidential requirements, which the lender must be able to provide to the court, to demonstrate the protocol has been adhered to. This provision has the greatest impact on lenders as there is no consistent approach by the courts in this respect. Many building societies use evidence 'checklists'. However, anecdotal evidence from societies suggests that there is no consistent approach by the courts or district Judges in relation to the evidence requirements. Not all courts accept evidence via checklists, some require greater evidence and some ask for none at all.

23. In order to ensure that building societies are able to provide the relevant evidence to the court, the BSA requests that the Ministry of Justice implement a consistent approach which the courts and district Judges adhere to.

24. In relation to industry guidance, the BSA has issued a detailed guide to members in relation to arrears and possessions, which includes the good practice examples issued by the FSA.

25. In addition the BSA will be issuing guidance on specific arrears and possessions issues including, assisted voluntary sales, voluntary possessions and abandonment, shortfall sales and deferring interest. The BSA will also be liaising with Money Advice Trust during the development of these guides for a consumer perspective.

26. We find that industry guidance is well received and is particularly important to smaller societies.

Issues of concern around the operation of sale and lease back schemes

27. The BSA recognises the very significant financial harm that sale and lease back schemes can cause homeowners, and as such we welcome the intention for them to be regulated by the FSA.

28. The BSA does not believe that building societies have provided any significant level of funding to sale and lease back operations. The requirement from societies for independent valuations and legal advice before going ahead with a mortgage application means that it is unlikely that building society are being used for this type of operation.

29. The BSA particularly welcome the requirements contained in the new regulatory regime for people considering sale and rent back to receive independent advice before going ahead with the sale and lease back transaction. For many victims of disreputable sale and lease back schemes talking to their mortgage lender or receiving other third party advice would have seen them able to keep their home on much more equitable terms than that offered by a sale and lease back operation.

30. While the BSA welcomes the intention for these companies to be regulated, for that regulation to be effective it must be properly policed by the FSA. This will require the deployment of a significant resource from the FSA to ensure that they can find unregulated operators. This will not be an easy task, in view of the reliance of many of the less reputable operators on direct approaches to householders, local newspaper classified advertising and adverts in shop windows to get business.

The success of those Government schemes in existence before the financial crisis to support homeowners facing difficulties with mortgage payments and/or at risk of repossession, as well as the effectiveness of initiatives introduced since the financial crisis began.

31. The principal Government scheme in existence prior to the financial crisis, has been Support for Mortgage Interest (SMI). This is a state benefit paid towards the mortgage interest payment, available to homeowners who are also in receipt of income support, Job Seekers Allowance or other income related allowances. SMI is only available for loans taken out to purchase the property, or for specific home improvement loans. As such, borrowers who have taken out second loans for a purpose other than home improvements are not eligible to claim assistance.

32. The BSA welcomed the changes made on 5 January 2009, to expand the benefit to cover loans up to £200,000 and to reduce the waiting period to 13 weeks. However, these changes are not permanent and do not go far enough to make a significant difference to borrowers in financial difficulty.

33. The BSA would welcome an overhaul to SMI, including an expansion of the criteria to make it available to all loans secured on the property and to be payable at a rate of interest due under the terms of the mortgage contract, not as a standard rate set by DWP. Similar recommendations were made in the recent report issued by the Scottish Government's Repossessions Group.[7]

34. The way in which SMI is paid could also be amended, paid on the basis of a grant rather than a benefit, to those borrowers who are not eligible for income related benefits, but who are in need of short term assistance with their mortgage payments. These customers are more likely to be those with an earning potential above an agreed level, whose payment difficulties are temporary. The grant would be repayable at an agreed level once the homeowner is back in employment.

35. We believe that these changes would have a direct impact on the number of people being able to support their mortgage payments and remain in their home until their circumstances improve. However, it is important that changes to SMI can be easily administered by DWP and are also easily understood by customers, lenders and money advisors.

36. On 16 January 2009 the Government launched a Mortgage Rescue Scheme for England, comprising of two options; Mortgage to Rent and Shared Equity.

37. At launch the Government anticipated that 6,000 homeowners would be helped over two years. Since its launch the scheme has been extended to include homeowners in negative equity, which we believe will have a positive effect on the number of homeowners receiving assistance under the scheme.

38. The take up of Mortgage Rescue in England, has so far been extremely low, with only two households being rescued since its launch. At a recent BSA arrears seminar CLG were questioned as to why take up has been so low and why some local authorities were not sufficiently trained, or engaged in the scheme. CLG have admitted that there are still some training needs and operational issues to overcome, which they are working to resolve.

39. The BSA acknowledge that the scheme will inevitably take some time to build and we welcome the acknowledgment from CLG that further work is required.

40. The Homeowner Mortgage Support Scheme (HMS) was launched on 21 April 2009 with all Government backed lenders signing up to the scheme, along with some specialist lenders and one building society.

41. Four other high street lenders, agreed to provide comparable arrangements to their customers. At the same time Nationwide Building Society released their Homeowner Mortgage Charter,[8] and the BSA released their Customer Commitment Statement[9] which is supported by the remainder of the building society sector.

42. The BSA believe it is too early to comment on the success of the scheme. The BSA remain in discussions with CLG with regards to the scheme criteria and reporting requirements, to make the scheme a viable option for building society customers.

43. The BSA believes that a major benefit from all the Government initiatives is that more customers are seeking money advice and/or contacting their lender much sooner in an effort to resolve their situation. The publicity surrounding the schemes has promoted the need to discuss difficulties with the lender. As a result many more customers are receiving assistance with their mortgage difficulties. Whether this is through the Government schemes or through extended lender forbearance measures is largely academic.

44. That said, further work is required by Government to reach out to those customers who are in difficulty, but are not talking to their lender or seeking money advice. As noted earlier, the BSA issued a consumer leaflet in conjunction with Money Advice Trust to explain to customers that contacting their lender does not immediately instigate repossession proceedings.

45. The BSA believe that more work is required to raise awareness among customers, that contacting their lender early is more likely to result in them keeping their home. The increase in voluntary repossessions demonstrates the need for this to happen.

The impact of the credit crunch on access to mortgage finance and the terms on which such finance is offered to first time homebuyers

46. The effective closure of the wholesale markets has resulted in increased competition for retail deposits, especially from firms which are now backed extensively by the Government, which previously raised a large proportion of their funding from the wholesale markets.

47. Building societies are required to have at least 50% of funding from retail deposits, therefore the increased competition from the banking sector, particularly those with explicit state backing, has had a significant impact on their ability to raise additional funds.

48. Combined with the additional liquidity and capital requirements on lenders, this has meant that the amount of funding available for new lending has reduced significantly. As such, lenders have moved to offering products to lower risk borrowers, especially those with a low loan to value (LTV).

49. The decline in house prices also meant that high LTV products were not readily available, with lenders withdrawing products with a LTV of 90% or more, to ensure that they were lending responsibly. With house prices falling on a month by month basis, customers may find themselves in negative equity almost immediately. The increased LTV will also have a further negative impact on the lender's capital requirements.

50. The recent Property Tracker[10] survey from the BSA indicates that consumers expect house prices to rise by an average of 1.4% over the next year. The latest figures from the Nationwide also show a more positive outlook with house prices rising by 1.2% in May and the annual rate of decline improving from—15.0% to—11.3%.[11]

51. However, the BSA survey also showed that consumers remain concerned with the lack of job security. 61% of respondents indicated that this was the biggest barrier to property purchase.

52. In response, many lenders are starting to offer higher LTV products, though potential customers do have to fulfil fairly tight lending criteria.

53. If house prices continue to stabilise over the coming months, the BSA expects the number of higher LTV products to increase, increasing the number of first time buyers who can gain access to a mortgage.

References

[1] Regulated mortgage lenders and administrators are required to submit a Mortgage Lending & Administration Return (MLAR) to the FSA each quarter, providing data on their mortgage lending activities. The figures released from the FSA are based on these returns. http://www.fsa.gov.uk/Pages/Doing/Regulated/Returns/IRR/statistics/index.shtml

[2] Arrears are defined as where the amount of arrears 1.5% or more of the current loan balance.

[3] The FSA compiles building society group level statistics, for use by the BSA and building societies. These statistics are not publicly available; therefore the exact figures have not been quoted.

[4] The CML housing market forecast 2009 http://www.cml.org.uk/cml/publications/marketcommentary/160

[5] Figures obtained from the FSA MLAR return http://www.fsa.gov.uk/Pages/Doing/Regulated/Returns/IRR/statistics/index.shtml

[6] The BSA/MAT consumer leaflet http://www.bsa.org.uk/consumer/factsheets/arrears_leaflet.htm

[7] The Scottish Government Repossession Group Final Report June 2009 http://www.scotland.gov.uk/Publications/2009/06/08164837/0

[8] Nationwide Building Society Homeowner Mortgage Charter http://www.nationwide.co.uk/payment_difficulties/homeowner_mortgage_charter/default.htm

[9] BSA Customer Commitment Statement http://www.bsa.org.uk/mediacentre/press/hmss.htm

[10] BSA Property Tracker Survey http://www.bsa.org.uk/mediacentre/press/propertytrackerjune09.htm

[11] Nationwide House Price Index http://www.nationwide.co.uk/hpi/

June 2009

Supplementary memorandum from the Building Societies Association

Further to the evidence session of Tuesday 30 June, I write to advise you of some changes made to the Homeowner Mortgage Support scheme.

Communities and Local Government (CLG) have been consulting the BSA and a number of other lenders, regarding changes to the reporting requirements under HMS, in order to reduce the burden on smaller lenders. Following these discussions, CLG have indicated that they would be willing to reduce the amount of reporting required for lenders, whose share of the mortgage market is less than 1%. Lenders which fall into this category will not be required to provide weekly or monthly management information. This concession is welcome and we are pleased that CLG have recognised that these changes were required.

I was unable to mention this during the evidence session, as it was unclear whether the introduction of the reduced reporting requirements were finalised and published. I understand that the changes are progressing and CLG are openly discussing the proposed changes with lenders. However, the legal documentation has not yet been amended to formally reflect the changes.

Although the BSA welcomes this concession, we remain of the view that many building societies will remain outside of the scheme. The scheme criteria offers little by way of forbearance which is not already considered by building societies. Many societies are confident that their existing policies will already offer assistance to customers, who may be eligible for HMS. These customers are therefore unlikely to suffer any detriment, as a result of their society not being part of the scheme.

All building societies support the intentions of the Government to help those borrowers who have experiencing financial difficulty, to remain in their homes. This has always been the objective of building societies and will continue to be so, whether that be via a Government scheme, or their own arrears management strategies, supported by the BSA customer commitment statement.

7 July 2009

Written evidence submitted by Which?

RE: MORTGAGE ARREARS AND ACCESS TO MORTGAGE FINANCE

1. Which? is an independent consumer organisation with around 700,000 members and is the largest consumer organisation in Europe. Which? is independent of Government and industry and is funded through the sales of Which? consumer magazines and books. We welcome this opportunity to comment on mortgage arrears and access to finance.

SUMMARY

2. The combination of growing unemployment, falling house prices and failure to pass on falls in interest rates to borrowers is leading to an increase in the number of consumers falling into mortgage arrears and facing repossession. At the same time, the move from "feast to famine" in the mortgage market has led to a shortage of good value mortgage finance for first-time buyers. While we welcome the substantial amount of action already taken and the new Government schemes introduced, Which? believe that lenders, regulators and the Government could do more to help consumers facing difficulties.

Mortgage arrears charges

3. Which? are concerned about the levying of excessive charges on consumers in mortgage arrears. We believe that levying excessive charges on these consumers worsens their financial situation and does not help them resolve it. We believe that:

— The Committee should ask lenders to provide an itemised breakdown of the additional costs their arrears and charges are supposed to cover.

— The FSA/OFT should review all arrears charges made by mortgage providers and secured lenders to determine whether they are reasonable. Any excessive fees should be automatically refunded to the consumer.

— All arrears charges should be suspended if a consumer has made an agreement to pay off the arrears.

— Consumers in discussions with an independent debt advice agency should be given a 90 day charge free window in which to negotiate an arrangement for the repayment of arrears.

— Consumers should be allowed to change their payment date without charge to help minimise the possibility of missing payments or getting into arrears.[10]

— Double dipping of fees (levying a fee for the missed payment on both the current account and the mortgage) where a consumer has a current account and a mortgage with the same bank should be stopped. Requests for Direct Debits should not be automatically re-presented later in the same month unless requested by the customer.

The FSA's regulatory approach

4. The principles-based nature of the FSA's rules and guidance mean that they need to be backed by robust monitoring and enforcement. Which? are concerned that the FSA's approach is not providing a strong enough incentive for lenders to treat customers fairly. We find it extraordinary that the FSA refuses to name the lenders involved because this might damage the dialogue it has with firms, damage lenders commercial interests or lead to unjustified consumer complaints. We believe the FSA should:

— Immediately publish its assessments of which lenders have been performing poorly with regards to treatment of customers in mortgage arrears and repossessions.

— Submit this information to the Judges hearing repossession cases involving these lenders.

— Levy high fines on those which consistently flout the rules. The revenue from these fines should be used to help borrowers access independent debt advice rather than be returned to the industry in the form of lower regulatory fees.

Securitised mortgages

5. Borrowers whose mortgages have been securitised are over twice as likely to be in arrears. Which? believes that it is important that the treatment of consumers in mortgage arrears is determined by the need to treat customers fairly and not by the contents of any securitisation agreement.

Codes of conduct and protocols

6. Codes of conduct and other guidance must have strong independent governance, robust monitoring and strong sanctions. We would like the OFT to conduct mystery shopping to monitor the implementation of its guidance for those providing second charge mortgages. The maximum OFT fine should be increased from £50,000.

Government support schemes

7. It is difficult to judge the success of the Homeowner Mortgage Support Scheme given that it has only just been introduced and no figures are available. However, it remains the case that around 20% of the market is outside of the scheme, including a disproportionate part of the sub-prime market where consumer detriment is likely to be greatest. We would like to see the Homeowner mortgage support scheme made compulsory for those lenders who have not yet signed up to the Scheme or have in place their own equivalent programme of assistance for borrowers. The Government should implement a programme of mystery shopping to monitor how the scheme (and any equivalent programmes claiming to offer the same level of assistance) are being fairly implemented.

The impact of the credit crunch on access to mortgage finance

8. The availability of mortgages has moved from "feast to famine" and it is increasingly clear that the market is not operating in consumers' best interests. Banks have used the lack of competition and falling interest rates to fatten their margins rather than concentrating on providing good value mortgages to first-time buyers and those coming to the end of short-term deals. The availability of 90% Loan-to-Value mortgages of the type needed by first time buyers has declined dramatically and the rates for those which are available are very high. For example, a two-year fixed rate 75% LTV mortgage with Natwest is available at 3.69%, whereas the rate for a 90% LTV mortgage is 6.59%. First time buyers and those coming off existing deals need lenders to increase the availability of competitively priced mortgages for those who are creditworthy but only have a small amount of equity in their home. This means increasing the supply of good value fixed rate or tracker deals for both existing and new borrowers with an LTV of up to 90%. The Government should ensure that its existing guarantee schemes and the lending agreements made by the participants in the Asset Protection Scheme address this issue.

[10] Kensington mortgages states that it does not allow the payment date to be changed: http://www.kmc.co.uk/KMOnline/Customer/PDFs/Frequently%20Asked%20Questions.pdf; Platform charges a £25 fee for changing the payment date: http://www.platform.co.uk/PDF/Tariff_of_Charges_April_09.pdf

The treatment by, and the approaches taken, by mortgage lenders towards homeowners in arrears and/or at risk of repossession, including issues relating to the treatment of homeowners by financial institutions specialising in mortgage lending to sub-prime borrowers

Mortgage arrears fees and charges

9. Which? are concerned that arrears charges are being applied unfairly and are used to enhance lenders' profits rather than being a real reflection of the additional administrative costs involved. Levying excessive charges on consumers in mortgage arrears worsens their financial difficulty and does not help them resolve their situation.

10. As can be seen from the table in Annex A, firms levy a variety of fees and charges on consumers who fall behind with their mortgage payments. Examples of the charges levied include:

— Charges of £25 to £35 for missing a payment/Direct Debit. This could be on top of any fee levied by the consumer's current account provider for missing the payment. Requests for payment could be resubmitted within the same month, resulting in a further set of charges.

— Charges for sending letters/making telephone calls of up to £35 for each occasion. Some limit the number of letters/telephone calls that can be charged for each month. Other banks charge a lower amount for the first letter.

— Monthly administration charge when a consumer is in arrears ranging from £25 to £60.

— Charges are incurred if the lender makes an appointment for the consumer with a debt counsellor or collection agent of up to £150.

— When a lender instructs a solicitor to begin repossession proceedings a further charge may be levied or the monthly arrears charge increased. Further charges will be levied if the property is repossessed and has to be sold.

11. Many (if not all) mortgage arrears charges will be imposed where a consumer is in breach of their mortgage contract. Under the Unfair Terms in Consumer Contracts Regulations 1999 (UTCCRs), contractual terms that require consumers to pay a "disproportionately high sum in compensation" to a business when the consumer is in breach of that contract are void and unenforceable. According to clear guidance issued by both the OFT and FSA, a charge will be "disproportionately high" where it does not reflect a genuine pre-estimate of the direct costs to the business of dealing with that consumer's default, for example, the administrative costs of writing to that consumer regarding the breach. The FSA's Mortgage Conduct of Business (MCOB) rules state that "Any arrears charges must be a reasonable estimate of the cost of the additional administration required as a result of the customer being in arrears."[11] Draft OFT guidance on second-charge lending states that any default or other charges should be limited to what is reasonable, doing no more than covering the lender's necessary administrative costs.

12. While a business can identify an average cost per consumer, the estimated costs cannot include a proportion of the company's overhead costs, nor be a means through which businesses can increase profits or offset costs from other parts of the business. The OFT adopted such an analysis when it ruled on credit card default charges in April 2006.[12]

13. In some circumstances mortgage arrears charges may be imposed where, upon a precise wording of the contract, there is no actual breach of the contract. Such a situation would be similar to that being considered in the current bank charges litigation. This is a case, taken by the OFT, addressing the charges which banks levy when consumers exceed their overdraft limit or a payment is rejected and can be up to £35 each time this occurs. The banks argue that the unauthorised overdraft charges are not imposed upon a breach of contract, but rather they are a fee charged in respect of a service provided by the banks (and so exempt from an assessment for fairness under the UTCCRs). The House of Lords is currently considering the issue, but both the High Court and the Court of Appeal have already ruled that even though there is no technical breach of contract, the charges are not protected from a fairness assessment. Given the charges are imposed in circumstances similar to a default situation, the expectation is that the OFT will in due course find that to be fair, the charges must relate to the direct costs associated with that customer moving into unauthorised overdraft. We would expect such a ruling to be applicable outside the bank charges arena.

14. If the mortgage arrears charges do exceed the reasonable administrative cost then they could be unenforceable. There is already evidence that some lenders have been using these charges to recover unreasonable costs. A senior FSA executive stated in a speech that one lender had used arrears charges to recoup advertising costs.[13] Which? submitted a Freedom of Information request to the FSA, asking for the name of this lender. This request was refused.

15. Levying excessive charges on consumers in mortgage arrears worsens their financial difficulty and does not help them resolve their situation. We believe the following action is necessary:

— The Committee should ask lenders to provide an itemised breakdown of the additional costs their arrears charges are supposed to cover.

[11] MCOB 12.4.1
[12] OFT, Calculating fair default charges in credit card contracts, A statement of the OFT's position, April 2006
[13] http://www.fsa.gov.uk/pages/Library/Communication/Speeches/2009/0512_jp.shtml

— The FSA/OFT should review all arrears charges made by mortgage providers and secured lenders to determine whether they are reasonable. Any excessive charges should be automatically refunded to the consumer.

— All arrears charges should be suspended if a consumer has made an agreement to pay off the arrears.

— Consumers in discussions with an independent debt advice agency should be given a 90 day charge free window in which to negotiate an arrangement for the repayment of arrears.

— Consumers should be allowed to change their payment date without charge to help minimise the possibility of missing payments or getting into arrears.[14]

— Double dipping of fees (levying a fee for the missed payment on both the current account and the mortgage) where a consumer has a current account and a mortgage with the same bank should be stopped. Requests for Direct Debits should not be automatically re-presented later in the same month unless requested by the customer.

Adherence to, and the effectiveness of, Financial Services Authority (FSA) rules and guidance for mortgage lenders on repossession policy and treatment of consumers in arrears as well as the FSA's regulatory approach in this area

16. The FSA's regulatory approach is not providing a strong enough incentive for mortgage lenders to treat customers fairly. Which? are very disappointed that the FSA places the commercial interests of firms above the interests of consumers by refusing to name those lenders which it found treating customers unfairly. Which? believes that the FSA should immediately publish its assessments of which lenders have been treating customers unfairly and be prepared to levy high fines on those which consistently flout the rules. The revenue from these fines should be used to help borrowers access independent debt advice rather than be returned to the industry in the form of lower regulatory fees.

17. The overriding principle of the FSA's rules and guidance requires firms to pay due regard to the interests of their customers and treat them fairly. In relation to the treatment of customers in mortgage arrears and those facing repossession the requirements are amplified in Chapter 13 of the FSA's Mortgage Conduct of Business (MCOB) rules and guidance. In broad terms these require firms to:

— Make reasonable efforts to reach an agreement with the customer on repaying any arrears

— Adopt a reasonable approach to the timescale

— Consider actions such as changing the type of mortgage (from a repayment to interest only), extending the term, or deferring the payment of interest

— Not put excessive pressure on the customer

— Levy reasonable arrears charges which reflect the additional administrative costs involved

— Repossess the property only after all other reasonable attempts to resolve the position have failed

— When the property has been repossessed, market it for sale as soon as possible, obtain the best price that might reasonably be paid and notify the customer of any shortfall and action that the firm might take to recover the shortfall from the customer

18. Which? supports these broad objectives, however, the principles-based nature of the rules and guidance means that they need to be backed by robust monitoring and enforcement. Many consumers in arrears will not be able to switch away from their current lender, be unaware of their rights and be vulnerable to unfair treatment. Consumers have got to be given the confidence that if they do approach their lender they will be treated positively. Our research suggests that only 35% of consumers trust their bank to be sympathetic if they run into financial difficulties.[15] Strong regulation is needed to ensure that customers are treated fairly.

19. The FSA published details of its thematic work into mortgage arrears in August 2008. The review found that particular concerns with specialist lenders including that they:

— Operated a "one size fits all" approach, focused too strongly on recovering arrears according to a strict mandate, without reference to the borrower's circumstances;

— Were too ready to take court action; and

— Had lower standards of systems and controls in place to control mortgage arrears handling, including training & competency arrangements.

20. The review also found issues with firms in general, including that some lenders:

[14] Kensington mortgages states that it does not allow the payment date to be changed: http://www.kmc.co.uk/KMOnline/Customer/PDFs/Frequently%20Asked%20Questions.pdf; Platform charges a £25 fee for changing the payment date: http://www.platform.co.uk/PDF/Tariff_of_Charges_April_09.pdf

[15] 1,974 adults aged 18 to 65 were interviewed online between 11 June and 25 June 2009. They were asked how strongly they agreed or disagreed with the following statement "I trust my bank to be sympathetic should I run into financial difficulty". This referred to all financial difficulties rather than those specifically relating to problems paying their mortgage.

— Could have done more to consider customers' individual circumstances and offer more options to resolve the arrears position;

— Imposed charges in circumstances that could result in the unfair treatment of customers; and

— Did not exercise sufficient oversight of third parties contracted to carry out mortgage arrears and repossessions handling activities on behalf of lenders.

21. Which? submitted a Freedom of Information request asking for the names of the lenders which had performed poorly. We believed that consumers and the judges deciding on repossession cases had a right to know which lenders had been assessed by the FSA as performing poorly and that disclosure would strengthen incentives for customers to be treated fairly.

22. The FSA rejected our request and refused to name the lenders, it upheld its position after our request for an internal review. Which? are very disappointed that the FSA continues to put the commercial interests of firms above the interests of consumers. We are concerned that the FSA's lack of transparency is weakening the incentives for lenders to treat customers fairly. Judges will be hearing repossession cases for these lenders and we believe the FSA should make this information available.

23. The FSA recognised the information would benefit consumers but offered a number of excuses for rejecting our request.[16]

> "Disclosure to the public of the names of the firms with whom we had discussions…would be likely to undermine theirs and other firms" willingness to engage in a dialogue with us and to provide us with information."
>
> "Disclosure could affect [a] firm's brand and reputation in the market in which it operates, thereby making it more difficult for it to win new business."
>
> "the publicity could lead to an increase in complaints from customers which, on analysis may turn out not to be justified, so not only causing additional burdens on the firm but also disappointing customer expectations."
>
> "Section 348 of the Financial Services and Markets Act 2000 ('FSMA') restricts the FSA from disclosing 'confidential information' it has received except in certain limited circumstances (none of which apply here). Confidential information for these purposes is defined as information which relates to the business or other affairs of any person and which was received by the FSA for the purposes of or in the discharge of its functions under FSMA and which is not in the public domain. Any information received by the FSA from the firms regarding their arrears and repossession practices has been received for the purpose of carrying out our supervision of those firms, so falls within Section 348."

24. We do not believe that any of the FSA's excuses stand up to external scrutiny. The FSA has provided no evidence that disclosure of the names of the firms which have been treating customers unfairly would reduce firms' willingness to provide it with information. Moreover, a strong regulator should not be relying on the voluntary disclosure of information in order to do its job effectively. Claiming that the naming of firms not treating customers fairly will lead to increases in complaints or a loss of business to those firms demonstrates the FSA's continual approach of placing commercial interests above the interests of consumers. In any case, hardly any of the specialist lenders are open to making new loans to consumers, with most focusing on managing their existing book of loans.

25. The provisions of Section 348 of FSMA have important gateways which allow the FSA to disclose information in certain circumstances. These include the ability for the FSA to disclose information to third parties to enable or assist the FSA to perform its functions. This allows the FSA to publish information in pursuance to its function of providing guidance, information or advice in order to meet its regulatory objectives such as securing the appropriate degree of protection for consumers. Which? believes that the disclosure of information would help achieve the FSA's objective that consumers in mortgage arrears are treated fairly.

26. In its most recent assessment published on 22 June 2009,[17] the FSA found continuing weaknesses in the way specialist lenders and third party administrators were handling mortgage arrears and repossession. Four firms were referred to enforcement and several more are being assessed for referral. The review found that specialist lenders were still not taking enough account of borrower's individual circumstances, were too ready to take court action, imposed arrears charges unfairly and did not exercise sufficient oversight of third party administrators. The FSA continues to protect the identity of those lenders where poor practice has been found and has not released the names of the firms referred to enforcement.

27. We believe that the excuses for not revealing this information are symptomatic of the cosy relationship the FSA has with the financial services industry. While the Chief Executive has recently been promising more intensive supervision and enforcement and has been stating that people should be "frightened"[18] of the FSA, this rhetoric has not yet been translated into firmer action against firms which treat customers unfairly. Practices will only improve when firms which treat their customers badly suffer damage to their reputation

[16] See FSA responses to Which? FOI requests, submitted separately
[17] http://www.fsa.gov.uk/Pages/Library/Communication/PR/2009/080.shtml
[18] http://www.fsa.gov.uk/pages/Library/Communication/Speeches/2009/0312_hs.shtml

and bottom line. The lack of information also leads to a lack of accountability. It is impossible for outside observers to determine whether the action the FSA has required firms to take to improve their practices has been effective.

28. Which? believes that the FSA should immediately publish its assessments of which lenders have been treating customers unfairly and be prepared to levy high fines on those which consistently flout the rules. The revenue from these fines should be used to help borrowers access independent debt advice rather than be returned to the industry in the form of lower regulatory fees.

Treatment of borrowers whose mortgages have been securitised

29. Which? believes that it is important that the treatment of consumers in mortgage arrears is determined by the need to treat customers fairly and not by the contents of any securitisation agreement. FSA statistics show that borrowers whose mortgages had been securitised are twice as likely to be in arrears as borrowers whose mortgages had not been securitised.[19]

30. In our evidence to the Committee's inquiry into banking we expressed concern that borrowers whose mortgages had been securitised might not be treated fairly. We had "specific concerns that because of the terms in the securitisation agreements borrowers whose mortgages have been securitised and who fall into arrears may be treated less sympathetically than borrowers whose mortgages are held on balance sheet by a balance sheet lender. They may also be restricted from participating in Government rescue schemes."[20]

31. The FSA has now identified "terms in securitisation covenants which could lead to inequitable treatment of borrowers in arrears, by restricting the scope for the lender to exercise flexibility and forbearance, for example by prohibiting an extension of the loan term, or conversion to interest only for a period."[21] We would want to be sure that those administering these mortgages do not adhere inflexibly to the statements that were made in the securitisation agreement or the prospectus/offering circular for the Mortgage Backed Securities. For example, we have seen offering circulars which state that "When the Borrower has missed the second payment, the procedures will usually include taking legal action for possession of the relevant Property and the subsequent sale of that Property. The time involved (assuming the institution of legal proceedings) from the point when a second payment is missed by the Borrower to the Administrator taking possession of the Property may be approximately nine to twelve months."[22]

32. Consumers in the United States have encountered similar problems with the agreements that govern securitisation. In May 2009, President Obama signed the Helping Families Save Their Homes Act (2009) into law. This provided a safe harbour for those administering mortgages which had been securitised to modify mortgage loans at risk of foreclosure by following applicable guidelines issued by the Secretary of the Treasury.[23] This was intended to remove legal obstacles set out in securitisation agreements by giving administrators the ability to conduct reasonable modifications such as changing the type of loan or forgiving interest or principal. Guidelines would be established, which administrators could follow which would protect them from lawsuits claiming that they had not acted in the best interests of investors. However, it is too early to say whether this has been successful in encouraging a more flexible attitude amongst mortgage administrators.

Adherence to, and the effectiveness of, codes of conduct, protocols and statements of good practice issued by industry bodies in this area

33. We are not in a position to judge the adherence to the codes although it would seem that there might not be the desired adherence to the FLA code judging by the evidence provided by the debt advice agencies in their recent research report on mortgage and secured loan arrears.[24]

34. We also have concerns that the CML code allows members to levy charges on mortgages in arrears and continue to do so as long as there is a shortfall on the account even when the borrower is sticking to an agreed repayment schedule for the arrears.

35. Furthermore, adherence to the codes is currently open to interpretation. The code set out that customers should be treated fairly and sympathetically, but the detail may be lacking or give lenders freedom to continue practices which we believe are unfair. In addition, FLA membership is voluntary although the FLA states that 80% of second-charge loans are provided by FLA members, and the code is voluntary with limited consequences for non-compliance.

36. Voluntary codes of conduct can be an effective way of addressing issues of concern but only when the following criteria are met:

— Strong Independent Governance

[19] At the end of 2009 Q1, 6.63% of the securitised mortgage loan book was in arrears. This compares to a figure of 2.93% of the un-securitised mortgage loan book. Source: FSA Statistics on mortgage lending, Commentary, June 2009, Para 18

[20] Which? submission to Treasury Select Committee inquiry on the banking crisis, January 2009, para 34

[21] FSA, press release, 22nd June 2009

[22] https://www.rmacinvestors.com/reports/OC/RMAC%202003-NS4.pdf

[23] S.896 Helping Families Save Their Homes Act of 2009, SEC. 201. Servicer Safe Harbor for Mortgage Loan Modifications

[24] Mortgage and secured loan arrears: Adviser and Borrower Surveys April 2009 Research from AdviceUK, Citizens Advice, Money Advice Trust and Shelter

— Clear objectives including a consumer focus

— Robust Standards

— Transparency

— External Consultation

— Adequate Funding for monitoring and supervision

— Promotion of the scheme

— High take up in the sector

— Effective monitoring, inspection and reporting

— Robust Sanctions

— Adequate redress

37. Failure to meet these criteria renders most voluntary codes ineffective and runs the risk of exacerbating the problem instead of resolving it. Generally, we believe that ultimate protection will have to come from the rules, regulation and guidance set out by the relevant regulators and the way compliance with them is monitored and enforced.

38. We acknowledge that the OFT will shortly publish guidance covering second-charge lending activities which will try and address some of the areas of concern highlighted by us. However, there is currently no mystery shopping carried out by the regulator, and the OFT only has very limited resources in monitoring and enforcing its consumer credit licensing regime. In our response to the OFT's consultation on their financial services strategy we stated that:

> "We would like to see a review of the OFT's capacity to provide more active monitoring of the activities of firms holding a consumer credit licence. We believe that the current economic circumstances are likely to have contributed to a workload for the OFT that is significantly higher than originally expected and that current licence fees are set at a level which is incongruous with the actual workload caused by the regime. Firms will only comply with rules, regulation and guidance if they deem the risk of being caught out high enough to justify the cost of compliance. We would like to see regular thematic reviews and mystery shopping exercises, especially for certain types of firms or products which are giving cause of concerns."

39. In addition to this, we would like to see an increase in the OFT's maximum fine level of £50,000 as we do not believe that this is an adequate deterrent, especially for larger firms.

40. We will also be very interested in seeing and commenting on the FSA's forthcoming discussion paper on regulation of the mortgage market including any proposals related to the regulation of second-charge mortgage lending. We will judge these proposals on the outcome for consumers.

41. *Poor treatment of homeowners—a case study*

In October 2008, Mr and Mrs C were given just 30 days notice that their bank was withdrawing their mortgage and loan facilities. The bank then attempted to start repossession proceedings until Which? intervened, forcing them to hold off until the case had been heard by the Ombudsman.

Mr & Mrs C could not understand why they had been subjected to this treatment. They told Which? that they were not in arrears, although they did have a previous dispute with the bank over two years ago. The bank refused to provide a reason—other than citing "exceptional circumstances".

The Financial Ombudsman (FOS) ruled that the lender should immediately cease all attempts to repossess Mr and Mrs C's home, and that the couple had been subject to "distress and inconvenience". A further appeal by the bank was dismissed.

Mrs C said: "We were very disappointed that it had to go this far—we were always willing to talk to the bank, and wrote letter after letter asking for an explanation. We even offered to pay a year up front! And all we met was a wall of silence.

"We would like to thank our families and friends who have been so supportive, as well as everyone at Which? who have guided us through a minefield of paperwork. Given the outcome of our case, we would very much hope that the bank does not treat anyone else the way that they treated us—we're just glad it's over."

The success of those Government schemes in existence before the financial crisis to support homeowners facing difficulties with mortgage payments and/or at risk of repossession, as well as the effectiveness of initiatives introduced since the financial crisis began

Mortgage Rescue Scheme

42. The £285 million Mortgage Rescue Scheme (MRS) has been operational across England since January 2009. The Scheme is intended to help homeowners who are at risk of homelessness as a result of mortgage repossession AND who fall within a priority need category.[25] It has two elements: (1) the "Government Mortgage to Rent" option which involves a Registered Social Landlord (RSL) purchasing the homeowner's property, enabling the household to remain in the property as a tenant on an assured short hold tenancy, paying an intermediate rent; and (2) the "Shared Equity" option which involves a RSL providing a loan to the homeowner to enable the homeowner's monthly mortgage payments to be reduced.

43. Headline data for January to April 2009, provided by local authorities operating the scheme indicate that 4,202 households approached local authorities with mortgage difficulties in this period (only a proportion will actually be eligible). Only two households accepted an offer through the scheme. However, there were 376 "live" applications at the end of the period.[26]

44. At Budget 2009 it was announced that the MRS would be expanded to include some households previously excluded due to negative equity. Regional property price caps have also been reviewed. These changes came into effect from 1 May. We welcome these changes as evidence from debt advice agencies found that these issues were the two most common problems experienced by clients in accessing the Mortgage Rescue Scheme.[27]

Homeowner Mortgage Support Scheme

45. The aim of the Homeowners Mortgage Support (HMS) scheme is to prevent repossessions, where households suffer a temporary income shock. After taking money advice, homeowners apply to their lenders to join the scheme, which allows them to defer up to 70 per cent of the interest due. Borrowers apply for the HMS scheme through their lender. Official figures on the number of households entering the scheme will be published later this year.

46. From April, the following major high street lenders will offer their customers HMS: Lloyds Banking Group (which includes Halifax, Cheltenham and Gloucester and Bank of Scotland), Northern Rock, the RBS (which includes NatWest and Ulster Bank, the One account, First Active (UK) and Direct Line), Bradford and Bingley, including Mortgage Express, Cumberland Building Society, and the National Australia Bank Group (which includes Clydesdale and Yorkshire Bank).

47. A number of other banks, building societies and specialist lenders have also claimed that they will offer their customers HMS as soon as possible. These are Bank of Ireland (which includes Bristol and West), GMAC, GE Money, Kensington Mortgages, the Post Office and Standard Life Bank.

48. Lenders offering HMS will have the security of a Government guarantee if the borrower defaults.

49. At the same time, four other high street lenders, Barclays (including First Plus), HSBC, Nationwide and Santander (including Abbey and Alliance and Leicester) have all confirmed that they will offer comparable arrangements to HMS to their customers, while opting not to take up the Government guarantee. Customers of these institutions experiencing a reduction in income and willing to make regular monthly payments will receive a similar level of support and be encouraged to seek independent money advice.

50. Lenders covering more than 80% of the mortgage market will now be providing enhanced support to their customers.

51. It is difficult to judge the success of the Scheme given that it has only just been introduced and no figures are available. However, it remains the case that around 20% of the market is outside of the scheme, including a disproportionate part of the sub-prime market where consumer detriment is likely to be greatest. We therefore believe the Scheme should be made compulsory for those lenders who have not yet signed up to the Scheme or have in place their own equivalent programme of assistance for borrowers.

52. We believe the Government should introduce a programme of mystery shopping to monitor how the scheme is being promoted by lenders and how the schemes which claim to provide a similar level of support are operating. The Government and the FSA should also review and remove any obstacles which may stop consumers whose mortgages had been securitised from participating in the scheme.

[25] These comprise: (1) dependent children, (2) pregnant woman, (3) vulnerable due to old age, physical/mental disability/other special reason

[26] Only around three quarters of Local Authorities returned monitoring forms

[27] Mortgage and secured loan arrears: Adviser and Borrower Surveys, April 2009, AdviceUK, CAB, Money Advice Trust, Shelter

The impact of the credit crunch on access to mortgage finance and the terms on which such finance is offered for first time homebuyers

53. It is increasingly clear that the market for mortgages is not operating in consumers' best interests. We recognise that there has to be an adjustment in the cost and availability of credit, but it would be damaging for consumers if we went from "feast to famine". We agree that there should be no return to irresponsible practices of the past such as unjustified self-certification of income, lending six or seven times a consumer's income or 125% of the value of the house. However, while it may be in the interests of each individual bank to cut back on lending if they all do this together it will increase volatility in the housing market and lead to more negative equity and financial difficulty for consumers.

54. The credit crunch has had the following impacts on the mortgage market:

— The closure, nationalisation or takeover of a number of major lenders, leading to a reduction in capacity.

— Mergers and takeovers have led to a significant increase in concentration of the major lenders, weakening competition.

— The closure of the securitisation markets leading to the withdrawal from the market of lenders which relied on the "originate to distribute" business model.

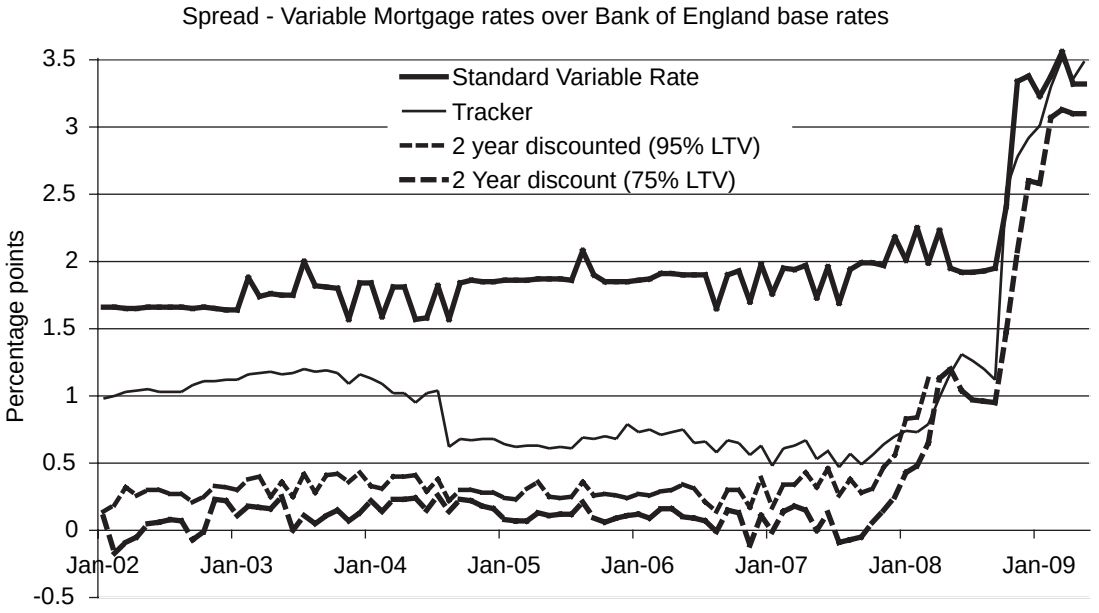
— Increasing loan losses which led to Banks/building societies have become far more risk averse and are concentrating on consumers needing to borrow 60–75% of the value of their property.

— Falling house prices and tightening lending criteria meant that the number of customers able to switch mortgage lender has declined significantly, weakening competitive pressures to keep rates low. Many customers may be stuck with their existing lender and in particular on their lenders Standard Variable Rate (SVR).

— Some banks and other lenders have been unwilling to pass on cuts in the Bank of England base rate and LIBOR to SVRs.

55. The chart below shows the significant rise in margins on tracker and discount mortgages since the start of the credit crunch. It can be seen that the combination of the factors above has led to a significant weakening of competition. Banks have used falling interest rates to fatten their margins, rather than providing good value mortgage finance to first-time buyers and those remortgaging.

Chart 1



The availability of mortgages to first-time homebuyers

56. The availability of 90% Loan-to-Value (LTV) mortgages has declined significantly, with less than one tenth of the products available compared to a year ago.[28] For first time buyers saving a 25% or even 40% deposit will be a significant barrier to being able to buy a house. With an average house price for a first-time buyer of £125,000,[29] buyers would need to find a deposit of £31,000 to £50,000, while in London this would rise to between £51,000 and £82,000. On top of this they would need to pay solicitors and surveyors fees and other moving costs, although outside London they would not have to pay Stamp duty.

[28] Bank of England, Trends in Lending, June 2009, page 9
[29] Nationwide, Q1 2009

57. Those 90% LTV mortgages which are available are at a significantly higher margin above base rates and other wholesale rates than previously. Rates charged are also substantially higher than the cost of 75% Loan-to-Value mortgages. The tables below shows the interest rates charged by major lenders at various LTVs. They show that there is a substantial higher interest rate charged at 90% LTV. For example, Natwest has a 2 year fixed rate mortgage available at 3.69% for a borrower with a 75% LTV mortgage. Those first time buyers needing a 90% LTV mortgage will pay a rate of 6.59%, almost three percentage points higher. We believe the Committee should question the banks as to why rates for first time buyers needing a 90% LTV mortgage remain so high.

Quoted Mortgage Rates on Offer from 6 Major Lenders[30]

Natwest	*2-year fixed*
75% Loan-to-Value	3.69%
85% Loan-to-Value	5.69%
90% Loan-to-Value	6.59%

Halifax	*2-year fixed*	*Tracker*
60% Loan-to-Value	4.59%	3.49%
75% Loan-to-Value	4.69%	3.74%
85% Loan-to-Value	6.84%	4.94%

Northern Rock	*2-year fixed*	*5-year fixed*
65% Loan-to-Value	4.19%	5.29%
75% Loan-to-Value	4.49%	5.79%
85% Loan-to-Value	6.59%	6.99%

Abbey	*3-year fixed*	*5-year fixed*
70% Loan-to-Value	4.58%	5.09%
75% Loan-to-Value	4.89%	5.29%
85% Loan-to-Value	5.74%	5.74%
90% Loan-to-Value	N/A	6.89%

Nationwide	*2-year fixed*	*3-year fixed*	*5-year fixed*
60% Loan-to-Value	4.18%	4.78%	5.68%
75% Loan-to-Value	4.58%	4.98%	5.98%
85% Loan-to-Value	6.44%	6.03%	6.88%

HSBC	*2-year fixed*	*5-year fixed*	*Tracker*
75% Loan-to-Value	4.09%	4.99%	2.95%
90% Loan-to-Value	5.99%	6.29%	4.59%

58. We have compared the cost of borrowing 75% of the value of a house, against the cost of borrowing 85%–90%. This allows us to estimate the marginal interest rate charged on the additional 10–15% of the value of the property. This analysis shows that first time buyers are paying a very high price for needing to borrow the additional amount. In some cases the marginal interest rate is over 20%. We question whether such high marginal interest rates are justified by the higher risk involved.

[30] Source: Providers web-sites. Rates correct as at 28 June 2009

Chart 2

2 year fixed rate - Marginal interest rate on additional 10-15% of the value of the property

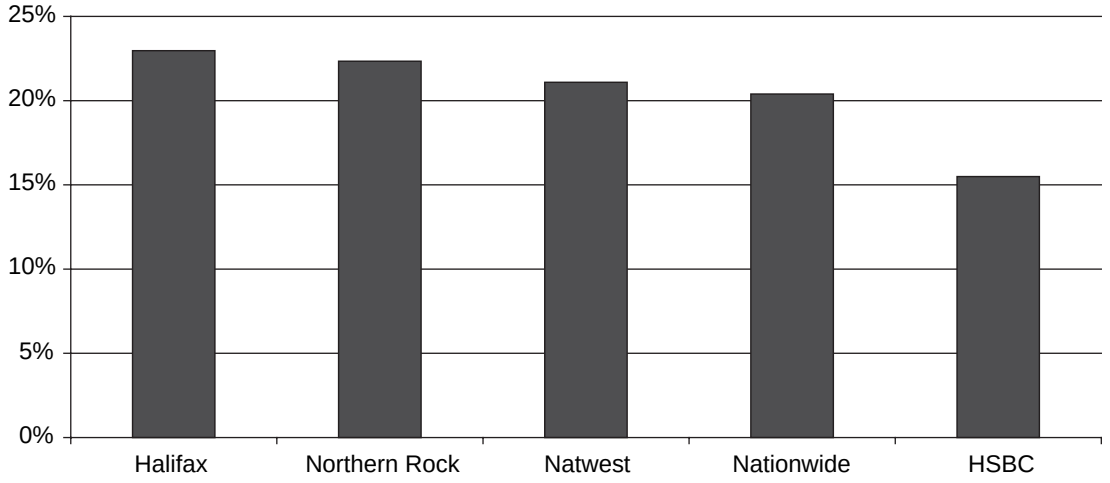
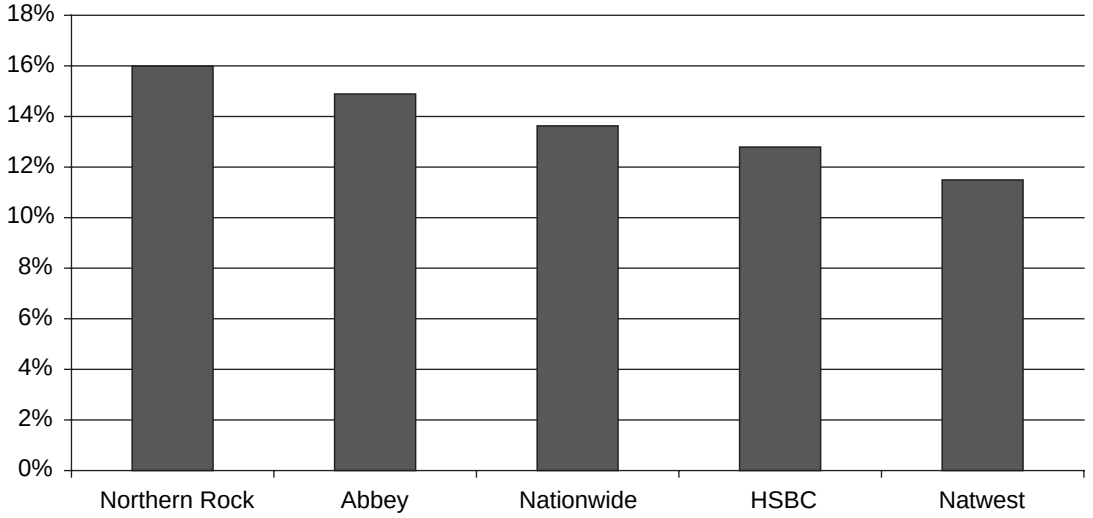


Chart 3

5 year fixed rate - Marginal interest rate on the additional 10-15% of the value of the property



59. First time buyers and those coming off existing deals need lenders to increase the availability of competitively priced mortgages for those who are creditworthy but only have a small amount of equity in their home. This means increasing the supply of good value fixed rate or tracker deals for both existing and new borrowers with an LTV of up to 90%. This would also have an additional benefit in that more deals in the market would enhance the competitive pressures for lenders to keep Standard Variable Rates low.

60. Banks have claimed that the shortage of 90% LTV mortgages has been caused by the Basle capital adequacy requirements. If the capital requirements are a barrier to offering 90% mortgages then these could be addressed by implementing an insurance scheme for lenders, whereby for a fee the Government could insure the additional risk of a 90%, versus say a 60%–75% mortgage. An alternative solution would be for the Government's existing measures such as the lending agreements, Credit Guarantee Scheme or Asset-backed Securities Guarantee Scheme to specifically address this issue.

61. At this stage, it is not clear whether the lending agreements made by RBS/Natwest and Lloyds banking group will be successful in addressing the shortage of mortgages for first time buyers. Lloyds banking group indicates that £3 billion will be made available to mortgage borrowers "within their current lending criteria".[31] RBS has promised to commit an additional £9 billion for mortgage lending to "homeowners … who meet RBS" ordinary course credit and pricing criteria on RBS' normal commercial terms".[32] Following the changes to its strategy, Northern Rock has developed plans to expand mortgage

[31] http://www.lloydsbankinggroup.com/media/pdfs/investors/2009/2009Mar7_LBG_APS_Presentation.pdf ; Slide 9
[32] RBS, press release, HM Treasury Asset Protection Scheme, 26 February 2009

lending by up to £5 billion in 2009 and a total of £14 billion over the next two years.[33] While we welcome these commitments, we note that it is important they are properly monitored and enforced. If these commitments are to be helpful in increasing the availability of mortgage finance for first time buyers it is vital that they make appropriate mortgages available at 90% LTV. It will not help first time buyers if the additional lending under these agreements is only concentrated on those with substantial amounts of equity in their homes remortgaging from other providers which are winding down their business and exiting the UK market.

Tracker mortgages

62. We are concerned that some first time buyers may take out tracker rates at very high margins above base rates and be unable to afford the repayments if interest rates were to rise significantly. For example, Halifax are promoting their first time buyer tracker mortgage which tracks at 4.44% above base rate by saying that "If you want to take advantage of interest rates if they go down, a tracker mortgage could be the perfect deal for you. Remember that interest rates can go up."[34] It is clear to us that the base rate is extremely unlikely to be cut further, but no one can predict when or how fast interest rates may return to their long-run average. Even if base rates were to return to their previous 50 year low of 3.5%, the consumer would end up paying a rate of 7.94%.

June 2009

[33] Northern Rock, Trading statement, 23rd April 2009
[34] http://www.halifax.co.uk/mortgages/first-time-buyer-tracker-75LTV.asp

Annex A

MORTGAGE ARREARS FEES

We have produced a table of five types of mortgage arrears fees charged by lenders. These have been sourced from a combination of the relevant lenders' websites and the Defaqto database. Further charges would typically be levied to cover the actual cost of repossession, management of the property and the eventual sale.

Bank/Sub-Primelender	*Unpaid Direct Debit/Standing Order/Cheque*	*Monthly arrears fee*	*Arears letter [sending a letter or default notice to the customer/general correspondence]*	*Visit of debt counsellor or collection agent*	*Arrears arrangement broken*	*Instructing Solicitors/ collection costs*
West Bromwich[1]	£35	£35	£20	£150	£40	£100
Britannia[2]	£20	£25		£92		£55 Referral to collections department; £50 for giving formal notice of intention to litigate; £115 litigation fee;
Kent Reliance[3]	£35		£25 per item up to £75 per month	£150		Instructing, litigation proceedings and letter before action £100.
Principality[4]	£33		Arrears Letter—monthly charge £30		£25	Arrears summons preparation fee £100
Skipton building society[5]	£25	2% of the amount of the arrears each month up to a maximum of £100 per month. [eg if in arrears for £1,500 then charge would be £30 a month]				Varies

Bank/Sub-Primelender	*Unpaid Direct Debit/Standing Order/Cheque*	*Monthly arrears fee*	*Arears letter [sending a letter or default notice to the customer/general correspondence]*	*Visit of debt counsellor or collection agent*	*Arrears arrangement broken*	*Instructing Solicitors/ collection costs*
Halifax[6]	£35		1st letter free. Each further letter/ telephone call £35	£100		£125
Nationwide[7]	£27.50	£20 [Charged if account is one or more months in arrears and there is no agreement to repay]	£10	£95 (described as an arrears visit)		£150 summons fee; £240 solicitors pre-enforcement litigation costs
Lloyds TSB[8]	£31		£10 for first letter, £31 for second letter	£94 (described as home visit)	£36	£206 for third stage/ pre litigation
Abbey[9]	£32	£35		£79.90		£195 Instruction and £70.50 processing fee
RBS/Natwest	£35	£25	£25	Unknown		Unknown
Barclays/Woolwich[10]	£27.50	£40				£100 Instruction fee £100 Instruction and £100 Enforcement fee
Bradford & Bingley[11]	£35	£25				Issue proceedings from £35 Instructing solicitors £300
HSBC[12]	£25	0.5% of amount in arrears from second month.	First month counted as missed payment. Second month into arrears so letter sent but not charged.			No set cost. Dependant on individual circumstance, fee set by solicitor.

Bank/Sub-Primelender	*Unpaid Direct Debit/Standing Order/Cheque*	*Monthly arrears fee*	*Arears letter [sending a letter or default notice to the customer/general correspondence]*	*Visit of debt counsellor or collection agent*	*Arrears arrangement broken*	*Instructing Solicitors/ collection costs*
Northern Rock[13]	£30	£25 a month if two months or more in arrears. £55 a month if more than three months in arrears		Varies—"depending on the level of help you need"		Varies
Scottish Widows[14]	£25	£30			£20	Unknown
GMAC[15]	£30	£50		£100		£100
GE Money[16]	£25	£40	£30	£86.25, £46 for refusal/no contact or cancellation after 4 working days from instruction		Variable
Kensington[17]	£25	£50				Unknown
Capstone[18] (Preferred and Southern Pacific mortgages)	£25 [Late payment]	£60—rising to £115 a month when they have instructed a solicitor		Varies		£115 per month when they have instructed a solicitor + additional variable solicitors fees
Rooftop	Unknown	£50 per month—was previously £75 per month[19]	Unknown	Unknown		Unknown
Beacon[20]	£30	£50		£100 or £57.50 if it is cancelled		

Bank/Sub-Primelender	*Unpaid Direct Debit/Standing Order/Cheque*	*Monthly arrears fee*	*Arears letter [sending a letter or default notice to the customer/general correspondence]*	*Visit of debt counsellor or collection agent*	*Arrears arrangement broken*	*Instructing Solicitors/ collection costs*
CHL mortgages[21]	£25	£50	£10 per letter (max two letters per month)	£95		£75 for preparing solicitors pack + additional legal costs
Platform[22]	£30	£40 late payment fee if a monthly repayment remains unpaid in the month following the due date.		Variable		Variable

NOTES:

[1] http://www.westbrom.co.uk/static/Tariff_of_Charges.pdf

[2] http://www.britannia.co.uk/home/mortgage/service_station/fees1.html

[3] http://www.krbs.com/pdfs/KRBSFeesandcharges31oct08.pdf

[4] http://www.principality.co.uk/pdf/FCA5%20WEB.pdf

[5] http://www.skipton.co.uk/mortgages/pdfs/mortgageTariffOfCharges.pdf

[6] http://www.halifax.co.uk/mortgages/mortgagefees.asp

[7] http://www.nationwide.co.uk/NR/rdonlyres/5DD01740-40C1-4B3F-B1B9-22183BF22357/0/M628Feb20082.pdf

[8] http://www.lloydstsb.com/mortgages/mortgages_charges.asp

[9] http://www.abbeyforintermediaries.com/library/lib_33.pdf

[10] http://www.personal.barclays.co.uk/PFS/A/Content/Files/Residential_tariff_charges_Mar09.pdf

[11] http://www.bradford-bingley.co.uk/_img/mortgages/LENDING_TARIFF_OF_CHARGES_cropped_HI_FP_130807.pdf

[12] From telephone enquiry to Mortgage Service Center.

[13] http://www.northernrock.co.uk/downloads/TariffOfMortgageFees.pdf

[14] http://swliterature.becomeinteractive.co.uk/content/sw/docs/public/41541.pdf

[15] http://www.gmacrfc.co.uk/about_your_mortgage/tariff_of_charges

[16] http://mortgage.gemoney.co.uk/en/images/1654103_1240838145_GUIDETOFEES.pdf

[17] http://www.kmc.co.uk/KMOnline/Customer/PDFs/Tariff%20of%20Fees.pdf

[18] http://www.capstonemortgageservices.co.uk/capstone/pdfs/Tariffs/74482_PML_Charges_9.pdf

[19] Telephone enquiry

[20] http://www.beaconhomeloans.co.uk/media/documents/pdf/literature/FeesAndCharges.pdf

[21] http://www.chlcommercial.co.uk/Downloads/tariffmortOct07.pdf

[22] http://www.platform.co.uk/PDF/Tariff_of_Charges_April_09.pdf

Written submitted by the Council of Mortgage Lenders

EXECUTIVE SUMMARY

— Lenders are showing very high forbearance to their customers. There are a number of measures in place to ensure that possession is a last resort.

— The vast majority of people who face temporary difficulties and talk with their lender successfully work with their lender to stay in their homes, and get their mortgage back on track over time. Where borrowers contact their lender early, maintain good communication and are committed to paying what they can afford and resolving their arrears, lenders work hard to help wherever the household's future prospects look feasible.

— Despite the rigorous efforts of lenders to show forbearance to their customers because of the economic climate we anticipate a further increase in arrears and possessions in 2010. The weak economic outlook means that a significant minority of those in difficulty will defer rather than resolve problems. We believe that relatively high levels of default could continue for some time as the effects of further job losses continue to feed through.

— Although reported figures for mortgage rescue and homeowner mortgage support seem low at this stage one of the prime benefits of these schemes is the increase in borrower engagement with lenders and/or the advice sector.

— There is scope for further assistance to borrowers by government. These include:

— further reforms to income support for mortgage interest;

— a targeted visible advertising campaign informing borrowers of the help available and encouraging contact with lenders/free advice providers;

— assistance to the housing market through changes to the stamp duty regime; and

— a simplification of low cost home ownership schemes..

INTRODUCTION

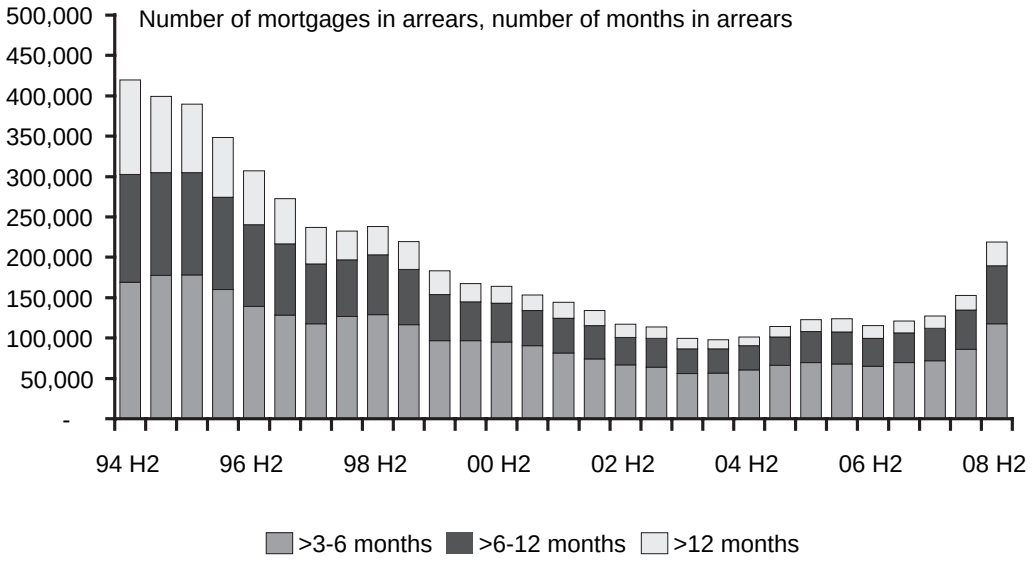
1. The Council of Mortgage Lenders (CML) is the representative trade body for the mortgage industry in the UK. Our 136 members account for 98% of the assets of the mortgage market, and their activities encompass all forms of housing tenure—home-ownership, low-cost home-ownership, buy to let and private and social rental. We are pleased to give written evidence to the Committee.

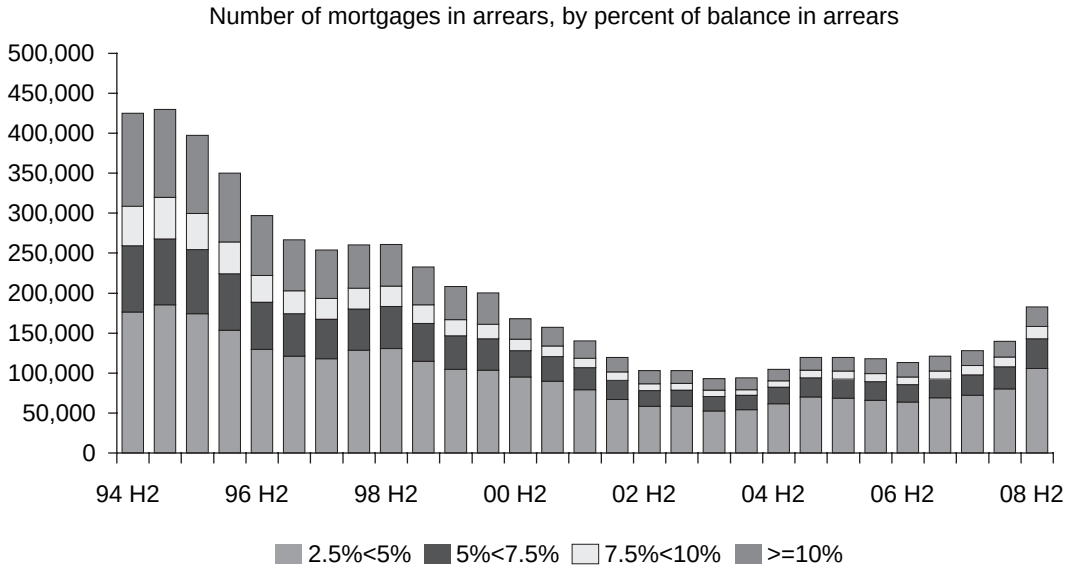
The current number of homeowners in mortgage arrears and forecasts for the trend in mortgage arrears over the medium term

2. The CML's arrears figures are estimates of arrears on first charge loans held by CML members. An explanation of our figures is set out in item 1 of the annex to this paper.

3. In May we reported that the number of mortgages in arrears continued to rise. Our usual "number of months" measure (calculated by dividing the total outstanding arrears by the current monthly payment) has been distorted through the low interest rate environment and is not truly representative of the arrears position at present. The alternative measure, showing arrears as a percentage of the total outstanding mortgage balance, currently gives a truer reading of underlying changes.

4. The graphs below show this effect, and how the "three months" and "2.5% balance" figures have diverged recently.





5. In Q1 of 2009 the number of loans with arrears of more than 2.5% of the mortgage balance rose by 12% from 182,600 in the fourth quarter of 2008 to 205,300 in the first quarter of this year (62% up on the 127,000 in the first quarter of 2008). For more information see the tables in the annex to this paper.

6. In our recent revised forecast we stated that we expect a further deterioration in the number of borrowers falling behind in their payments. But this will be at a slower pace than anticipated, largely due to the low interest rate environment.

7. We now expect 360,000 borrowers to be in arrears of 2.5% or more of the balance of their mortgage at the end of this year, up from 183,000 at the end of last year. The impact of lower interest rates means that the number of mortgages more than three months in arrears is expected to rise to around 425,000 —up from 219,000 at the end of last year, and compared to our earlier forecast of 500,000.

8. Anecdotally our members report that one of the main challenges for borrowers is reduced income rather than a complete cessation of income through unemployment. Lenders do not believe that the impact of unemployment has yet been significantly reflected in the arrears experience. We have not issued a forecast for 2010 but given negative expectations about unemployment and the possibility of an interest rate rise we would not anticipate a reduction in the number of customers having difficulties making payments in the medium term

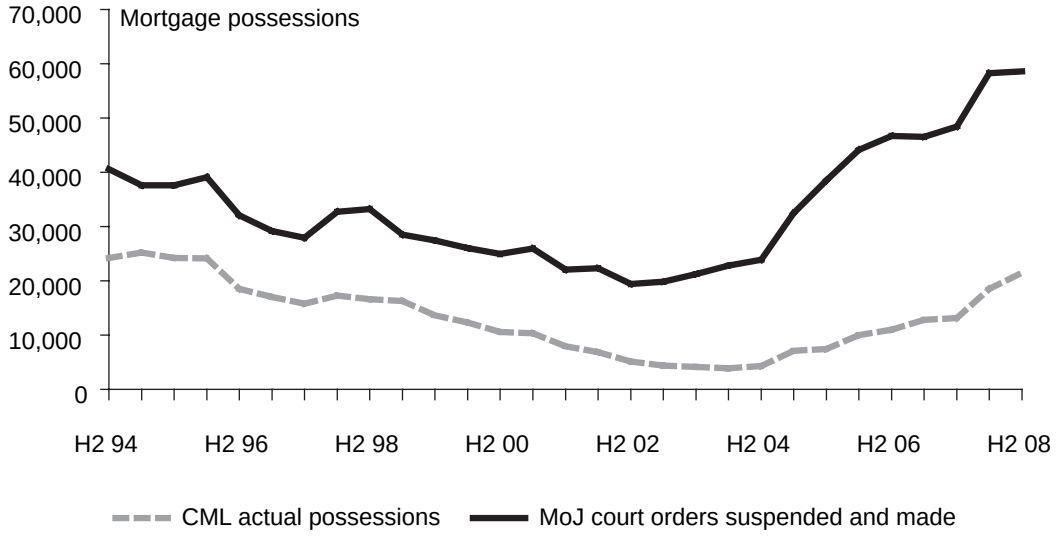
The number and characteristics of homeowners who have had their properties repossessed, the number in the process of having their homes repossessed, as well as forecasts for the trend in repossession levels over the medium term

9. We do not collect data on the characteristics of homeowners subject to possession proceedings.

10. In 2008 we had estimated that the total number of properties taken into possession would be 45,000. The actual outturn figure was some 5,000 less with 40,000 repossessions in the year which equates to 1 in every 290 mortgages

11. Our initial forecast for this year was 75,000 actual possessions. As a result of the lower interest rates slowing the fall into arrears and allowing extra scope for lenders to show forbearance, we have lowered our forecast for the number facing possession this year to 65,000 from the estimate of 75,000.

12. The following graph shows the divergence between the possession orders and actual possessions.



13. The large difference between the numbers of court orders and actual possessions illustrates the fact that lenders continue to explore workable options for addressing a borrower's payment problems, even after obtaining a court order, right up to the point of possession. A possession order does not equate to actual possession.

14. The fact that there were 11% fewer repossessions than expected in 2008, despite a worsening economy and rising unemployment, demonstrates that mortgage lenders are making strenuous efforts to ensure that repossession really is a last resort.

15. However even with high levels of lender forbearance and low interest rates, as with arrears we anticipate a further increase in possessions in 2010. Forbearance may in some cases be delaying or exacerbating the problem.

The treatment by, and the approaches taken, by mortgage lenders towards homeowners in arrears and/or at risk of repossession, including issues relating to the treatment of homeowners by financial institutions specialising in mortgage lending to sub-prime borrowers

16. All first charge loans over residential property entered on or after 31 October 2004 are regulated by the FSA. Under FSA regulation, lenders are obliged to follow a regulatory framework set out in the Mortgage Conduct of Business (MCOB). The FSA's rules on arrears and possessions are in MCOB 13.

17. The FSA regulatory framework is backed up by the Financial Services Ombudsman service which allows borrowers to complain to the Ombudsman if the borrower considers that he has been treated unfairly by the lender. The service is at no cost to the borrower.

18. In addition to the overarching regulatory principle requiring lenders to treat their customers fairly, MCOB 13 specifically requires a lender to deal fairly with a customer in arrears. Most importantly MCOB 13 stipulates that lenders should only repossess the property where all other reasonable attempts to resolve the position have failed.

19. Lenders are required to have written policies in place to evidence that they are dealing fairly with customers in arrears and the rules set out issues that should be covered in lenders' policies together with detailed requirements on behaviour by lenders.

20. Compliance with this regulatory requirement is the basic approach taken by lenders —that is possession is the last resort. Lenders try very hard to engage with customers to show forbearance. However any change to the mortgage contract requires consent from the borrower so lenders can only assist when the borrower makes contact with the lender. Lenders go to great lengths to make contact with borrowers but there are some borrowers who are just not willing to engage.

21. In addition to compliance with regulation, many lenders have taken on their own initiatives to assist customers. Many have given undertakings not to go to court within specified time periods. Many lenders are actively supporting schemes such as the mortgage rescue scheme and the homeowner mortgage support or its equivalent. Lenders have reviewed their correspondence with borrowers to ensure that borrowers understand the process better.

22. Many lenders have actively sought to ensure that borrowers receive independent free debt advice. They have created links and hot keying facilities to advice providers such as the Consumer Credit Counselling Service and Payplan. Several of our members are taking part in a Ministry of Justice pilot scheme to assess the benefits of advice and meditation in possession claims.

23. First charge sub—prime lenders are subject to exactly the same regulatory regime as mainstream prime lenders and the approach of sub prime lenders is therefore subject to the same requirements as other first charge lenders. The nature of specialist lending is by definition more risky than prime lending and this risk factor is taken into account by lenders.

24. The vast majority of people who face temporary difficulties and talk with their lender successfully work with their lender to stay in their homes, and get their mortgage back on track over time. Where borrowers contact their lender early, maintain good communication and are committed to paying what they can afford and resolving their arrears, lenders work hard to help wherever the household's future prospects look feasible.

Adherence to and the effectiveness of, Financial Service Authority (FSA) rules and guidance for mortgage lenders on repossession policy and treatment of consumers in arrears as well as the FSA's regulatory approach in this area

25. We believe that adherence to the FSA's rules (TCF and MCOB 13) by mortgage lenders is prevalent. Lenders have compliance functions in place to ensure this.

26. The FSA's rules are very comprehensive and effective and aim to strike a fair balance between the consumer and the lender. The rules cover procedures adopted when handling arrears and possessions, the subsequent sale of a property in possession, the records lenders must keep, the information that must be provided to customers, and the recovery of any outstanding (shortfall) debt.

27. In order for the rules to be effective they need to be policed and enforced effectively and we are unconvinced that the FSA has performed well in its role as regulator in this respect.

28. In 2008 the FSA carried out a thematic review of lenders' practices in arrears and possessions. This was a wide ranging review that looked at 13 firms (accounting for 24 brands). The FSA found that mainstream lenders are largely complying with the FSA's requirements and have policies and practices in place that ensure customers are treated fairly. This indicates that the rules are both effective and are substantially being adhered to.

29. We recognise that in its first thematic the FSA identified some areas for improvement and the need for further work particularly in the specialist lender sector and we have worked with lenders on this through the guidance referred to below.

30. The second part of the thematic was published recently and shows some areas of concern in the specialist lending sector.

31. In our view any legitimate findings of poor practice identified by that work should be rectified. However one difficulty with the thematic approach is that all lenders within a particular sector are tainted by findings regardless as to their individual performance. More effective, regular, in firm monitoring would be fairer and more efficient than the blanket approach of thematic reviews.

32. In the past there has not been a direct link between regulatory requirements and the court possession process. This position has changed since the judiciary introduced the pre-action protocol for possession claims based on mortgage arrears in November 2008. Also as already mentioned the Financial Ombudsman jurisdiction is in place to ensure fair treatment of borrowers. So in addition to the regulatory regime there are two separate ways of ensuring compliance with that regime.

Adherence to, and the effectiveness of, codes of conduct, protocols and statements of good practice issued by industry bodies in this area

33. The pre-action protocol came into existence in November 2008. It was broadly welcomed by lenders as it allows lenders to demonstrate that they are complying with their regulatory requirements. For the majority of lenders, the protocol was simply a case of formalising a process which they already had in place. We believe that protocol is extremely effective. Adherence is not optional as it is tested by the court.

34. As far as codes of conduct are concerned following the publication of the first part of the thematic the CML published industry guidance on arrears and possessions handling. This expands on TCF, existing MCOB rules and other issues raised by the FSA and the FOS and was welcomed by the Financial Services Authority (FSA) and by consumer groups. We understand that it has been widely adopted by members and that members have undertaken gap analyses between the guidance and their arrears policies.

35. Some years ago the CML issued guidance on mortgage shortfall. That guidance effectively limits the time limit for pursuing shortfall to six years from twelve years. As with the arrears and possessions guidance adherence is voluntary but we understand that this is followed by our members and we believe it is used as a benchmark by the FOS.

Issues of concern around the operation of sale and leaseback

36. The CML recognised the potential consumer detriment as a result of the sale and rent back market and led the call for regulation of this sector. We very much welcome the fact that the government has committed to do this and has introduced a regime relatively speedily.

37. One of the real problems with these products from a lender's perspective is the difficulty in identifying them and distinguishing them from other mortgage transactions.

The success of those government schemes in existence before the financial crisis to support homeowners facing difficulties with mortgage payments and/or at risk of repossession, as well as the effectiveness of initiatives introduced since the financial crisis began

38. It would be difficult to attribute success to any of the government schemes to help homeowners facing difficulties before the financial crisis. Engaging with government on the ineffectiveness of the safety net prior to the financial crisis was challenging.

39. Reliance on private mortgage protection insurance was seen as the main form of support. However takeup of such insurance has been low and take up was to some extent tainted by the enquiries by the Competition Commission and the FSA.

40. As far as initiatives since the financial crisis are concerned we welcomed the changes to income support to mortgage interest. We had been campaigning for reform to this benefit for some time. In particular, we welcome the reduction of the waiting period down to three months. This greatly enhances a lender's ability to show forbearance. We believe that this should be introduced as a permanent measure

41. However we do not think the changes go far enough. Access to ISMI should be much more widely available at the point of need by households experiencing payment difficulty due to a partial loss of income. It could also be extended to cover the interest actually being paid by borrowers. The additional cost of this could be offset by taking a second charge on the property, so that any benefit paid to borrowers could be recovered over time. The self-employed are a group where help now seems to be lacking.

42. Mortgage rescue is widely supported by lenders. The change to include customers in negative equity is welcomed and was called for by the CML. We are aware that reported take-up seems to be low at present but the number of parties involved means that the process is slow and we understand that there are a significant number of cases in the pipeline.

43. The Homeowner Mortgage Support Scheme has been supported by a number of lenders. Others have decided that the scheme is not appropriate or have decided to offer their own equivalent forbearance scheme.

44. The scheme remains complex for lenders and borrowers. It puts a very high administrative burden on the lender and we believe this acted as a barrier to entry, especially if a lender does not anticipate that many borrowers will benefit from the scheme. For those lenders in the scheme they are finding that they can often help borrowers through their normal forbearance tools.

45. The key benefit of the government initiatives is increased engagement with lenders and money advice. Lenders cannot help borrowers who do not engage.

The impact of the credit crunch on access to mortgage finance and the terms on which such finance is offered for first time buyers

46. The credit crunch has had profound effects on the availability of funding and which parts of the lending market can access it.

47. The overall impact of the difficulties in lenders accessing funding is that active mortgage lending is in the hands of a few major lenders. The majority of building societies and specialist non-deposit-takers are effectively dormant and there is very limited appetite for higher risk lending.

48. The credit crunch triggered an immediate very sharp fall in house purchase lending, not least because of lender uncertainty about house price movements and credit risk concerns associated with the resulting higher LTV profile across mortgage books.

49. Inevitably given the more highly leveraged natured of such lending, FTB numbers have fallen sharply, but perhaps surprisingly their share of overall house purchase lending has nudged up a little over the past two years.

50. Despite peak-to-trough falls in house prices nationally of about 20%, we have not yet seen any improvement in the underlying affordability position of would-be FTBs. This is because the benefits (for younger households) of falling house prices have to date been fully offset by the more restrictive lending criteria being applied by mortgage lenders. The net effect has been for the deposit requirement to mushroom over the past two years. CML estimates (currently unpublished) suggest that 80% of younger FTBs (those under 30) are currently relying on parents or relatives for financial support with the deposit —up from about a half just a year ago and less than 40% back in 2006.

51. Although funding remains constrained and higher LTV lending carries a more punitive treatment under Basel 2 rules, lenders continue to explore how to serve FTBs. But it is difficult to find ways of improving lending offers prudently while house prices continue to weaken.

52. The position of would-be FTBs is very important for a lasting recovery of the housing market. Until the funding position improves materially, market conditions are likely to remain difficult and any upturn hesitant.

53. To assist FTBs and stimulate the property market generally our Budget submission called for changes to the stamp duty regime and an expansion and simplification of the government's low cost home ownership schemes. These changes have not yet been introduced and we still believe these would make a difference.

Annexe

54. There are two regularly published sources of market information on mortgage possessions in the UK, namely the CML and the Ministry of Justice (MoJ). There are many differences between the two data sources, but the most important one is that CML figures relate to actual properties taken into possession by CML members, whereas MoJ figures relate to court orders for possession. A court order is in many cases a precursor to possession, but does not necessarily up in an actual possession.

55. A summary of the differences between CML and MoJ data is set out in Table 1 below.

Table 1

CML AND MoJ MORTGAGE POSSESSIONS DATA

	CML	*MoJ*	*Resulting difference*[1]
Data type	Physical possessions	Court orders for possession	MoJ figures higher
Regional coverage	UK	England and Wales	CML figures higher
Creditor coverage	1st charge mortgages by CML members only	All 1st and subsequent charge mortgages and other creditors	MoJ figures higher
Possession coverage	Court-ordered and voluntary possessions	Court orders only	CML figures higher

Notes:
1. assuming all other factors are equal

56. There are several factors that will cause the figures to diverge. The CML data is for properties that are physically taken into possessions—not all court orders will end up in possession. The CML data includes cases where borrowers voluntarily hand over the property, which are not captured by the MoJ. The CML's data is based on possessions taken by its members under first charge mortgages only, accounting for around 98% of the first charge market. The MoJ figures include possessions by non-CML members and those taken under additional charges. In terms of a geographic split, the CML data covers the entire UK, while the MoJ covers England and Wales only.

57. The differences in coverage and definition mean that CML and MoJ figures are unlikely to be of a similar magnitude in absolute terms, except by coincidence. In fact the overall effect of the differences is that MoJ figures for total possession orders have been tended to be significantly higher than CML possession figures.

58. Please see attached the latest quarterly data for arrears as measured by number of months (AP1) and % of outstanding balance (AP2), properties taken into possession (AP4) and loans to first-time buyers (ML2).

Table AP1

ARREARS ON MORTGAGES, BY NUMBER OF MONTHS IN ARREARS

Period		*1* *Mortgages outstanding, end period*	*2* *Mortgages > 3–6 months in arrears, end period*	*3* *Mortgages > 3–6 months in arrears, end period*	*4* *Mortgages < 6–12 months in arrears, end period*	*5* *Mortgages > 6–12 months in arrears, end period*	*6* *Mortgages > 12 months in arrears, end period*	*7* *Mortgages > 12 months in arrears, end period*	*8* *All > 3 months in arrears, end period*	*9* *All > 3 months in arrears, end period*
		number	*number*	*% all loans*	*number*	*% all loans*	*number*	*% all loans*	*number*	*% all loans*
2008	Q1	11,787,000	78,600	0.67	43,900	0.37	16,000	0.14	138,500	1.18
	Q2R	11,763,000	86,000	0.73	48,700	0.41	18,000	0.15	152,700	1.30
	Q3R	11,718,000	92,900	0.79	53,700	0.46	20,100	0.17	166,700	1.42
	Q4R	11,667,000	117,400	1.01	72,000	0.62	29,500	0.25	218,900	1.88
2009[2]	Q1	11,105,000	123,500	1.11	90,900	0.82	50,700	0.46	265,100	2.39

R = revised
Source: CML Research

Notes:

1. Figures are estimates of arrears on first charge loans held by CML members. They do not include arrears relating to other secured lending or to firms that are not CML members. As our figures also relate to the number of borrowers rather than individual loan accounts, they will be materially lower than, and not strictly comparable with, the aggregate MLAR figures published by the FSA.
2. In Q1 2009 around 490,000 "legacy loans" (those for which only a nominal balance is retained, for example for deed storage purposes) which had previously been reported were newly excluded, to bring reporting in line with our guidance notes. Accordingly our estimate for the total number of mortgages up to and including 2008 is not comparable with estimates thereafter. It has not been possible to revise earlier estimates in line with this guidance. The total number of arrears and possessions are not affected by this change.
3. These estimates are based on reporting by a sample of CML members, which are then grossed up to be representative of the lending undertaken by CML members as a whole. In Q1 2009 these accounted for over 95% of first charge mortgages.
4. Figures are subject to revision as we get better information about rates of growth and performance in different parts of the market, lenders report to us for the first time or re-submit earlier figures.
5. Care should be taken when looking at changes over time as lenders newly reporting figures may distort comparisons.
6. Trends in the number of months arrears data may also be distorted by changes in mortgage rates. When rates change this may alter the contractual mortgage repayments due and so affect the number of months that a given arrears amount represents. In the case of variable rate products, with lower mortgage rates a given amount of arrears represents a higher number of monthly payments.
7. Properties in possession are not counted as arrears.
8. Arrears and possession figures are rounded to the nearest hundred.
9. Minor revisions have been made to 2008 data.

Table AP2

ARREARS ON MORTGAGES, BY PERCENTAGE OF TOTAL BALANCE IN ARREARS

Period		*1 Mortgages outstanding, end period*	*2 Mortgages 1.5%< 2.5% in arrears, end period*	*3 Mortgages 1.5%< 2.5% in arrears, end period*	*4 Mortgages 2.5%< 5% in arrears, end period*	*5 Mortgages 2.5%< 5% in arrears, end period*	*6 Mortgages 5%< 7.5% in arrears, end period*	*7 Mortgages 5%< 7.5% in arrears, end period*	*8 Mortgages 7.5%< 10% in arrears, end period*	*9 Mortgages 7.5%< 10% in arrears, end period*	*10 Mortgages > = 10% in arrears, end period*	*11 Mortgages >10% in arrears, end period*
		number	*number*	*% all loans*	*number*	*% all loans*	*number*	*% all loans*	*number*	*% all loans*	*number*	*% all loans*
2008	Q1	11,787,000	.	.	73,800	0.63	25,200	0.21	10,700	0.09	17,300	0.15
	Q2R	11,763,000	.	.	80,000	0.68	28,000	0.24	12,300	0.10	19,400	0.16
	Q3R	11,718,000	.	.	88,300	0.75	29,500	0.25	12,800	0.11	20,200	0.17
	Q4R	11,667,000	101,800	0.87	105,900	0.91	36,800	0.32	15,600	0.13	24,300	0.21
2009[2]	Q1	11,105,000	128,500	1.16	117,200	1.06	42,600	0.38	17,900	0.16	27,600	0.25

Source: CML Research

Notes:

1. Figures are estimates of arrears on first charge loans held by CML members. They do not include arrears relating to other secured lending or to firms that are not CML members. As our figures also relate to the number of borrowers rather than individual loan accounts, they will be materially lower than, and not strictly comparable with, the aggregate MLAR figures published by the FSA.
2. In Q1 2009 around 490,000 "legacy loans" (those for which only a nominal balance is retained, for example for deed storage purposes) which had previously been reported were newly excluded, to bring reporting in line with our guidance notes. Accordingly our estimate for the total number of mortgages up to and including 2008 is not comparable with estimates thereafter. It has not been possible to revise earlier estimates in line with this guidance. The total number of arrears and possessions are not affected by this change.
3. These estimates are based on reporting by a sample of CML members, which are then grossed up to be representative of the lending undertaken by CML members as a whole. In Q1 2009 these accounted for over 95% of first charge mortgages.
4. Figures are subject to revision as we get better information about rates of growth and performance in different parts of the market, lenders report to us for the first time or re-submit earlier figures.
5. Care should be taken when looking at changes over time as lenders newly reporting figures may distort comparisons.
6. Trends in the number of months' arrears data may also be distorted by changes in mortgage rates. When rates change this may alter the contractual mortgage repayments due and so affect the number of months that a given arrears amount represents. In the case of variable rate products, with lower mortgage rates a given amount of arrears represents a higher number of monthly payments.
7. Properties in possession are not counted as arrears.
8. Arrears and possession figures are rounded to the nearest hundred.
9. Minor revisions have been made to 2008 data.

Table AP4

POSSESSIONS ON MORTGAGED PROPERTIES

Period		*1 Mortgages outstanding, end period*	*2 Properties taken into possession in period*	*3 Properties taken into possession in period*	*4 Properties in possession at end period*	*5 Properties in possession at end period*	*6 Possessed properties sold in period*	*7 Properties taken into possession in period*	*8 Voluntary possessions*	*9 Voluntary Possessions Share*
		number	*number*	*% all loans*	*number*	*% all loans*	*number*	*% change on last period*	*number*	*% of possessions*
2008	Q1	11,787,000	8,500	0.07	15,600	0.13	5,200	1,200	14.1	
	Q2R	11,763,000	10,000	0.09	18,700	0.16	6,400	17.6	1,600	16.0
	Q3R	11,718,000	11,100	0.09	22,700	0.19	6,800	11.0	2,100	18.9
	Q4R	11,667,000	10,400	0.09	22,700	0.19	10,900	−6.3	2,530	24.3
2009[2]	Q1	11,105,000	12,800	0.12	25,100	0.23	12,200	23.1	3,440	26.9

R = revised

Source: CML Research

Notes:

1. Figures are estimates of arrears on first charge loans held by CML members. They do not include arrears relating to other secured lending or to firms that are not CML members. As our figures also relate to the number of borrowers rather than individual loan accounts, they will be materially lower than, and not strictly comparable with, the aggregate MLAR figures published by the FSA.
2. In Q1 2009 around 490,000 "legacy loans" (those for which only a nominal balance is retained, for example for deed storage purposes) which had previously been reported were newly excluded, to bring reporting in line with our guidance notes. Accordingly our estimate for the total number of mortgages up to and including 2008 is not comparable with estimates thereafter. It has not been possible to revise earlier estimates in line with this guidance. The total number of arrears and possessions are not affected by this change.
3. These estimates are based on reporting by a sample of CML members, which are then grossed up to be representative of the lending undertaken by CML members as a whole. In Q1 2009 these accounted for over 95% of first charge mortgages.
4. Figures are subject to revision as we get better information about rates of growth and performance in different parts of the market, lenders report to us for the first time or re-submit earlier figures.
5. Care should be taken when looking at changes over time as lenders newly reporting figures may distort comparisons.
6. Trends in the number of months arrears data may also be distorted by changes in mortgage rates. When rates change this may alter the contractual mortgage repayments due and so affect the number of months that a given arrears amount represents. In the case of variable rate products, with lower mortgage rates a given amount of arrears represents a higher number of monthly payments.
7. Properties in possession are not counted as arrears.
8. Arrears and possession figures are rounded to the nearest hundred.
9. Minor revisions have been made to 2008 data.

Table ML2

FIRST-TIME BUYERS: LENDING AND AFFORDABILITY UK

		Number of loans	*Number of loans*	*Value of loans*	*Age of borrower*	*Advance*	*Income*	*Percent advance*	*Income multiple*	*Interest payments as % of income*
			% of total for house purchase			*£*	*£*			
		number		*£m*	*median*	*median*	*median*	*median*	*median*	*median*
2000	Q1	125,700	49	7,429	31	50,000	21,500	90	2.40	13.5
	Q2	126,900	44	7,806	30	51,775	22,452	90	2.44	14.7
	Q3	130,600	43	7,847	30	52,000	22,072	90	2.40	14.3
	Q4	117,000	43	7,120	30	50,753	22,482	90	2.44	14.7
2001	Q1	108,300	44	6,840	30	53,995	22,500	90	2.44	14.4
	Q2	137,600	42	9,094	30	55,000	23,282	90	2.46	13.6
	Q3	167,400	44	11,412	31	58,200	24,000	90	2.49	13.5
	Q4	154,900	43	10,798	30	60,000	24,386	90	2.53	12.3
2002	Q1	111,100	40	8,240	31	63,050	24,899	90	2.62	12.4
	Q2	133,600	37	10,562	31	67,352	26,050	90	2.68	12.2
	Q3	149,200	38	12,605	31	70,015	27,672	90	2.67	12.1
	Q4	137,900	39	11,732	31	72,995	27,860	90	2.72	12.2
2003	Q1	86,300	33	7,242	31	68,469	26,635	89	2.69	11.9
	Q2	88,900	31	7,591	32	71,000	26,690	89	2.75	11.6
	Q3	97,200	28	8,850	31	79,563	26,804	90	2.91	11.7
	Q4	97,200	28	9,254	31	84,250	28,400	89	2.91	11.9
2004	Q1	87,200	30	8,150	32	80,000	27,500	87	2.88	12.7
	Q2	97,000	28	9,818	31	90,000	29,626	87	3.00	14.4
	Q3	95,900	28	10,105	31	94,500	30,000	87	3.11	16.1
	Q4	78,000	30	8,193	31	94,950	28,666	88	3.17	17.7
2005	Q1	58,900	30	6,276	31	95,490	30,700	89	3.13	16.3
	Q2	104,500	39	11,187	29	96,950	31,844	90	3.01	16.7
	Q3	106,300	38	11,719	29	100,000	32,320	90	3.06	16.4
	Q4	102,600	38	11,577	29	101,850	32,702	90	3.11	15.9
2006	Q1	87,000	38	9,892	29	101,700	32,512	90	3.13	16.0
	Q2	102,700	36	12,277	29	107,880	33,562	90	3.20	16.4
	Q3	107,100	35	13,660	29	110,980	34,258	90	3.25	17.0
	Q4	104,200	35	13,121	29	113,645	34,495	90	3.30	17.7
2007	Q1	84,900	36	10,795	29	113,950	34,344	90	3.32	18.0
	Q2	95,400	35	12,463	28	116,700	35,000	90	3.36	19.1
	Q3	96,100	34	12,972	29	118,899	35,516	90	3.39	20.0
	4	81,400	36	10,689	29	117,499	35,202	90	3.36	20.6
2008	Q1	53,200	38	6,828	29	114,750	35,000	89	3.35	20.1
	Q2	56,700	38	7,291	28	14,000	35,000	88	3.34	19.7
	Q3	44,500	36	5,454	29	108,000	34,243	85	3.23	19.8
	Q4	40,000	38	4,585	29	102,478	33,773	82	3.12	18.2
2009	Q1	30,100	39	3,216	29	95,765	32,690	75	3.00	15.4

Source: CML/BankSearch Regulated Mortgage Survey

Notes:

1. Totals shown are estimates grossed up from the sample of lenders reporting to reflect total market size.
2. All figures from April 2005 onwards are based on Product Sales Data reported to CML. Figures pre-April 2005 are taken from the Survey of Mortgage Lenders. Prior to 1992 Q2 (and annually prior to 1993) figures are taken from the Building Societies 5% sample of mortgage completions. There are material differences in both the reporting methodologies and the sample of contributing lenders for the different surveys. Figures after April 2005 are not strictly comparable with those up to that point.
3. Before Q2 1992 figures on loans for house purchase are for all building societies only.
4. Average figures shown are medians, as this tends to better represent the position of the typical borrower.
5. Interest payment calculations are net of MIRAS (and previous to this MITR) up until MIRAS was discontinued in April 2000.
6. Affordability calculations are based on averages of calculations for individual transactions.
7. Prior to April 2005, estimates of the proportion of first time buyers and movers exclude cases where the previous tenure of buyers is not known.
8. First time buyer numbers will include some buyers who have previously owned a property before, but are not in owner-occupation at the time of this purchase. Estimates from the Survey of English Housing suggest that that around 20% of stated first-time buyers may in fact fall into this category (http://www.communities.gov.uk/index.asp?id = 1154799).
9. There is no data available on capital and interest payment as % of income before April 2005.

Written evidence submitted by the Intermediary Mortgage Lenders Association

Executive Summary

— IMLA is the mortgage trade body for lenders who distribute mortgages via intermediaries.

— The shortage of mortgage finance sits at the heart of the issues under discussion. It is vital a fully functioning and competitive mortgage market is restored as soon as possible.

— All lenders are making strenuous efforts to control arrears and limit possessions and the evidence suggests that this in conjunction with the government schemes and lower interest rates is making a difference.

— There is a strong case for a full review of SMI to bring it up to date and make it more effective.

— Local authorities should have wider powers to buy homes where re-possession is taking place.

— All lenders should have access to the government schemes in place to support the mortgage market. The current approach is market distorting and adds to the stresses being faced in specific sub markets.

— First time buyers face considerable difficulties and IMLA would welcome a comprehensive re-working of low cost home ownership.

Introduction

1. The Intermediary Mortgage Lenders Association is pleased to respond to the Treasury Committee's request for evidence. Reflecting the tight timescale this is a brief response.

2. IMLA is a trade body for lenders who distribute their products via intermediaries. Its membership includes major banks and building societies as well as specialist lenders. A full range of products is sold via intermediaries covering the prime, non prime and buy to let markets. Some of the more specialist products are only sold via intermediaries reflecting the need for careful advice and guidance.

3. In the paragraphs below we respond to the Committee's detailed questions. However before doing so we would want to highlight the issue we believe should be at the heart of the Committee's deliberations. This is the supply of mortgage finance. Currently, a small group of large lenders are being asked to fund all lending while a large group of smaller lenders, typically specialist lenders and building societies, are currently unable to lend. This inability to lend is due to a range of restrictions placed upon them by a combination of the perhaps understandably cautious capital requirements of the government and the regulator, competition in the savings market for retail deposits and the closure of alternative sources of funding such as the securitisation market. The resulting mortgage drought has limited the alternative options for customers and contributed to the delay in the revival of the housing market.

Mortgage Arrears and Possessions

4. All lenders are making strenuous efforts to control arrears and limit possession cases not least because of the financial and other costs these impose. This includes loan modification, capitalisation, term extension and assisted sales along with direct links to external advice agencies. Such mechanisms are used by mainstream and specialist lenders. However, in a market where house prices are at best stable if not falling options can be more limited. Whereas in a rising market, the practice of borrowers "trading out" of any financial difficulties is common place, in a declining housing market and with limited mortgage supply this is a much rarer occurrence.

5. However, with the potential stabilisation of house prices, the impact of lower interest rates and the beneficial results of a range of government and lender initiatives starting to impact, our members feel there are grounds for some optimism regarding the level of mortgage arrears and the number of possessions.

6. Setting aside the differing basis for the numbers produced by the FSA and the Council of Mortgage Lenders (see the very useful Ministry of Justice Technical note on this topic—attached) IMLA shares the view that the number of repossessions may be lower than previously anticipated. While, IMLA worked to ensure that the government backed support schemes for borrowers in difficulty included those homeowners excluded from the mainstream mortgage market, we would highlight the continuing difficulties of borrowers in the non-prime market and those who might previously have migrated from prime to non prime as their credit situation deteriorated. The non prime market covers a wide spectrum of customers, from those with only very modest credit weaknesses such as missed payments to others with major arrears and county court judgements. The spectrum runs from near prime to heavy sub prime though it is worth noting an estimated 80% of loans were in the near prime end of this.

7. Like many mortgage customers, non-prime borrowers are benefitting significantly by the fall in interest rates, in particular in the LIBOR rate as the price of many non prime mortgages are based on LIBOR. However, over the medium term we can expect to see interest rates rise and the combination of rising rates and rising unemployment could pose considerable difficulties in the next two to three years for some borrowers in both prime and non-prime—markets.

8. This current downturn is really the first experienced by the borrowers in the non prime market since this emerged in the mid 1990s. This market grew rapidly in the last decade to around 10/15% of the total volume of mortgages in a year. The expansion of a non-prime market helped some new borrowers (not least the self-employed) into home ownership and kept others in home ownership when their credit deteriorated.

9. Although the largest banks and building societies were major players in these sub-markets (non prime, self certificated, buy to let) they were also core markets for the specialist lenders most of whom are not currently taking on new business.

10. Most specialist lenders were funded through the capital markets (via securitisation), by the sale of mortgage books to other lenders and by balance sheet support from parent companies. The devastating effect of the credit crunch has meant that effectively all of these channels are now closed. As they are ineligible for the generous government support that has been provided to UK deposit takers, specialist lenders are unable to continue to lend to their customer base and are instead managing down their existing loan books and their costs.

11. This is a significant factor behind the UK's present lack of mortgage lending, restraining the housing market's ability to recover. All lenders and not least specialist lenders are working hard to help those in difficulty stay in their homes. In so doing they are following FSA requirements and industry guidelines. The recent FSA review (results were published on 22 June) identified a number of problems with existing arrears and possessions procedures and practices but did acknowledge that the lenders were making efforts and that their systems were still absorbing the procedural changes required by the introduction of the Pre-Action Protocol, the Home-Owner mortgage support scheme (HMS) and Mortgage Rescue scheme (MRS) as well as the industry guidelines issued by the CML.

12. Some lenders have exited the market and the responsibilities for the continuing servicing of their loan book will pass to whoever bought it plus any third party service provider. Without doubt this is a possible area of tension and where consumer detriment could be an issue. However the FSA has examined this and has not identified any additional problems.

13. All lenders of whatever type work closely with the FSA and its supervisory teams. Lenders have also found the guidance produced through the CML a useful way of translating the regulatory guidelines into practicalities. The general view is that the industry is managing through arrears and possessions. There is concern that going forward rising unemployment will make this more difficult as some households are sustaining but not curing their arrears position.

THE GOVERNMENT SCHEMES

14. There are a range of government programmes in place, some pre- existing, others a product of the credit crunch. Those that seek to assist borrowers experiencing difficulties with their mortgage are as follows:

— Support for mortgage interest (SMI)

— Home-Owner mortgage support scheme (HMS)

— Mortgage Rescue scheme (MRS)

— Interest rate reductions

5. Those that seek to provide liquidity assistance to deposit takers are as follows:

— Special Liquidity scheme (SLS)

— Credit Guarantee scheme

— Bank Recapitalisation Fund

— Asset Protection scheme

— Asset Backed guarantee scheme

16. Commenting briefly upon some of the schemes, the SMI scheme has been updated to cover larger mortgages, quicker access to the system and a lower standard rate of interest. Unfortunately, these concessions have all been time limited by the Government and will be withdrawn over a varying period. This will generate confusion. In addition, though access has been widened the capital limits and working rules imposed through the social security system are such that most households in difficulty will not be eligible. In the 1991 recession only 25% of those in difficulty got access to what was then called income support for mortgage interest (ISMI). As this begins to suggest many households solve the problem with their lender directly or through trading down.

17. There has been extensive press comment on the small number of cases going through the HMS and Mortgage Rescue schemes. However, firstly there have been a lot of enquiries and this has itself triggered closer working between lenders and borrowers. Second both schemes are complex and so the number of borrowers being assisted will take time to increase. In particular, the Mortgage Rescue scheme is complex and it will take time to select and agree each case. Lenders have been active in getting the scheme off the ground and one of our members has seconded a staff member to the Department of Communities and Local Government to assist the process. However, we understand there appears to be a slow level of take up among local authorities and would urge the Committee to seek clarity from CLG as to the steps being taken to ensure all local authorities are aware of the scheme and how they can use it to assist vulnerable borrowers in financial difficulties. While some authorities are proactively engaging with lenders as to how to identify and assist vulnerable borrowers, others have not accessed the scheme yet.

18. Our view is that the HMS scheme has been "over-engineered" in terms of processes but also that the restrictions imposed in terms of government guarantees have themselves been limiting. After lengthy negotiations in which IMLA and specialist lenders were active, a number of lenders have opted not to participate in HMS and operate a "parallel" system without some of the management burden associated with HMS. However some IMLA members are in the scheme or about to join it once IT systems are in place to deal with the reporting requirements.

19. Going forward we feel there is a strong case for local authorities to have a mandatory duty to buy in homes where re-possession is threatened and where homelessness might arise. This would help underpin the market and spread the range of homes in council ownership. The recent allocation of £20 million to help local authorities assist those in difficulty is a step in the right direction.

ACCESS TO MORTGAGE FINANCE

20. Without going into the detail of the different schemes put in place to support lenders we would stress to the Committee, the damaging impact of the Government's decision to exclude non-deposit (non-banks) taking institutions from all of them. IMLA has held a number of meetings with HM Treasury to try to widen access but to date this has not been possible.

21. The Government is focussing all its assistance on a small number of lenders, which, in our view, has prolonged the mortgage drought, delayed the recovery of the housing market as well as weakening the competitive pressures in the market place, giving advantages to a minority of firms, many of whom are relying upon taxpayer support.

22. The extension of these existing measures of support to non-banks could stimulate a resumption of lending by those non-banks, with particular benefit for the niche markets that have been hit hard by the withdrawal of credit (first-time buyers, the self-employed, non-prime and buy-to- let). The non-banks are ready, willing and able to resume lending upon access to support measures from the Government.

23. Meanwhile, the Government is trying very hard to get the banks to maximise the amount of lending they are prepared to undertake. So it seems odd, at the same time, to keep non-banks out of its various market support schemes, as non-banks can make an immediate contribution to new lending volumes.

24. The same is true with respect to the many building societies who are facing intense competition for savings along with a reluctance by local authorities to place short and medium term funds with them, the extra costs coming through the Financial Services Compensation scheme along with higher regulatory capital requirements from the FSA. Taken together little wonder lending has also fallen off in that sector. The recently announced profit participating deferred shares (PPDS) are unlikely to provide a major source of new funds for the sector.

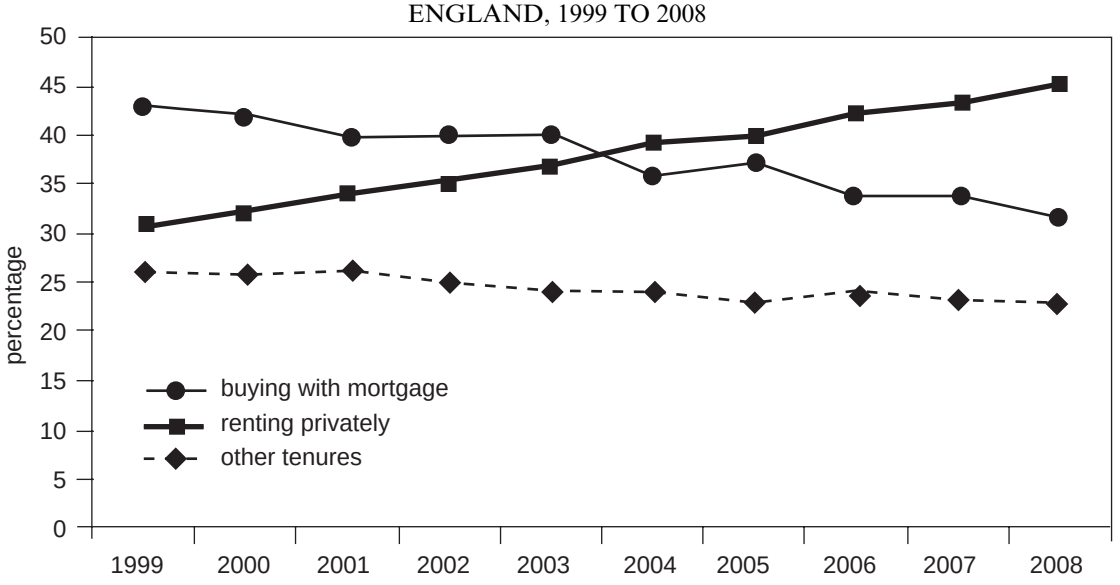
25. From an IMLA perspective our view is that we need to restore a fully functioning and competitive mortgage market. As matters stand we are some distance from that. Extending the current government schemes to cover all deposit taking and non deposit taking lenders would be a sensible step forward.

FIRST TIME BUYERS

26. In the immediate aftermath of the Credit Crunch lenders cut back on their loan to value ratios and increased their deposit requirements. This meant that most high LTV products were withdrawn from the market. This situation has eased a little with a number of 90% LTV products back in the market place increasing slightly (though the volume might also be an issue). All surveys continue to point to the difficulty first time buyers are having with respect to access to the market. Little wonder then that there has been a major shift in the tenure patterns of households under 30 (see Chart 1 below for England).

Chart 1

TRENDS IN TENURE OF HOUSEHOLDS WITH HRP AGED LESS THAN 30, ENGLAND, 1999 TO 2008



Source: ONS, Labour Force Survey

27. IMLA has raised the question of what might happen to the high LTV market so central to first time buyers. The general view from the industry is that this market will return over time. However this could be some while and much of that is conditional upon the regulatory regime that comes into place through the FSA and the EU. The FSA's current mortgage market review has high loan to value and loan to income

ratios on its agenda along with questions around specific products such as self certificated mortgages. The industry would be strongly opposed to product regulation preferring that controls over lender risk appetite is dealt with via prudential regulation and capital requirements. The view is that product controls can normally be avoided in some way and that the regulations would constrain product development and innovation.

28. In raising the question of high LTV lending IMLA raised the issue of the role of mortgage guarantee schemes. In other countries these have an important part to play in assisting first time buyers enter the market but in a relatively low risk way. The experience of the last recession when many lenders found their mortgage insurance policies did not pay out to the extent the lenders were expecting has meant there is only limited support for this approach.

29. Instead the UK has put considerable reliance upon low cost home ownership schemes funded by the taxpayer. Typically these take one of two forms;

— Shared ownership where the occupier pays part rent, part mortgage, the precise % depending upon their circumstances. The occupier pays rent to the housing association with whom he/she shares the freehold in the case of houses and or as a leaseholder in the case of flats.

— Shared equity where the occupier takes out a mortgage for a proportion of the purchase price. The occupier owns the freehold interest and the holder of the equity loan (government, housing association or developer and sometime in combination) which makes up the difference has a second charge on the home.

30. Despite efforts to rationalise the schemes in England there remain a number of variants (New Build HomeBuy (shared ownership), Open Market Homebuy—two variants—My Choice Homebuy and Own Home Homebuy (though both somewhat diminished because the HCA has limited funds) and HomeBuy Direct with housebuilders as well as a small scheme for existing social housing tenants to buy their homes. By contrast, the schemes in Northern Ireland and Wales have been reasonably stable

31. In brief the schemes in England have suffered from a number of weaknesses;

— A lack of clarity around aims and outcomes compounded by very limited performance monitoring.

— The lack of a secondary market so that subsidised homes can be retained with the LCHO sector.

— Complex management arrangements between lenders and associations in terms of arrears and possessions which have resulted in lenders favouring shared equity over shared ownership.

— Constant change in programme scale and content.

— A lack of focus on the purchasers interests both in terms of access into this market but also how they might exit.

32. Most recently a number of lenders have steeped back from the LCHO market reflecting their general concern about higher risk lending. Unfortunately the Mortgagee Protection clause which is in place to help lenders recover losses in the event of default is itself not as effective as might be hoped. Moreover because it does not constitute a guarantee in the sense of the Capital Requirements Directive it means lenders have to provide more regulatory capital to cover the risk of LCHO loans. This is a further disincentive.

Conclusion

33. This brief response has been prepared to meet the Committee timetable. It has not been possible to supply data or case study examples.

34. Lenders remain very committed to managing down arrears and possessions. The evidence suggests this is what they have been able to do. Clearly there will always be the potential to do more and not least as the new systems and arrangements bed down. The specialist lending sector is one in which a wide array of lenders participate. It deals with some higher risk customers and with more difficult credit histories. IMLA along with other trade bodies and the regulator continues to work to improve practice in this market and to ensure it is supported. There is now a closer working relationship with the government around this agenda and this has been invaluable. Without doubt, the major unresolved issue is funding and the restoration of fully active mortgage market.

June 2009

Written evidence submitted by Home Funding Limited

Introduction

Home Funding Limited (HFL) is pleased to respond to the Treasury Committee's request for evidence.

HFL is a mortgage lending servicing and consulting company which, among other things, provides full operational, strategic and management support to Basinghall Finance PLC, a UK mortgage lender which is a wholly owned subsidiary of WestLB AG.

We will attempt to cover the key elements of the Committee's Terms of Reference but will focus on what we see as the key issue facing the mortgage market at the moment—the lack of credit available to consumers for mortgage finance in general and the impact of this on vulnerable consumer sectors which includes first time buyers.

Mortgage Arrears and Possessions

In summary

1. Our experience is that mortgage arrears and repossessions have tended to stabilise. This is attributable to two main factors: a reduction in interest rates applied by lenders following cuts in the Bank of England Bank Rate and the forbearance shown by lenders to help borrowers stay in the their homes.

2. We forecast that this trend will be sustainable for as long as:

   (a) Mortgage Interest rates stay low.

   (b) The economy begins an upturn in performance.

   (c) A supply of credit to key sectors (currently not available—see below) of both the consumer and business markets is made available.

This is in line with the current OECD thinking.

3. Lenders have taken different approaches to dealing with borrower's in arrears. Those lenders which fund mortgages entirely on-balance sheet do not have the constraints of securitisation or covered bonds which may set limits on the degree of arrears that are allowed to roll-up unpaid by the borrower under the terms of the transaction. Whilst we are not aware that this has caused any significant problems to date it could in the future. It is worth noting that the largest users of these funding mechanisms were the mainstream lenders such as HBOS, Abbey National and Northern Rock. These lenders make up a sizeable proportion of the market.

4. Some lenders (and in particular the non-bank specialist lenders) use third party administrators to administer their mortgage loans, including arrears management. Whilst this activity has been outsourced to a regulated entity, the lender remains responsible for the actions of its administrator. Although the FSA recently identified a problem with some lenders/servicers we would be surprised if this were widespread.

5. Of more concern is the recent sale of certain mortgage portfolios to unregulated hedge funds. Their primary motive is to make money and they are perhaps more likely to follow the path of least resistance to achieve this. This may include the realisation of sale proceeds from a repossessed property rather than the more unlikely repayment or refinancing of the loan by the borrower. The safeguard that exists here is that the outsourced third party administrator will be regulated.

Current Government Assistance and Recommendations for Improvement

Mortgage Rescue

6. Following the government's original announcement of the scheme, experience has been that it is difficult to find candidates that fit. The initial obstacles being equity and the regional caps imposed on property value. Furthermore, Local Authorities appear to have differing levels of knowledge of mortgage rescue and their approaches have seemed mixed. The recent changes to criteria and the ongoing work to improve the consistency of approach are welcomed. Reports show that just six borrowers have been helped under this scheme for the year to the end of May.

Support Mortgage Interest

7. This is the most immediate form of assistance provided by government and recent amendments have allowed more to benefit from earlier payments paid at an increased level. In practice this can allow relief payments to be received by the lender prior to the arrears situation becoming a concern.

8. In the current market, it may be considered that lenders would be satisfied to receive the benefit payable under SMI in combination with a possible contribution from the borrower rather than face the prospect of a shortfall on sale. However, it may also be fair to state that historical levels of re-mortgage activity present in the UK have meant that debt consolidation can be a significant percentage of the loan balance on a significant proportion of loans. In some instances the gap between the benefit paid and the required monthly payment may be too wide for the lender to allow extended forbearance, if the customer is unable to contribute.

Homeowner Mortgage Support (HMS)

9. The objective of the scheme can be considered a positive step for those experiencing some level of payment difficulty but who do not qualify for SMI. With work ongoing to simplify the administration of the scheme this looks to be moving forward albeit from a very low base. However, implementation has been very limited. Lenders have found it difficult to implement the reporting and procedures required for a questionable benefit, particularly where administration has been outsourced to a third party. Furthermore, the scheme does not sit well within securitisation funding structures (circa 25% of all UK mortgage funding)

nor does the guarantee have enormous appeal when one considers that the only way of realising the benefit is to repossess the property. There is a risk that the HMS will serve to hold repossession in abeyance in the short term but we could see a spike in the repossession rate in the future if the economic and funding issues do not become more positive to alleviate the long-term stress to borrowers.

10. Many lenders will consider allowing loans to continue to accumulate arrears at a low rate as a reasonable alternative to experiencing a loss on sale, where there is a chance of the customer turning the situation around. However, some concerns relating to the scheme would be:

— Customers with mortgage arrears often have other debt issues and tend to be poor with money management. Often this means that payments are missed. This will have a knock-on effect on the amount of loans which will be eligible for entry and on those which will remain in the scheme. Ensuring that customers obtain good quality money advice is key to resolving this.

— What is reasonable to consider as a short term issue? This is relatively simple to assess when there has been, for example, a short term health issue, but consider the situation where one borrower faces unemployment. It is difficult for lenders to make an objective judgement about how likely an individual is to be re-employed in the short term. There is a danger of generalisations as to the likelihood of employment in specific industries and geographic areas.

— A reduction in the income of self employed persons is the cause of arrears for a significant number of accounts. Many self-employed people are or will be reliant on credit to either keep them going or to kick-start their business after the down-turn. In the current climate, lenders are far from confident that this vital supply of credit will be available.

— Allowing this extended forbearance could prove ultimately to be to the customer's detriment ie their situation doesn't improve and they find themselves in a worsened negative equity situation with the house price having fallen in the interim. Where this is the case, it is possible that lenders may be exposed to retrospective assessment of their decision making in this respect? (eg a customer feels they should be compensated for losses incurred following the lender choosing not to repossess).

— Customers who will be eligible for the scheme are those who are struggling to maintain payments at a time of low interest rates.

What can be done to improve the management of loans in arrears?

11. In addition to the assistance put in place by government, there is a great deal of work being undertaken by mortgage lenders to allow customers a reasonable amount of time to overcome their difficulties. However, despite these initiatives, lenders are still proceeding with court action for possession.

Some of the key problems that lenders face when managing loans in arrears are as follows:

— A lack of information which lenders need to assess a customer's circumstances. Some customers will cut off all communication with the lender. Debt advice agencies do assist, however, this is not observed frequently enough, and the quality of the output is not always beneficial, especially from institutions which rely on untrained volunteers.

— There is a failure to adequately prioritise debt. It may well be that concessions are agreed by mortgage lenders but that this "breathing space" is used to keep other unsecured lenders at bay. Too often customers are dealing with each debt in isolation rather than looking at them as a whole and prioritising accordingly.

— Customer's over-promise and then fail to deliver.

12. In order to overcome these issues, there is a need to further raise the level of awareness of the benefits of debt advice among the public and increase the number of those receiving high quality advice. No reasonable lender should fail to allow a sensible proposal put forward by a customer following receipt of advice in line with industry best practice and steps should be made to ensure this is available to all who need it in a timely manner.

13. It is noted that efforts have been made to increase the level of debt advice available, however, it is felt that further work to improve the provision and quality of advice would reap benefits. Additionally, a change in the public's attitude to debt advice needs to be facilitated. This would not only assist lenders generally but would specifically help to overcome some of the concerns raised earlier in relation to HMS.

Access to Mortgage Finance

This, we believe, is the most important issue to be addressed and has a knock-on impact on mortgage arrears and the wider impacts on the state of the UK economy.

INTRODUCTION

14. Since the 1980s the provision of mortgage finance has been through a number of different types of lender including building societies, banks and specialist lenders. There has been a plentiful supply and a reliance on credit by consumers has become embedded in the normal operations of the economy. This is no longer the case. It is the current lack of supply that is causing such dislocation and is providing a positive feedback loop resulting in falls in spending which is reinforcing recessionary pressures.

15. Funding for the market has been provided by a number of different sources including retail deposits, wholesale committed bank funding lines, commercial paper, interbank, covered bonds and securitisation.

16. Since the commencement of the credit crisis in August 2007, the provision of funding though the securitisation, covered bonds and committed bank funding (warehouse funding) has become closed (other than as a mechanism to access the European Central Bank or Bank of England facilities such as the Special Liquidity Scheme). Even retail funded mortgage lenders are in short supply given that they are conserving capital, have an inherent mismatch between the asset and liability side of their balance sheet and are under increasingly close regulatory scrutiny to ensure solvency.

The non-bank specialised lenders accounted for six out of the top 30 lenders in the UK mortgage market in 2007 but more significantly they covered the majority of the markets which are now most needed—the first time buyer, key worker, impaired credit and buy-to-let markets. They were the majority players in these markets.

The majority of the finance that is currently available from existing bank and building society mortgage lenders is to the sub 75% LTV high quality credit market. There is virtually no provision of finance where the market needs it most—the very markets that the specialist lenders have predominated in. Although there have been some positive announcements recently regarding Northern Rock's re-entry into the mortgage market for loans up to 90% LTV, this is not in itself going to make a significant difference to the wider economy without the provision of funding on a similar basis from other lenders.

At present it is clear that all Government initiatives have been directed at the seven largest lenders:

— Lloyds Bank Group

— Royal Bank of Scotland

— Barclays Bank

— HSBC

— Nationwide

— Abbey/Santander

— Northern Rock

By far the majority of lenders have little or no support being made available to them by Government and this includes virtually all Building Societies and the non-bank specialist lenders. The majority of lending to first time buyers, key workers and other important sectors of our mortgage market has historically been provided by the smaller and specialist lenders. The lack of supply of liquidity to these sectors is now causing a drought within these key mortgage sectors and an impact on the recovery of the wider economy.

This situation, if left unaddressed, will hinder the recovery of the housing market and wider economy. Further, it is anti-competitive and in the long term will likely prove to be to the consumer's detriment with low levels of innovation and uncompetitive pricing. It could ultimately lead to cartel-like practices emerging.

The Government's objective

17. The key objective has been to kick-start mortgage lending, particularly in the sectors where supply is poor such as first time buyers, key workers and the growing number of people who have had some credit/payment difficulties (the latter category was estimated to have in the region of 100,000 borrowers a year moving down the credit spectrum before the credit crisis but will now be a potentially significant larger number). This must be dealt with if we are to avoid a continuing stagnation in credit supply and knock-on impact into the wider economy.

Lack of success

18. The focus up to now has been on providing support to the banking sector through a variety of mechanisms such as the asset purchase schemes, SLS, guarantees and securitisation AAA guarantees. These have yet to make any real impact on the freeing up of credit in the mortgage market and in any event all of these activities are focussed on the above major lenders.

What's missing?

19. Little or no support has yet been provided to the small to medium sized building societies and non-bank specialist lending sector which is deemed to be higher risk. This latter sector was key to the development of the mortgage market and is estimated to have accounted for 66% of the specialist lending market in 2007. (Total specialist market excluding buy-to-let estimated at £35 billion in 2007).

20. Whilst deemed to be higher risk by Government, it is worth considering that the specialist lending sector has had no funding support or Government bailouts (nor has it asked for any) unlike the mainstream banking sector.

URGENT RECOMMENDATIONS

Provide support at mortgage level

21. The Government should steer away from trying to deal with the solutions at a lender and funding model level and concentrate on providing support where it is needed—at mortgage level. This will avoid complexities as to funding structure and the bank/non-bank argument and will simplify the method of support considerably. A solution that would go to the heart of this objective would be to provide a Government guarantee for mortgage lending at Loan to Values (LTVs) above 75% and up to 95%. It would be chargeable, to be paid for either by the borrower or the lender (competition and the market should determine this) and the lender would share in some of the risk in the event of a claim under the guarantee consistent with existing guarantee schemes. This will ensure that the lender/Government have aligned interests in trying to minimise risk on these higher risk loans. Insurance premiums would vary depending on the degree of risk ie the higher the LTV and the poorer the underlying credit, the higher the premiums.

Enable more institutions to lend

22. The Government may be able to reinsure all or some of this risk with the insurance market so as to limit its liability and cost to the tax payer. By attaching a guarantee to the mortgage it moves away from worrying about whether banks or non-banks should be assisted. It will allow building societies to commence lending in these sectors without the FSA halting them (which we understand for some building societies is currently the case). For other lenders using either covered bond or securitisation techniques, the guarantee would be factored into the structure by the Ratings Agencies and investors as a positive contribution. It will be essential that the cover is transferable with the mortgage if it is sold eg to an SPV securitisation vehicle. This approach would also be consistent with the recently announced FSA Consultation Paper CP09/17.

23. Provision of mortgage funding lines to non-bank lenders and smaller regional building societies on economically viable terms would also allow those lenders to recommence lending in the key sectors identified earlier. It is feasible for the Government to influence state controlled banks to make this possible.

Secondary Markets—Covered Bonds and Securitisation Markets

24. Traditionally these instruments have been invested in by:

— Banks

— Hedge Funds

— Structured Investment Vehicles (SIVs)

— Life and Pension Funds

25. Of these entities, the only viable investors right now are Banks and Life and Pension Funds.

26. Banks have traditionally been big investors but capital and liquidity resources have diverted their focus. They do have assistance from the Bank of England through the Discount Window Facility and the Asset Purchase Scheme which have taken the place of the Special Liquidity Scheme going forward.

27. Life and Pension Funds have been and still are long-term investors. High quality credit performance and returns have made RMBS (particularly at the senior AAA and AA level) a natural investment for them. Having said that, they need an active secondary market available to them to ensure they can liquidate their holdings if necessary to preserve critical free asset ratios. Without an active secondary market and no access to the Bank of England schemes they are unlikely to want to invest in these instruments. This needs to be addressed urgently.

28. Hedge Funds continue to buy distressed sales of RMBS issues opportunistically but this is not thought to be a major part of the market going forward. The main reason is that Hedge Funds were accustomed to investing on a very significantly leveraged basis—typically 100 times. That just isn't possible now given that they are unable to raise senior debt finance from banks to build a fund. Typical Hedge Fund leverage is just "times one" now. Structured Investment Vehicles are similarly afflicted.

29. It is not going to be feasible to commence new issuance of covered bonds or mortgage-backed securities until existing stocks of bonds, that are currently being traded on a distressed sale basis in an illiquid market, are cleared from the market. For example, why would an investor choose to invest in a new AAA security when they can invest in an existing AAA security for a significant discount to par? Once the markets are cleared of existing stock, a secondary market maker needs to be established to encourage initial investment and to provide the secondary market liquidity essential for a healthy investment market.

30. The Bank of England is the obvious counterparty. Currently the Bank of England makes some provision for this through the Asset Purchase and Discount Window facilities. Although these are helpful they are only available to banks and need to be extended to non-bank investors who will then have a secondary market to trade with (eg Life Funds and Hedge Funds).

Conclusion

31. Given the truncated timeframes for the production of this note, it has not been possible to provide and exhaustive review of the key market issues nor to look at specific case studies in any real depth.

32. Arrears and repossessions are looking a little less under pressure at the moment from the statistics which we attribute mainly to the low interest rate environment and forbearance strategies being followed by lenders. They are clearly at significant risk if rates rise, particularly without an underlying sustained recovery in the economy and credit markets.

33. Clearly we should be concerned about the lag in unemployment which is still to work its way through the system.

34. A significant issue that needs addressing is the supply of credit to vulnerable sectors of the market including first time buyers, key workers and those suffering credit difficulties.

35. Provision of Government assistance is almost entirely through the seven largest lenders with little or no provision to smaller lenders including building societies and non-bank specialist lenders. This is seriously impacting on the markets ability to provide mortgage finance to key sectors. This is viewed as the most significant issue which we currently face.

June 2009

Written evidence submitted by Mr Fulcher

Executive Summary

1. The following submission, in response to the *Treasury Select Committee's* call for submissions, made 17th June, 2009, submits evidence of widespread consumer detriment experienced as a result of practices in the *"sub-prime" mortgage market* which are systemic, in breach of regulatory instruments, and by consequence therefore unlawful. These practices, as will be identified, fall within the *oversight and compliance responsibilities* of the *FSA*, the *OFT* and *FOS*.

2. The scale of consumer detriment is both unparalleled & appalling. The CML[35] figures serially underestimate the real scale of repossession action. The repossession figures will typically only reveal 1st charge repossessions, will *not* reveal how many repossession claims are brought in relation to 2nd charge mortgages which are prevalent in the sub-prime sector, will *not* reveal how many possession claims are "in the pipeline" and will also *never* fully disclose the vast quantity of suspended possession orders which are waiting *now* to be converted, alas all to easily, to full possession orders.

3. The submission will present three main points; (i) systematic abuse of consumers of sub prime mortgages in origination, and subsequent management and operation by *TPAs*(Third Party Administrators); (ii) regulatory failure, not in the substance of the regulations themselves (clarity prevails), but in their enforcement, chiefly the responsibility of *Financial Services Authority* and the *Office of Fair Trading* and finally, (iii) the inability or unwillingness of the County Courts to exercise application of the law in relation to examining the terms and conditions of the contracts, due scrutiny of the defendant's defence statements, examining fully the *claimant's locus standi* and examining the *bona fides* of the claimant's alleged calculations of arrears which are often substantially comprised of unlawful and therefore unrecoverable charges.

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[35] http://www.homemove.co.uk/news/22-06-2009/cml-revises-repossession-forecast-downwards.html

SUBMISSION

Origination:

4. Almost without exclusion most *sub prime* mortgages originate through a broker. These brokers have clear responsibilities under law. The lenders also are governed by responsibilities for the broker's actions.[36] It is sadly far from uncommon that brokers act with cavalier disregard for the consumer. It is paramount that the deal is struck and the commission is paid. The commission is then added on to the loan, and compound interest is added over the lifetime of the mortgage.

5. The consumer of such products will inevitably pay a higher rate of interest (between 8 and 14% is not uncommon) on even relatively small 2nd charge mortgages. The assumption has hitherto been that the consumer in question is a higher category of risk. Often these will have been the very consumers who have fallen foul of punitive and unlawful charges in other aspects of their finances, thus resulting in negative, and sometimes unlawful, entries on their credit references. It is worth noting that the vast majority of bank charge and credit card or other personal finance settlement claims have *not resulted* in a full removal of default notices applied to the consumer's credit record, thus artificially creating this "higher risk category" of consumer. In this respect the consumer is therefore pressurized (if not forced) into the "specialised" sector of the market for his, her or their mortgage.

6. Further, it is never fully and transparently disclosed in *plain and intelligible terms* that the consumer has contracted to a contract which provides that the mortgage will then be "marketed" and sold as an investment opportunity. The typical attraction of these "notes" for the investor are the high rates of interest, *and crucially*, their early redemption period. To clarify for the committee: early redemption in respect of these mortgages does not usually mean that the borrower is able to pay off the mortgage earlier than the stipulated term. It typically means asset stripping the equity in the mortgagee's home through repossession. The lender thereby has a vested interest in pursuing an aggressive repossession strategy. At no time has any consumer of these mortgage products consented either expressly or otherwise to the subsequent sale of their mortgage, nor typically was he or she ever informed.[37] The issue of securitization and subsequent consumer detriment has been submitted before this committee in prior submissions on the banking crisis.

7. Terms are not individually negotiated, and express consent to all terms whether lawful of not is not possible.

Operation and performance

8. There is growing disquiet concerning the treatment of consumers in the sub prime sector.[38] The anecdotal evidence, behind which lies a real life story, is also growing. The costs of family breakdown as a result of malicious and often unlawfully premised repossession will mount if serious regard is not in the first instance given to lender's lawful responsibilities, and the *duty of enforcement* by the various regulatory authorities and services.

9. The scale of misconduct and consumer detriment is enormous. In a submission of 3000 words it is impossible to even begin to scratch the surface of the seriously deficient maladministration of consumer accounts, the mistreatment of consumers including those who *are able* to meet their onerous obligations, and the treatment of those who fall short of meeting theirs. The mortgage products are deliberately designed to result in *alleged* default, typically within a three to five year period of origination.[39]

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[36] The Non-Status Lending Guidelines for Lenders and Brokers issued by the OFT in July 1997 and revised in November 1997 apply to all secured loans made to "non-status borrowers". The Guidelines provide guidance as to the activities of lenders and brokers in the non-status secured lending market in areas such as advertising and marketing, loan documentation and contract terms, selling methods, underwriting, dual interest rates, flat interest rates and early redemption payments. According to the Guidelines, advertising and other promotional material must be clear and easily legible and should not be misleading, and the Guidelines prohibit unfair sales tactics. Brokers are obliged to disclose at the outset of the transaction their status with regard to the borrower and the lender, together with details of any fee or commission payable to them as broker or if they are tied to a particular lender. Lenders must take all reasonable steps to ensure that brokers and other intermediaries regularly marketing their products do not engage in unfair business practices or act unlawfully, that they serve the best interests of the borrowers and explain clearly the documentation and consequences of any breach or early repayment by the borrowers. The actions of any broker or other intermediary involved in marketing a lender's products can jeopardise the lender's fitness to hold a consumer credit licence, and the Guidelines make clear that lenders must take all reasonable steps to ensure that such brokers and other intermediaries comply with the Guidelines and all relevant statutory requirements. This is so even if the lender has no formal or informal control or influence over the broker.

[37] "The effect of (i) not giving notice to the Borrowers of the sale of the relevant Loans and their Collateral Security to the Issuer and the charging of the Issuer's interest in the Loans and their Collateral Security to the Trustee and (ii) the charge of the Issuer's rights thereto in favour of the Trustee pursuant to the Deed of Charge taking effect in equity (or extending over the Issuer's beneficial interest) only, is that the rights of the Issuer and the Trustee may be, or may become, subject to equities as well as to the interests of third parties who perfect a legal interest prior to the Issuer or the Trustee acquiring and perfecting a legal interest" SPML *Offering Circular to Investors 8 August 2005 p.69*

[38] http://www.consumeractiongroup.co.uk/forum/mortgages-secured-loans/170607-spml-london-mortgage-company.html

[39] Prior to enforcement, the Notes will be subject to mandatory redemption in part on each Interest Payment Date in accordance with Condition 5(b) (*Mandatory redemption in part of the Notes*). This mandatory redemption in part will be funded primarily by scheduled principal payments by the Borrowers under the Loans and principal prepayments (whether voluntarily by the Borrowers, as a result of enforcement of security in respect of the related Property or otherwise) and/or by Loan Sale Principal Proceeds not applied to purchase Additional Loans. (Source Mortgage Funding PLC 2008-1 Prospectus, 18th March 2008) p.14.

10. Consumers of these products will variously and typically experience the following:

(a) failure of notification of the fact that their mortgage has been securitized usually within three to six months;

(b) absence of consent to a disposition of property as mandated by law

(c) failure to lawfully perfect the sale of the mortgage

(d) Failure of notification that by default any sub prime mortgage is placed on a block building insurance policy even if the consumer of the mortgage product has valid buildings insurance; compound interest is charged thereon;

(e) alleged none payment where payment has been tendered;

(f) alleged late payment where payment has been tendered upon date due;

(g) falsely alleged shortfalls in payments;

(h) failure to change payment due date to reflect that not all consumers are paid on regular dates or even the same date as collection is deemed due;

(i) false entries onto consumer accounts regarding alleged failed payments;

(j) failure to correct such entries after complaint;

(k) failure to amortize the debt with payments made over and above the interest due, thus creating a higher level of compound interest over the term of the mortgage and increasing over time the likelihood of default;

(l) failure to acknowledge consumer complaints;

(m) failure to respond within a reasonable time scale to consumer complaints;

(n) failure to comply with Data Protection Subject Access Requests;

(o) willful ignorance of duties under CPR 31.6 in respect of planned or listed litigation;

(p) commission of offences against both the *Telecommunications Act 2003* and the *Harassment Act 1997* in the form of unwarranted and intrusive telephone calls often designed to cause embarrassment for example with frequent calls made to the consumer's workplace; unlawfully threatening repossession via a telephone call;

(q) routine monthly access to and entry upon consumers credit reference files;

(r) Unlawful and punitively raised charges with no prior notification of their application; compound interest applied thereon;

(s) Failure to provide a breakdown of solicitors cost; dumping said costs onto arrears and applying compound interest thereon;

(t) undue haste in litigation and claiming to observe the CJC pre action protocols but failing *absolutely to do so.*

(u) Threatening consumers with costs which are at the discretion of the court;

(v) Breaches of the *FSMA* (2000); *Mortgage Conduct of Business (MCOB)* rules; the *UTCCRs* (1999) The *Unfair Consumer Practices Directive* (2008) and where applicable the *Consumer Credit Act* (2006); breaches of the criminal law in failure to register that a disposition of land has taken place (s.2 *Property Act*, 1989, s.127 *Land Registry Act* 2002); breaches of s.1 and s.5 of the *Fraud Act*, 2006.

(w) In litigation, failure to seek possession only as a *last resort;* failure to serve documents upon the defendant; failure to offer to capitalize genuinely constituted arrears; failure to accept temporarily reduced payments without inferring delinquency; failure to accept payments from customers in arrears where the full alleged arrears is not tendered, failure to refund unlawfully applied charges and compound interest applied; failure to waive charges where a performing arrangement for arrears clearance is in place;

(x) In suspended cases, the application of charges without notice in excess of the overage paid by consumers to clear their arrears; misrepresentation to the courts that such arrangements will clear the arrears when typically they will not, as a consequence of yet further charges disguised with various nomenclature as *arrears management fee, litigation fee, arrears interest, interest charged* and so on;

(y) Willful exaggeration of the consumer's genuine level of arrears, which may be typically half of the overall total claimed.

Post possession treatment

11. The willful mistreatment of consumers does not end with possession. Rather this is just the beginning. Consumers will be faced with costs in respect of: eviction; clearance and storage of goods; locksmiths; often unnecessary "improvement" to the property; valuation fees; estate agency costs and ancillary legal fees; finally there is the grossly excessive "early redemption figure" which in absence of a true redemption should not be charged at all but in practice is used to strip the remaining equity out of the property; post—possession harassment of consumers is sadly as common as the harassment endured pre-possession.

12. Multiple anecdotal evidence of such treatment is available in the form of often desperate postings made to consumer web sites. Such information is readily available to committee members; see for example the consumer action group's website.

Regulatory failure

13. A strange conundrum arises when one considers the regulatory framework that binds the operation of consumer contracts including mortgages. Historic and recent legislation and regulations, *prima facia,* provide the consumer with a great deal of protection from unfair terms, contractual irregularities or breaches and unlawful conduct by the credit provider. The conundrum is a simple and powerful one. *How is such treatment of consumers even possible?*

14. The *FSA* took on responsibility for mortgage regulation in 2004. FSA Statutory objectives include securing the appropriate degree of protection for consumers (*The Financial Services and Markets Act 2000 (Part 1, Section 3)*

15. The FSA also regulates by reference to its own principles of good regulation amongst which are that a firm must conduct its business with due skill, care and integrity; observe proper standards of market conduct and pay due regard to the interests of its consumers and treat them fairly. Finally a firm must take reasonable care to ensure the suitability of its advice and discretionary decisions for any customer who is entitled to rely upon its judgment.

16. The FSA's own performance report has nine high level indicators by which to assess performance in achieving its strategic aims. Indicator four is particularly instructive: (4)Firms are financially sound, well managed and *compliant with their regulatory obligations;*

17. Furthermore in reference to the FSA *Treating Customers Fairly—outcomes for consumers*, July 2006.

> "Consumers can be confident that they are dealing with firms where the fair treatment of customers is central to the corporate culture. Consumers are provided with clear information and are kept appropriately informed before, during and after the point of sale"

Further:

> "*Consumers do not face unreasonable post-sale barriers imposed by firms to change product, switch provider, submit a claim or make a complaint."*

18. If a firm breaches FSA's rules, enforcement action may follow. If enforcement action is taken the FSA has a range of disciplinary, civil and criminal powers which it can use against regulated and non-regulated firms. The sanctions include financial penalties, removal of authorisation or even criminal prosecution in cases of misconduct.

19. Additionally, *The Unfair Commercial Practices Directive (UCPD 2008)*[40] seeks to protect consumer interests from unfair business-to-consumer commercial practices. In particular, commercial practices will be unfair if they are misleading (this includes both acts and omissions) or aggressive.

20. Further the UTCCRs (1999) provide that: (a) a consumer may challenge a standard term in an agreement on the basis that it is "unfair" within the Regulations and therefore not binding on the consumer.

21. The scale of consumer detriment by consequence of the practices identified in *paragraph 10*are part of the corporate culture of the so called "sub-prime" market. Such practices represent clear contempt for the rules and regulations the FSA in conjunction with the OFT and the FOS have laid down.[41] Regulation is *clearly insufficient.* Only the FSA, together with the FOS and the OFT can give consumer protections real effect. *Qui custodientipsoscustodes?*

22. There has been much recent discussion elsewhere that the regulatory systems and authorities have failed in their primary duties of oversight and compliance and that better governance is needed.[42] It is submitted before this committee that where the law is clear then observation of the various laws and regulations *must be enforced. In absentia* the rule of law and the sovereignty of parliament are subjugated to the will of the finance industry, a clear case of the tail wagging the dog.

[40] http://www.berr.gov.uk/whatwedo/consumers/buying-selling/ucp/index.html
[41] http://www.fsa.gov.uk/pubs/other/concordat08_fsa_oft.pdf
[42] http://www.ft.com/cms/s/0/b92f8ef2-578b-11de-8c47-00144feabdc0,dwp_uuid=5158848c-b6a7-11db-8bc2-0000779e2340.html

23. The regulatory instruments are clear but seem unable to prevent breaches so as to lack effect. The FSA seems unable to sanction firms breaching its own regulations, often arising from EU directives, which if inadequately applied lay the state itself (or various emanations thereof) potentially open to damages claims, chiefly under the *Francovich principle*.[43]

The role of the County Courts

24. The FOS may take many months to investigate individual complaints against traders[44] and since the process of repossession is often very swift, it invariably falls to the courts to ensure the application of the *overriding objective* of the *Civil Procedure Rules.*

25. In many, if not all instances, the consumer is a litigant in person, in ignorance of the law. Anecdotal evidence suggests that the litigant in person does not receive fair treatment before the courts, with defence statements summarily dismissed in some cases.[45]

26. In possession claims the courts rely on four outmoded assumptions. These are as follows. (a) that repossession doesn't benefit the lender and that therefore the lender will avoid it whenever they can; (b) that only people who have built up unsustainable arrears will be repossessed; (c) that the alleged arrears are always accurately calculated; (d) that where breaches of an arrangement are made these are borrower breaches and *never* lender breaches.

27. Under [2000] EUECJ C-240/98[46] courts are mandated by operation of this decision to assess the fairness of the terms of a contract on the consumer's behalf, even if the consumer does not ask the court to do so. On this premise alone the legality of many thousands of possessions which have already taken place is subject to challenge. There has been a visible error in law where courts have not assessed the fairness of the terms of the mortgage contract.

28. The courts also fail in the primary duty to place claimants to a strict burden of proof that they retain *locus standi* following securitisation of mortgages in the mortgage pool. Possession is a drastic measure of last resort and should only take place where the *locus standi* of the claimant is *fully satisfied*. References to the Land Registry entry of charge and the mortgage deeds are insufficient given the practice of securitisation, where the originator of the loan clearly states in their *Offering Circular* that they do not "currently intend to effect any registration at the Land Registry of England and Wales."[47]

29. Further the court sanctions an abuse of its own process when it allows suspended orders to be made or suspended orders to become full possession orders. Without *full satisfaction* of the claimant's *locus standi* there can be no right of claim.

Conclusion

30. *This submission has been presented in a personal capacity by the witness, as a consumer of a "sub-prime" mortgage product.*

31. The overall impact of these widespread practices is that consumers are being serially and unlawfully overcharged, treated with contempt and subject to reprisals when making complaint. They are then ultimately (and often unlawfully) repossessed, in addition to which the equity is then stripped from their homes with hugely disproportionate early redemption charges, following on from repossession. Often their only valuable asset is knowingly undersold in order to realize any cash value remaining, in an uncertain property market, not for the benefit of the former owner, but for the benefit of the possessing party, and on the behalf of those for whom they act, as a consequence of the securitization process.

32. Furthermore, the *Financial Services Authority* and the *Office of Fair Trading* have failed in their duty to regulate effectively these firms, the *Financial Ombudsman Service* is too slow to act on consumer complaints and enforce the regulations in this area, and the courts themselves consistently fail in their duty to examine the fairness of standard terms in the terms and conditions of the relevant mortgage contracts as they are mandated by virtue of *Murciano Quintero (Environment and consumers) [2000] EUECJ C-240/98 (27 June 2000)*.

33. The courts place too much faith in outmoded concepts of the "honourable" wronged lender seeking a last resort lawful remedy for breach by a "delinquent" consumer, when in fact it is the lender that is delinquent in origination and subsequent operation and performance of the contract.

34. The devastating cumulative impact is as follows; family breakdown, homelessness, unemployment and increased child poverty and neglect. Few studies have been conducted but one such study was reported as follows: Understanding the social consequences of mortgage repossession by Sarah Nettleton, Roger Burrows, Jude England and Jenny Seavers, and was published on behalf of the Joseph Rowntree Foundation by York Publishing Services Ltd.[48] These are the inevitable but entirely avoidable consequences

[43] http://www.eurofound.europa.eu/areas/industrialrelations/dictionary/definitions/francovichprinciple.htm
[44] http://www.financial-ombudsman.org.uk/publications/consumer-leaflet.htm
[45] http://www.consumeractiongroup.co.uk/forum/mortgages-secured-loans/170607-spml-london-mortgage-company.html
[46] http://www.eipa.eu/files/repository/product/20070813130142_EA_07_w_01e.pdf
[47] *SPML/SPPL Offering Circular to Investors 8 August 2005 p.69*
[48] http://www.jrf.org.uk/sites/files/jrf/F829-social-consequences-mortgage-repossession.pdf

of the drive for possessions neither mandated in law or in any meaningful sense *fair* to the consumer. The regulations are adequate (though far from perfect); compliance with the regulations is woeful. Exhortation has failed. It is time for the "big stick" of compliance *enforcement*.

June 2009.

Written evidence submitted by moneysupermarket.com

ACCESS TO MORTGAGE FINANCE FOR FIRST TIME BUYERS

Executive Summary

The problems in the mortgage (and therefore housing) market are on the supply side. There has been a catastrophic decline in the availability of mortgages—in terms of the number of products, the Loan To Value at which they are available and the acceptance criteria. This has particularly impacted First Time Buyers.

About moneysupermarket.com

moneysupermarket.com is the UK's leading price comparison website. Our position in the market gives us two major strengths—firstly, we have an overview of the entire mortgage market as we display all mortgage products on our website. Secondly, we have a unique insight into what consumers are doing as we have millions of UK consumers visit our site each month and we can track their mortgage search and buying habits.

moneysupermarket.com is listed on the London stock Exchange and is included in the FTSE250. We are based in Flintshire, North Wales where we employ around 450 staff. In 2008 we had over 120 million visits to our website—which enables consumers to compare and buy products including mortgages, savings accounts, credit cards, car insurance, home insurance, utilities and broadband.

EVIDENCE

1. Since a high point in the summer of 2007 there has been a catastrophic decline in the availability of mortgage finance. The total number of available products has fallen from over 30,000 to around 2,000 (graph one attached).

2. First Time Buyers (FTBs) have been particularly hard hit—the total number of products available to them has fallen from approx 20,000 to approximately 1,000.

3. Even this masks a more serious issue—although these products are nominally available, the reality is that they are not available at the higher loan to value amounts required by FTBs.

4. As you can see from the table below the number of products available at 90% LTV and above has fallen from a peak of 3,481 to 127.

Date	*Number of Products available at 90% LTV*	*Average Rate*	*BoE Base Rate*	*Difference*
Jan 2007	3148	6.20%	5.00%	1.20%
Jun 2007	3481	6.51%	5.50%	1.01%
Jan 2008	1541	6.72%	5.50%	1.22%
Jun 2008	785	7.73%	5.00%	2.73%
Jan 2009	179	6.24%	2.00%	4.24%
Jun 2009	127	6.29%	0.50%	5.79%

5. Over the same period the cost of those 90% plus loans has actually increased, despite the Base Rate falling by 4.5%.

6. The problem is not limited to 90% plus loans—as graph two shows all lending over 75% LTV has been significantly reduced.

7. The decline in higher LTV mortgages will have an exaggerated impact as the decline in house prices over the past two years will have reduced the equity that all homeowners hold in their property.

8. Research conducted by moneysupermarket.com in June 2009 (amongst 4,021 UK adults) shows that 16% of homeowners had bought their property with a 100% mortgage. There are now just two lenders offering these products. A further 7% of homebuyers took an additional loan (other than their mortgage) to borrow the deposit for their property.

9. As well as the decline in the number of mortgage products, and the restrictions in higher LTV lending, our figures also indicate that lenders are reducing salary multiples and tightening other lending criteria. Whilst these hit all new borrowers they are particularly restrictive for first time buyers, who tend to have to stretch themselves the most.

10. Some areas of the mortgage market have almost completely disappeared—such as buy to let mortgages. In addition mortgages for people with a patchy credit record (perhaps a CCJ for missed utility bill payments in the past) are now close to non-existent. Some figures suggest that there are 17m UK adults who are now financially excluded in this way.

11. We are not suggesting a return to the lending market of two years ago—when arguably credit of all sorts was too readily available and risk was not adequately factored into cost.

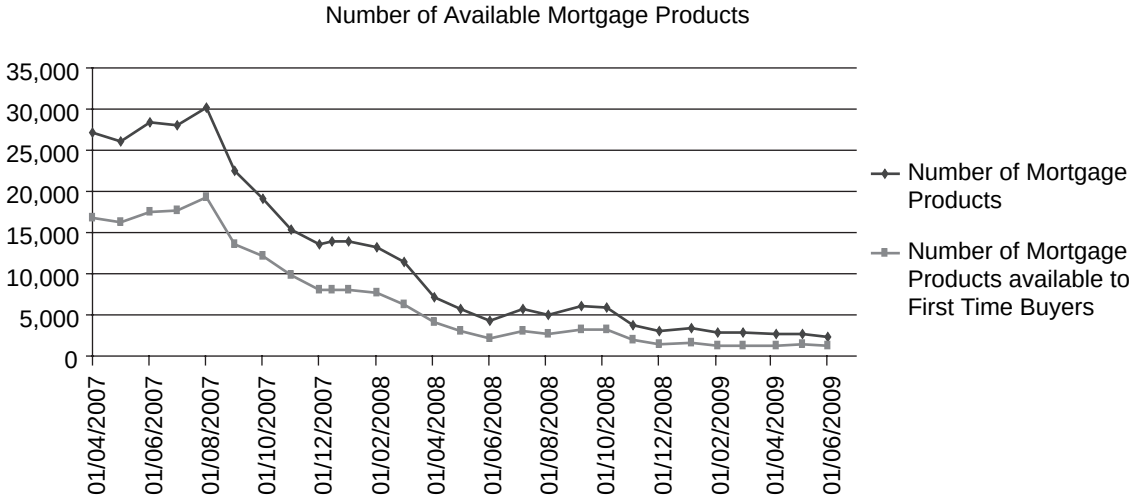
12. However we are suggesting that whilst banks and building societies are insisting that they will maintain lending, the reality is that mortgages are not available for a very great many consumers, in particular First Time Buyers. Until this changes, and we see a much more inclusive approach to lending, there is no real prospect of a sustainable upturn in the housing market. We have not seen a decline in the number of people search for mortgages—in fact they have been rising. The crisis in the mortgage market is on the supply side.

We hope you find this useful. We'd be happy to provide additional information if required.

July 2009

Graph 1

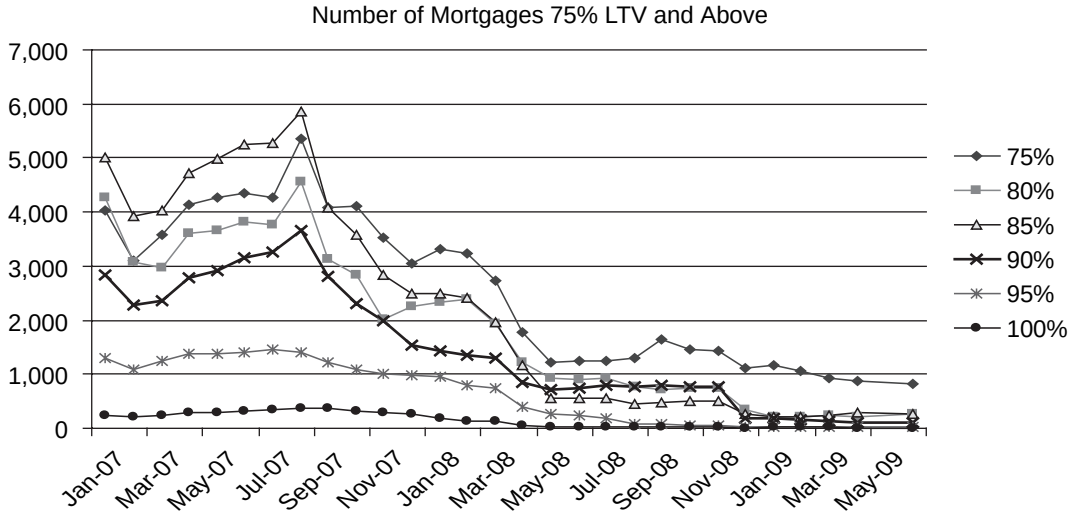
NUMBER OF AVAILABLE MORTGAGE PRODUCTS OVER TIME



Sourced by www.moneysupermarket.com

Graph 2

AVAILABILITY OF MORTGAGE PRODUCTS BY LTV BAND OVER TIME



Written evidence submitted by the Home Builders Federation (HBF)

Introduction

1. The Home Builders Federation (HBF) is the principle trade association representing the interests of private housebuilders in England and Wales. Our members, who include companies ranging from major national firms, through regional companies to smaller local companies, are responsible for more than 80% of the new homes built every year.

2. The following comments relate to the final bullet point of the Terms of Reference:

3. *"The impact of the credit crunch on access to mortgage finance and the terms on which such finance is offered to first-time homebuyers."*

4. The home building industry is reliant on the availability of mortgage finance for a large proportion of its sales. Therefore the health of the mortgage market is critically important for housing output, house building jobs, and the wider economic and social benefits of new housing supply.

5. The credit crunch first hit the home building industry in Autumn 2007 when the availability of mortgage finance was suddenly severely curtailed. Since then, private housing starts have fallen very steeply. Until the flow of mortgage finance is restored, and mortgage terms eased, the industry will not be able to raise housing output significantly.

Detailed Comments

6. Home builders report no easing in the severely restricted availability of mortgage finance, whether for first-time buyers or other categories of buyers.

7. Mortgage terms remain highly restricted. It is difficult for buyers to borrow more than 80% of the purchase price. Low loan-to-value (LTV) ratios hit first-time buyers particularly hard as they rarely have a significant deposit.

8. Where higher LTV ratio mortgages are available, the mortgage rate is significantly higher. Rates can vary by as much as three percentage points between LTVs of 70% and 80–85%. This again hits first-time buyers particularly hard.

9. Some lenders differentiate between loans on new and second-hand properties, with loans on new properties at less favourable terms or limited in scope, further compounding the adverse impact of limited mortgage availability on home builders.

10. Many house builders have gained the impression that lenders are looking for any reason to refuse a loan. Credit scoring has been tightened, much more information is sought, and loan refusals can be made on the smallest of details.

11. Lenders change their rates and terms constantly. Even more worrying, house builders report that these changes are made, or even products withdrawn altogether, after buyers have had a mortgage offer and during the buying process, sometimes as late as just before exchange of contracts. As a results, sales fall through after buyers have paid out for solicitor's costs and valuation fees. These abortive costs can be a severe burden for cash-strapped first-time buyers. The principle should be that lenders cannot change the rate or terms of a loan once they have made an offer, subject to the normal time limit on such offers. They should not be able to change these unilaterally mid-process, to the detriment of home buyers and home builders.

12. At present, we understand just three lenders are responsible for a high proportion of lending on new homes, leaving the industry in a very vulnerable position. While this is not in any way a criticism of these three lenders, whose support is highly valued, we are concerned about the short and longer-term implications. Lenders accept only a limited exposure to any one development site, so that when a lender has reached this maximum, the house builder is left with only two, or even one major lender willing to lend on this site. In the longer term, we are concerned about the availability of mortgage finance and competition in the wider mortgage market, particularly in relation to new homes.

13. Many home builders have introduced shared equity products to help buyers get over the deposit requirements of lenders. It is therefore very frustrating when lenders still require a 5% or 10% deposit. In the case of, say, a 70%/30% shared ownership sale (the buyer pays 70%, the developer effectively lends the buyer the remaining 30% via a second charge), the lender's risk is limited to 70% of the sale price, which is a very low risk. So it is unnecessary to require a deposit from the buyer on risk grounds.

14. The Government's HomeBuy Direct (HBD) product, which the industry keenly supports, has two lenders willing to lend 100% on the 70% of the price funded by the purchaser, but the other three lenders require a deposit from the first-time buyer. As the whole point of HBD is to allow cash-strapped first-time buyers to get over the deposit requirements imposed by lenders, and the developer and Government take the first 30% risk, this is self defeating and undermines the effectiveness of the scheme.

15. If the Committee wishes to follow up on any of the comments in this submission, we would be pleased to assist, including putting the Committee in touch with member companies for direct evidence.

July 2009

Written evidence submitted by Genworth Financial

1. Number of Homeowners in Mortgage Arrears

We have noted with interest some of the latest figures published by the Council of Mortgage Lenders (CML) which show that:

— Arrears and repossessions both rose in the first quarter of 2009, but remain lower than they were at their peak in the last recession in the early 1990s.

— The number of voluntary possessions rose more sharply and accounted for 27% of the total, compared to 14% a year ago.

— The current forecast is for a total number of 65,000 cases of repossession in 2009 out of a total number of 11.1 million mortgages.

The Committee will be interested in an innovative scheme that Genworth Financial has launched in the US and Canada and hope to introduce in the UK and other parts of Europe to limit repossessions. The Homeowner Assistance Programme works with lenders and borrowers to find alternative solutions if a borrower is in financial difficulties. We provide borrowers with insight into how our loss mitigation process works, and we partner with lenders to provide customers who show signs of being in financial difficulties with educational material.

By brokering payment solutions between the different parties involved, we have prevented foreclosures on more than $2 billion worth of mortgages in the US during the 12 months ending in March 2009. During this time we completed more than 15000 successful mortgage "workouts", which typically involve changes to the repayment plan or to the original terms of the loan. For a more detailed breakdown by state, please refer to our Foreclosure Prevention Scorecard at: http://smartermi.com/homeowner-assistance.asp

2. Adherence to Codes of Conduct and Statement of Good Practice

Whenever we do business with lenders, including in the UK, we expect our clients to adhere to Genworth's *Gold Standard in Mortgage Lending*, which is attached in Annex I. These standards were reflected in Sir James Crosby's Review on Mortgage Finance of November 2008, and we continue promoting them as industry best practice in all markets in which we operate.

Genworth's mortgage scoring data from lenders show that delinquency rates of loans over 80% LTV are almost double in cases where the gold standard has not been applied.

We recommend that the Government:

— Build on international experience and promote greater use of Mortgage Insurance or other credit risk mitigants to manage risk in mortgage lending and support access to homes for first-time buyers.

— Promote a gold standard in mortgage lending, consisting of responsible lending criteria including strict underwriting standards, transparency and standardisation to help the mortgage funding markets.

3. Impact of Credit Crunch on Access to Mortgage Finance for First-Time Buyers

The issue

It is now widely recognised that as a result of the credit crunch, banks have been pulling back on high loan to value (HLTV) lending, which has a disproportionate impact on first-time buyers who may have perfectly good credit histories and stable incomes, but are unable to get a foot on the housing ladder. There are two principal reasons for retraction in this area:

— A lack of funding available to banks due to shortages in the wholesale funding markets

— Banks are choosing not to lend to HLTV customers due to the additional regulatory capital requirements associated with those loans.

To illustrate the current bottlenecks in the system, the Moneysupermarket website (www.moneysupermarket.com) reports just 102 mortgages that are currently available at 90% LTV, compared with 3,148 such products back in January 2007. This represents just 3% of the previous range.

What we currently see in the marketplace is that loans to first-time buyers reached an all-time low of 30,100 in the first quarter of 2009, compared with an average of 110,000 per quarter over the preceding decade. A median LTV of 75% represents the typical maximum offered by most lenders today, compared to an average of 90% LTV for most of the last decade. Some lenders also say that as a result of new capital requirements they can originate significantly more low LTV mortgages for every high LTV mortgages.

The virtual disappearance of HLTV lending has an impact on the rest of the market. The absence of first-time buyers (as well as falling house prices pushing approximately 2 million existing borrowers into low or negative equity) constrains activity on subsequent steps on the housing ladder, as people looking to trade up are unable to find buyers for their property.

A Genworth Solution Presented to Government

We noted with interest the announcement of the Government's scheme for asset-backed securities and consider this as a constructive first step in addressing the current funding crisis that affects the mortgage market. However, we are concerned about the practicalities of implementing the scheme effectively.

Practical implementation of Sir James Crosby's central recommendation will require a number of specific capabilities:

— Setting prudent underwriting criteria for mortgage lending, including appropriate standards for high loan to value loans, which are vital in re-starting the housing market.

— Pricing that risk.

— Implementing and administering the guarantee scheme including compliance with lending criteria.

— Tracking and analysing the performance of loan portfolios.

— Provisioning and reserving for delinquent loans.

— Deciding what constitutes a valid claim under the guarantee. This is vital to mitigate against moral hazard.

— Implementing loss mitigation measures in order to reduce risk exposure and to keep borrowers in their homes where possible.

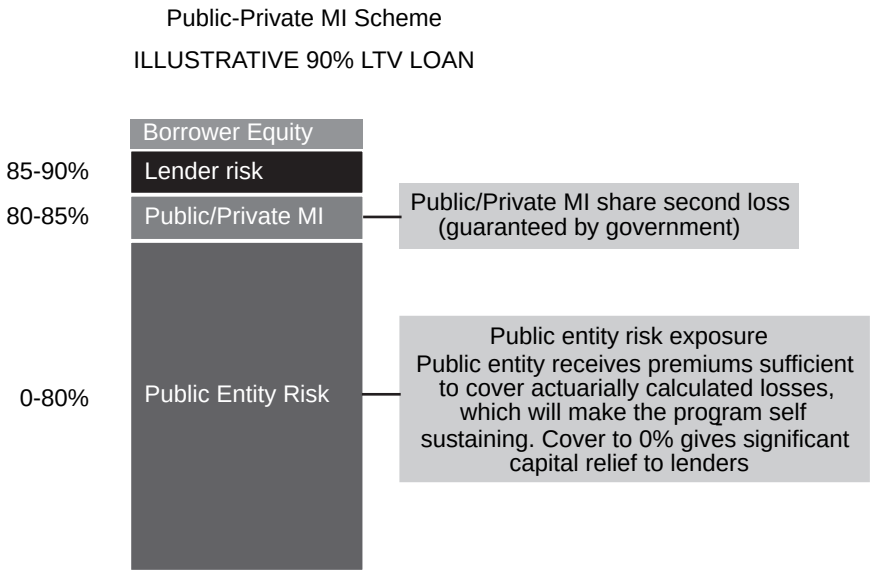
These tasks require specialist capabilities that are scarce in the market. The Government should take advantage of the existing Mortgage Insurance (MI) industry in order to facilitate the implementation of the scheme. For example, Genworth has been active in the Mortgage Insurance market in Europe since 1993 and has developed its expertise in underwriting, pricing, assessing risk, analysing performance data on loan portfolios and loss mitigation. We are ready to share this specialist knowledge, as a first step towards a long-term, sustainable solution.

Currently, the Government guarantee on asset-backed securities will only be realised if there is an "AAA" stress in the market. Investors have inferred to us that they do not see this as a likely scenario and therefore the guarantee may have a limited effect in providing a lasting solution to the RMBS market.

Instead, by introducing a loan-by-loan insurance scheme, underwritten by the Government and with the MI industry as a government guaranteed minority risk partner, investors would have full confidence that any losses on RMBS would be recoverable. Combined with prudent and sustainable underwriting, agreed between lenders and MI providers, the quality of assets originated would be safeguarded. The importance of the MI provider with considerable relative experience and critical mass is crucial, as is their expertise in mortgage originations and independent risk management.

We acknowledge that today there is not enough capacity in the private sector to insure the entire mortgage market. Therefore we recommend a two-stage approach. Namely, during the initial period the state would act as a direct guarantor, with MI providers as notional risk partners. Over time, as capacity in the private sector expands, the state would reduce its role from being a direct insurer to being a guarantor of the private MI providers. This is in fact how the Canadian model has evolved.

Given that governments in general do not have the expertise to design and administer such programmes, we feel that a new approach, along the lines of the model below, is needed which combines the best elements of the public and private sectors.



Advantages of a public-private insurance-partnership scheme:

— Existing industry used as part of market-based solution

— Not "reinventing the wheel"—MI providers have systems and expertise to implement system quickly and efficiently

— Government guarantee of mortgage insurance provides comfort to re-start RMBS/CB markets and subsequently new mortgage lending

— Has the support of major lenders

— Private sector insurance reduces UK taxpayer risk exposure and makes the programme more sustainable.

Conclusion

We urge the Government to consider developing a partnership with Mortgage Insurance providers in order to prudently and efficiently provide a lasting and sustainable solution for the wholesale mortgage market. This will ensure an outcome that is attractive to the banking and investor communities, coupled with advancing the Government's aims.

We recommend a model that follows the evolution of the Canadian mortgage market. It would give a central role to Government in the short term and would take advantage of the specialised capabilities that exist in the private sector. This solution is designed for sustainability by allowing the private sector to expand and transition the Government's role to that of guarantor. The Canadian model provides a roadmap for the evolution of a similar system in the UK.

Insurance-based systems of mortgage finance have a precedent in Canada that has functioned well, even during the last 18 months of unprecedented global financial turmoil. We urge the Government to review the Canadian model and implement a similar scheme, appropriate to the UK market, at the earliest opportunity.

Background to Genworth Financial

Genworth Financial is a leading financial security company serving the lifestyle protection, retirement income, investment and mortgage insurance needs of more than 15 million customers, with operations in 25 countries.

In the UK, Genworth focuses on two product lines—Lifestyle Protection insurance for individual consumers and Mortgage Insurance for lenders. These products play a valuable role in providing long-term stability for borrowers and lenders and expanding sustainable homeownership.

Genworth's expertise gives a clear perspective on some of the most critical global economic trends, their impacts and how they might best be mitigated in the UK.

Genworth has embedded the FSA's principles of Treating Customers Fairly into all aspects of our business. We believe in providing customer choice and customer service. We are committed to transparency and furthering consumer education. We also believe in playing by the rules and strongly endorse any regulation that eradicates mis-selling.

For more information please contact Jürgen Boltz, Government Relations UK & Ireland on 020 8380 2164

To see more about our business, visit www.genworth.co.uk

Genworth Financial Mortgage Insurance:

Our Mortgage Insurance product can help lenders and investors in the event that a mortgage borrower defaults on a loan and the proceeds of the sale of the property after repossession are insufficient to pay the outstanding debt. As well as offering growth opportunities in some sections of the mortgage market, MI reduces loss volatility from the transfer of credit risk, makes for more efficient use of capital and enhances the quality of mortgage-backed bonds, facilitating funding. Our products can provide the borrower with earlier and potentially more affordable access to home ownership by enabling a lower initial deposit.

June 2009

Annex I

THE GOLD STANDARD IN MORTGAGE LENDING

1. Responsible Lending

We support and advocate a return to prudent and responsible lending, with LTV not exceeding 90%. Only in exceptional cases would we support lending up to 95%.

HLTV loans entail an element of risk but are here to stay as credit demand continues from borrowers with disposable income. These borrowers tend to be young, educated and with good prospects but no deposit—they do not deserve to be marginalised. Mortgage insurance (MI) can bridge the gap between the needs of

these consumers for credit and the concerns of lenders who need to transfer HLTV-related risk, as MI providers have the incentive and the expertise to assess the true nature and extent of that underlying risk. HLTV mortgages are not the same as sub-prime mortgages.

Quality standards have been adopted in other markets such as Canada, where there is a statutory requirement for mortgage insurance on all loans exceeding the 80% LTV threshold. This creates a balanced risk pool, eliminating the problem of adverse selection and lowering costs. The transfer of default risk and prudential quality standards also act as a stabiliser to the overall financial system and economy in Canada.

2. Transparency in Underwriting

Consistent and transparent standards are needed for establishing the two primary factors which determine any residential mortgage lending decision: the creditworthiness of the borrower and the value of the collateral against which the loan is being made.

Sometimes the absence of credible and reliable information leads to inappropriate lending decisions and allocation of capital to risk. Clarity and consistency in establishing the L and the V in LTV are essential for delivering transparency and so restoring confidence in the market.

3. Risk-related Capital Levels

As a leading global provider of residential mortgage insurance, we have significant experience in several countries of the performance of high loan-to-value (HLTV) mortgage loans in good times and bad. While it is generally true that mortgage lending is one of the safest forms of lending, experience demonstrates that over the full economic cycle HLTV lending represents a significantly riskier portion of the mortgage lending market. It is therefore critical that higher levels of capital are held to reflect the increased risk, and that incentives exist to manage this risk properly.

Written evidence submitted by The Paragon Group of Companies

Executive Summary

Paragon welcomes the opportunity to submit evidence to the Treasury Select Committee's inquiry into mortgage arrears and access to mortgage finance. This submission focuses on:

— Paragon's approach to mortgage arrears;

— the importance of the Receiver of Rent process to private tenants and lenders in the event that borrower landlords run into financial difficulties; and

— the impact of ongoing problems in wholesale funding markets on the supply of finance into the private rented sector, and the lack of policy progress in this area.

Paragon is the UK's leading specialist provider of residential mortgages to professional and investor landlords. We launched our first specifically targeted mortgages in 1995 and over the last 14 years have increasingly specialised in this market. We are currently the UK's third largest lender on privately rented residential property and have approximately £9.5 billion of assets under management. We are a leading member of the Council of Mortgage Lenders and the Intermediary Mortgage Lenders Association.

Due to Paragon's conservative lending policies, the performance of our originated assets is materially better than the industry average and we have remained profitable despite current market conditions. In addition, we have received no support from Government.

In a recessionary environment, the private rented sector takes on increased significance, which can be evidenced by the experience of the recessionary years of the early 1990s, when the private rented sector experienced its fastest period of growth, expanding by nearly a fifth between 1990 and 1995. Many individuals, particularly potential first-time buyers, are having increasing difficulty securing mortgage finance or are putting off home purchases while the housing market remains unstable, and private landlords are providing an increasingly vital source of affordable and flexible accommodation for many people.

Private landlords, using buy-to-let mortgage finance, have played a key role in responding to tenant demand for private rented property over the last 15 years. Sustaining this investment is increasingly important in the current economic climate. However, the closure of wholesale funding markets has prevented non-deposit taking institutions, from this point referred to as non-banks, from continuing to meet this demand. According to independent research, there has been a 95% reduction in available buy-to-let mortgage products in the past two years and only two of the top 10 buy-to-let lenders from 2007 are currently writing new business in this sector. Measures must therefore be taken to stimulate the flow of mortgage finance to private landlords at this crucially important time.

We recognise that there is ongoing concern about the specific impact of the credit crunch on arrears levels being experienced by individual landlords. As we outline below, buy-to-let lenders can utilise the Receiver of Rent process, which protects the interests of tenants and safeguards the condition of the property. Paragon is a recognised exemplar of best practice in this area.

Mortgage Arrears: Paragon's Approach

The buy-to-let sector has been the focus of a degree of negative and ill-informed attention in recent months due to a number of isolated incidents of tenants facing eviction due to their landlords' properties being repossessed. Paragon is clear that the situation of tenants should not be neglected in this context and has been leading discussions within Government in this important area.

Whilst the credit performance of Paragon's borrowers has remained robust and compares favourably with industry competitors—our buy-to-let arrears remain well below industry averages and the new arrears flow has slowed significantly since December 2008—we recognise the concerns that policy-makers currently have given recent rises in repossessions. Increases in arrears levels are being experienced in both the owner-occupier and the buy-to-let market. Where sitting tenants are affected by this, it is important to take action that protects their interests.

However, policy-makers and opinion-formers should be clear that very different circumstances apply in each of these sectors—a fact that has often not been recognised. In considering the implications of a private landlord falling into arrears, it is crucial that a clear distinction is drawn between:

— tenants of rented properties subject to buy-to-let mortgages;

— tenants of rented properties subject to owner-occupier mortgages where the lender has given permission for the property to be let; and

— tenants of rented properties subject to owner-occupier mortgages where the lender has not granted permission for the property to be let and is typically not even aware that the property is being let out.

In the first two cases, the existing Assured Shorthold Tenancy (AST) agreement is binding on the lender if enforcement is pursued against the borrower landlord, and the tenant is entitled to the remainder of their initial tenancy period—typically six months—and to a minimum of two months' notice.

However, the situation is different when an owner-occupier borrower has not sought the permission of the lender. The borrower in these cases is in breach of the terms of the mortgage by letting the property out, and while the tenancy agreement is binding between the tenant and landlord, it is not binding on the lender. Furthermore, the responsibility of the lender required by MCOB in these situations is to the borrower to minimise arrears and obtain the best price for the property. It is clearly still desirable for repossession to be very much a last resort, and the court in these situations will only allow possession during the term of the tenancy if it is just and equitable to do so.

In addition, lenders are able to utilise the Receiver of Rent process, which is most commonly used by buy-to-let lenders. The Receiver of Rent process helps the tenants who maintain regular rental payments under the terms of their AST or contract in cases where the borrower landlord is struggling with mortgage repayments. It aligns lenders' and tenants' interests, allowing tenants to remain in the property and ensuring that lenders continue to receive rent payments.

A Receiver of Rent is appointed by the lender, effectively to take over the responsibilities of the landlord, collecting rental payments direct from the tenant and applying them to the borrower's account and maintaining the condition of the property. A mortgage lender can only instruct a Receiver of Rent when the landlord is not making payments under their mortgage agreement.

Paragon is an exemplar of best practice in this area, a fact that has been recognised by Government. We first consider the range of options for the borrower, while always ensuring that the welfare of tenants is our highest priority. When we have to take control of a property due to non-payment, we honour the tenant's rights under the terms of their contract and ensure that the property is professionally managed and maintained through a Receiver of Rent. This secures the tenant's position, ensures the property is maintained, and guarantees the rent payment profile.

The Government is to date taking a measured response to repossessions and is resisting the temptation to over-regulate. This is a sensible approach and Government should look in the first instance to build on the best practice of Paragon and other participants in the buy-to-let mortgage sector.

Paragon notes the buy-to-let arrears and possessions guidance issued by The Council of Mortgage Lenders in June. Paragon fully endorses and adheres to this guidance.

Sale and rent back

We note the recent Treasury and FSA consultations on regulation of the sale and rent back sector. This is not a sector that Paragon has engaged in, and it is important to appreciate the distinction between buy-to-let and sale and rent back. Contrary to some beliefs, buy-to-let and sale and rent back are two distinct products and should not be confused when considering regulatory responses.

IMPACT OF CREDIT CRUNCH ON ACCESS TO MORTGAGE FINANCE

Paragon has submitted evidence to the Treasury Select Committee's inquiry into the banking crisis on the lack of finance available to non-banks and the impact that this is having on the private rented sector.

As previously indicated, the private rented sector takes on increased significance in an economic downturn, with the sector experiencing its strongest period of growth in the recessionary years of the early 1990s when it responded to the phenomenal demand for rented property. In the current market environment, many first-time buyers are unwilling or unable to move into the owner-occupier sector and, with the social rented sector already under severe strain, many are utilising private rented accommodation until the economy improves.

Rising tenant demand is placing increasing pressure on the private rented sector. However, professional private landlords who are, and will continue to be, the mainstay of this sector of the housing market, are currently finding it very difficult to respond to increasing tenant demand. This is due to a lack of finance for residential property investment caused by the serious funding constraints being experienced by non-bank lenders, and a consequential fall in buy-to-let mortgage availability.

Non-banks have hitherto provided a vital source of mortgage finance to consumers and finance for investment in the private rented sector. As highlighted by Prime Minister Gordon Brown, over the last decade, 40% of new mortgages came from non-bank institutions and foreign banks. Paragon and other lenders in the non-bank sector are reliant on wholesale funding in order to originate new loans, but are currently unable to access funding from this source. Despite this clear funding shortage, the Treasury has not included non-banks in the lending support measures it has introduced in recent months.

The recent Budget confirmed the non-inclusion of non-banks from the Treasury's Guarantee scheme for Asset Backed Securities (ABS). This scheme was based on proposals put forward in last year's Crosby Review of mortgage finance, designed specifically to help revive UK securitisation markets in order to allow more funds to become available for mortgage lending.

The Crosby Review acknowledged the role played by specialist lenders such as Paragon and called for guarantees to be available to them as well as the mainstream banks. Given the key role of the non-bank sector in serving critical parts of the UK's mortgage market and providing much needed finance for the private rented sector, and that the case for non-banks' inclusion in the Guarantee scheme for ABS is strong, the non-inclusion in the scheme is frustrating.

The lack of available finance for non-bank lenders and absence of Government support is causing considerable consumer detriment, by limiting the vital competition that is necessary for a well-functioning and customer-focused mortgage market. In some markets there is already clear evidence that competition is being eradicated. The buy-to-let market, in particular, currently lacks any form of genuine competition; recent figures issued by moneysupermarket.com show that the number of buy-to-let mortgages available has fallen in two years by 95%. Furthermore, of the top ten buy-to-let lenders (by gross advance) in 2007, only two are now writing new business.

As a result of non-inclusion, specialist lenders such as Paragon have been unable to access funds through the securitisation markets that have historically funded lending. Compounding this, there has been no secondary lending effect from the Government's lending support measures; high street banks are not passing any new funding onto specialist non-bank lenders.

There have been no clear explanations from HM Treasury as to why non-banks have not been included in the Guarantee scheme. However, even if non-banks are deemed to be eligible for the ABS Guarantee scheme, there are certain aspects of the scheme's design which render it unusable for non-banks, and more fundamentally, appear out-of-step with other Government initiatives. These particularly relate to the AAA rating requirement and the counter indemnity requirement.

Primarily, the AAA rating requirement is not consistent with the requirements for other Government schemes, such as the Credit Guarantee Scheme, the Asset Purchase Facility or the Asset Protection Scheme, all of which encompass non-AAA ratings. At an operational level, non-banks are not in a position to be able to fund the non-AAA portion of securitisation structures, unlike banks and building societies that can draw on their deposit base.

The overwhelming majority of the non-bank sector, including Paragon, have taken a prudent approach to lending, and have used securitisation in a transparent and responsible way. Paragon itself has securitised nearly £20 billion of first mortgages and consumer loans through fifty-three public transactions.

Through securitisation, our £9.5 billion portfolio is match-funded to maturity and we have a strong cash position and a positive operational cash flow. The belief in some quarters that the non-bank sector is inherently risky belies our results. All of our securitisations have performed well, and within the parameters agreed by the parties involved at the outset, and all have been:

— Straightforward.

— Transparent.

— Low-risk.

However, since our last securitisation in July 2007, credit market conditions globally have deteriorated considerably and it has not been possible to raise finance through securitisation.

We highlight that:

— The performance of Paragon's buy-to-let loans outstrips the wider market.

— The performance of Paragon's securitisation deals has been exemplary.

— Paragon's securitisation deals have never been downgraded and no investor has ever lost money as a result of investing in Paragon's securitisations.

— Paragon's overall financial strength compares favourably with the wider bank and building society sector, and on a like-for-like basis would be the UK's fifth largest building society. Almost uniquely among publicly quoted lending institutions, Paragon remains profitable, demonstrated by your interim results published on 19 May 2009.

— Paragon has no liquidity risk as all funding is fully matched to maturity.

For the UK mortgage markets to function properly, there needs to be a recovery of the securitisation funding markets. Used properly and responsibly, securitisation is an excellent way to provide long-term, committed-for-life finance. The historic performance of securitisations in the UK is such that it is almost impossible to find a transaction that has not performed within the expected parameters agreed by the various parties at the outset, be they bankers, credit rating agencies, issuers or investors. Government needs to focus its efforts on restoring the securitisation markets and creating the vital source of funding required to meet future mortgage demand.

Paragon has submitted a detailed Budget response to HM Treasury calling for a reconsideration of the exclusion of non-bank lenders from the guarantee scheme for ABS. This emphasised the urgent need for non-bank lenders to be included in the scheme in order for their flow of lending to resume, and for private landlords to get access to finance they require to make an expanded contribution to meeting the country's future housing needs.

Conclusion

Mortgage arrears and access to mortgage finance will remain important issues in the coming months as the effects of the economic downturn continue to be felt. It is important that Government take a sympathetic yet measured response.

On the subject of repossessions, Government should look to build on industry best practice and disseminate the lessons that can be learnt from leading lenders across the sector. In particular, the importance of the Receiver of Rent process in providing stability and continuity for tenants and lenders alike should not be underestimated.

The private rented sector is taking on increasing importance in the current economic environment. In this context, it is disappointing that Government has not to date recognised the significant contribution the non-bank sector has made in providing funding to private landlords. It is vital that the Treasury's Guarantee scheme for ABS is extended to this sector as a matter of urgency to allow mortgage funding to flow to the private rented sector.

June 2009

Written evidence submitted by the National Housing Federation

Executive summary

The National Housing Federation represents 1,200 independent, not-for-profit housing associations in England and is the voice of affordable housing. Our members develop and manage more than two million affordable homes for five million people as well as delivering a wide range of community and regeneration services. They also provide a range of low cost home ownership schemes that have helped over 200,000 households buy an affordable home.

Our key recommendations for the committee to consider are:

Mortgage availability for shared ownership schemes—government should compel banks that have benefited from bailout by the public purse to guarantee a flow of mortgages to the shared ownership sector. Government should also work with lenders to ensure there is a range of affordable and flexible mortgages available for someone buying a home through a government low cost home ownership scheme.

FSA regulation—Treasury should work with the FSA to consider the impact of the Capital Requirements Directive on shared ownership mortgage lending and recognise the Mortgage Protection Clause as the equivalent of a "recognised guarantee."

Mortgage rescue scheme—we recommend that more flexibility is allowed in relation to the level of the price cap. If take up of the scheme continues to be limited government should also consider extending the eligibility criteria for the scheme.

1. Introduction

1.1 The National Housing Federation welcomes the opportunity to submit written evidence to the Treasury Select Committee into Mortgage Arrears and Access to Mortgage Finance. We would like to comment on three issues that the committee will be considering:

— the impact of the credit crunch on access to mortgage finance and the terms on which such finance is offered for first time homebuyers;

— adherence to, and the effectiveness of, Financial Services Authority (FSA) rules and guidance for mortgage lenders on repossession policy and treatment of consumers in arrears as well as the FSA's regulatory approach in this area; and

— the success of those Government schemes in existence before the financial crisis to support homeowners facing difficulties with mortgage payments and/or at risk of repossession, as well as the effectiveness of initiatives introduced since the financial crisis began.

2. Mortgage Availability for Shared Ownership Schemes for First Time Buyers

2.1 Housing associations provide a range of low cost home ownership schemes to help first time buyers, key workers and social tenants buy an affordable home. Schemes include shared ownership, shared equity and mortgage to rent. Housing associations have been offering shared ownership (part-buy part-rent) schemes for 30 years. Shared ownership has been a hugely successful tenure that has offered over 155,000 families a flexible, affordable and importantly sustainable route into home ownership.

2.2 Shared ownership is the most affordable low cost homes ownership (LCHO) product for people on low incomes as it offers shares as low as 25 per cent. In 2007–08 the average household income of someone buying a shared ownership home was £26,000, compared to £35,000 of someone buying through a shared equity scheme and £43,000 for the average first time buyer.

2.3 Mortgage availability for shared ownership has become severely restricted since the credit crunch and there are no lenders willing to offer higher loan to value mortgages. The current issue with mortgage availability for shared ownership is caused both by lenders unfair perceptions as to the profile of customers and is compounded by lenders' policies on new build properties.

2.4 Some lenders view people buying a home though shared ownership schemes as "marginal purchasers" because they are typically on low and moderate incomes and unable to save up large deposits. This is misinformed as whilst no doubt some shared ownership purchasers will be more "risky" than many existing owner occupiers with high levels of equity and incomes, people buying a home through shared ownership are no riskier to lend to than first time buyers. There is no evidence to support the view that people on lower incomes are more likely to default on mortgage payments. The Federation is clear that we are not advocating risky lending, but where household's affordability is good, providing access to mortgage finance will allow households that would otherwise have been unable to house themselves to find a home. This in turn reduces pressure on the affordable and social rented sectors.

2.5 All grant funded shared ownership homes must include a mortgagee protection clause (MPC) in the lease to protect lenders against loss on default. The MPC is designed to cover part of a lender's loss should the lender have to take possession of the property on default. The MPC only operates where the sale proceeds are insufficient to cover:

— the principal amount due under the mortgage;

— the reasonable cost of recovering or trying to recover any money due under the mortgage;

— acquiring and selling the freehold (including a reasonable allowance for legal, valuation and estate agency work undertaken by the lender's employees);

— any mortgagee protection or endowment policy premiums payable by, or recoverable from, the leaseholder and secured by the mortgage; and

— no more than 12 months' unpaid interest due under the mortgage.

The lender is also able to claim back capitalised rent through the MPC.

2.6 For access to LCHO products there are also robust affordability and eligibility assessments in place that promote fairness and flexibility, as well as measures to ensure home ownership for first time buyers is sustainable over the long term. All potential applicants access independent financial advice and a standardised affordability assessment as a basis for determining applicants' ability to sustain home ownership in the long term. On average this has consistently remained at about 3.5–4 times annual income. Housing associations also offer "downstream" support if a customer runs into financial difficulties or experiences a change in circumstances. Financial advice is offered, as well as opportunities to "downward staircase" to a own a smaller proportion of the property in severe cases of financial difficulty.

2.7 The government must ensure that in future there will be a range of affordable and accessible mortgages available to people purchasing a shared ownership home. We recommend that Government should compel banks that have benefited from bailout by the public purse to guarantee a flow of mortgages to the shared ownership sector.

2.8 People buying a home through shared ownership schemes, even if they are only buying a small share of 25% are required to find hefty deposits. New Build HomeBuy is the main shared ownership product and is available on new build properties. The majority of mortgages on offer are 80% loan to value and do not take into account that someone is only acquiring a mortgage for a small share of the overall property value.

2.9 Members are also reporting that the average rates offered for most shared ownership mortgages are currently around 6–7% APR, accept for 75% LTV mortgages. This is an unacceptably high rate given the historically low Bank of England base rate and does not reflect the protection lenders are offered through the shared ownership model. The rates of these mortgages are far too high compared with other mortgages for first time buyers and do not reflect the excellent risk protection that the shared ownership model offers lenders. This is a critical issue for housing associations and for the first time buyers, key workers and social tenants that they help buy a home through these schemes.

2.10 The Federation believes that government should work with lenders to ensure there is a range of affordable and flexible mortgages available for someone buying a home through a government low cost home ownership scheme.

2.11 This is despite many housing associations reporting their highest ever demand for LCHO products. In 2007/08 there were around 4 applications for every one home available, with over 101,000 applications for HomeBuy products. Notting Hill Housing Group saw a 47% increase of enquiries in February 2009 compared to the same period the previous year. Moat, a HomeBuy Agent, has seen a 63% increase in enquires and a 28% increase in applications in the April to May this year compared to the same period last year.

2.12 We believe ensuring a flow of mortgages for shared ownership could help play an important role in boosting housing transactions in a declining market. As well as helping many people who are priced out of the open market to realise their aspiration for home ownership and to move into a home that meets their needs and that of their family. This in turn relieves pressure off the housing waiting lists.

3. Financial Services Authority—Regulatory Approach

3.1 The National Housing Federation is concerned by lenders reports that they are required by the Financial Services Authority to hold additional regulatory capital against shared ownership mortgages compare to shared equity schemes. Whilst lenders apply the same capital treatment to shared ownership mortgages as conventional mortgages the protection against lost offered by the MPC is not taken into account.

3.2 This is a critical factor further undermining the supply of mortgages for shared ownership schemes. The Treasury should work with the FSA to consider the impact of the Capital Requirements Directive on shared ownership mortgage lending and recognise the MPC as the equivalent of a "recognised guarantee." This would enable lenders to hold less regulatory capital against shared ownership mortgages and facilitate a greater supply of mortgages.

4. Mortgage Rescue Scheme

4.1 Housing associations are key partners in delivering the national mortgage rescue scheme. The scheme is designed to help vulnerable people at risk of repossession stay in their homes by a housing association buying a property at a fair market rate with a tenant staying in their home either through shared equity or as tenants paying an affordable rent.

4.2 In the six months since government launched a national mortgage rescue scheme there have been over 4000 public enquires about the scheme and 600 people applying for the scheme. However, only a handful of people have so far been gone on to see take up the shared equity or affordable rent option. It is worth bearing in mind that whilst the scheme was originally announced in September 08 it was only up and running in January 2009.

4.3 From the beginning, the Federation and its members have worked with the Government to make the scheme a success. Success should not be judged purely in terms of hitting targets, but in terms of supporting families facing homelessness and recognising the wider costs to society and the public purse when intervention comes too late.

4.4 Housing associations have reported that there are a number of factors that are currently limiting the success of the scheme. The price caps, limiting the value of a property eligible for mortgage rescue, are set too low in many areas preventing many eligible families from being helped by the scheme. Some members have also expressed concern that the eligible criteria may be too restive.

4.5 We recommend that more flexibility is allowed in relation to the level of the price cap. If take up of the scheme continues to be limited government should also consider extending the eligibility criteria for the scheme.

July 2009

Written evidence submitted by the Consumer Credit Counselling Service

About Consumer Credit Counselling Service

The Consumer Credit Counselling Service (CCCS) is the UK's leading debt charity, responsible for managing over £3 billion (some 10 percent) of the UK's problem debt. For the first half of 2009, our helplines received over 2,000 calls a day and we provided full counselling sessions to 50,000 people.

In 2008, almost half (47.4 percent) of those seeking our help were homeowners.

Since September 2007, CCCS has referred clients two months in arrears to a specialist mortgage arrears and repossessions counselling centre. Prior to this mortgage arrears would always have been prioritised with the expectation that clients would be able to keep hold of their property. This is of course no longer the case.

In line with our policy we are responding to this inquiry only where we have actual evidence. In this instance our evidence is based on the information available from the mortgage arrears and repossessions counselling service which advises about 150 people a week, but there has been a marked change in the last six months which is worth bringing to the Committee's attention.

1. *Trends in mortgage arrears*: since September 2007, any clients two months in arrears have been referred to our specialist mortgage arrears and repossession team. We were advising about 150 such clients a week, many of whom typically have high loan to value mortgages, a substantial proportion have second charge loans and, virtually without exception, high levels of unsecured debt. In January we were advising some 20 percent of these clients that they could no longer afford their homes.

During the second quarter of this year the percentage of people advised that they cannot stay in their home dropped to less than six percent. This is because lenders are prepared to be more flexible and slower to repossess.

We are certainly seeing fewer clients with imminent repossession hearings; even in cases where clients have missed payments on suspended possession orders, lenders are generally more willing to come to a new arrangement rather than repossess.

On the basis of our experience, therefore, it seems likely that the revised downward forecast for the numbers of repossessions this year by the Council of Mortgage Lenders (CML) is justified.

2. *Issues for homeowners over the medium-term*: although lenders are showing more forbearance and greater flexibility in their treatment of defaulting clients, this is likely to be, at least in part, a reflection of commercial reality. Once the market improves and property prices start to increase, lenders' attitudes are likely to harden and we can expect to see many more sales proceed against clients with suspended possession orders.

At the same time, those homeowners who have taken advantage of the various initiatives on offer which allow them to stay in their home, such as deferred payments, or interest only mortgages, may find that they have added considerably to both the cost and the length of their mortgages. Depending on their own personal circumstances, including how long they remain unemployed or incomes remain reduced, such homeowners may find themselves with unsustainable debt burdens in the near future, particularly if they are also carrying high levels of unsecured debt.

3. *Lenders' treatment of homeowners in arrears*: mainstream lenders are definitely adapting a more flexible attitude to customers in difficulties, including those who have defaulted with a suspended possession order or those who have not contacted the lender for as long as six months. However, both sub-prime lenders and second charge lenders are not being as flexible with borrowers. There are exceptions but generally these lenders are less likely to accept lower or interest-only offers, they are more likely to repossess and they are often changeable and difficult to deal with.

4. *Sale and leaseback*: while we welcome the interim rules and guidance introduced by the FSA from July 1 as offering some protection to new customers of sale and leaseback, we are still concerned that these interim regulations may lead to increased consumer confidence and more applications without the protection a full regulatory regime provides. During this interim period therefore, before committing to such schemes, consumers should receive independent legal and debt advice. In addition it should be incumbent on each company offering sale and leaseback to fully disclose its interim status and the impact that has on each customer.

5. *Overall effectiveness of initiatives to help homeowners*: while the majority of lenders are behaving fairly to customers in difficulties, it remains to be seen whether this is primarily in response to FSA guidelines, commitments by industry bodies and other initiatives such as the pre-action protocol or because of the commercial realities of a falling housing market.

As far as Government initiatives are concerned, since it was launched in April, CCCS has recommended 48 clients as eligible for HMS and none for the Mortgage Rescue Scheme. Nevertheless we believe that these initiatives, particularly HMS, have had a beneficial effect through encouraging mainstream lenders to be more flexible towards their customers.

Written evidence submitted by Home Saver

1. About Us

1.1 We welcome the Treasury Select Committee hearings on this crucial issue and are grateful for the opportunity to contribute to the national debate.

1.2 Home Saver is a third sector not for profit group working to develop and implement a self funding comprehensive not for profit solution to the problems of mortgage arrears/repossessions.

1.3 The team which is operating under the umbrella of Housing First Limited a 100% owned subsidiary of Housing Action, a registered UK charity includes experts in housing and social policy; lender policy and execution; securitisation markets and a former member of the Bank of England Monetary Policy Committee. The team has undertaken extensive external validation of its models including but not limited to detailed work with a Big 4 accounting practice; ratings agency; focus groups with front line practitioners; discussions with other industry stakeholders.

2. Executive Summary

2.1 We believe that despite substantial effort being devoted to stabilising the housing market and addressing repossession issues, even the optimistic estimates mean only 50% of cases are supported.

2.2 *Crucially there is a public expectation of help being universally available that is not and will not be met under current plans. More needs to be done and needs to be done now.*

2.3 There is immediate need for a comprehensive scheme. We believe that this should be delivered as a not for profit scheme, that is self funding, addresses housing market stress, reduces financial burdens on lenders and government and that contributes to reopening securitisation markets.

2.4 Home Saver is such a scheme. This scheme is:

2.4.1 Open to all in true need regardless of negative equity, mortgage size or family circumstance; supports all borrowers at repossession risk or in systemic arrears.

2.4.2 Self Funding.

2.4.3 Structured to support lenders by reducing financial provisioning and freeing risk weighted assets to help lending flows with associated benefits for holders of Residential Mortgage Backed Securities.

2.4.4 Meets those in need where they are by undertaking an initial visit to the borrowers property and then working with the borrower to establish a financial debt management plan; the scheme is flexible and able to help absorb changes in individual circumstances.

2.4.5 Tops up mortgage payments with an interest free loan (held as a subsequent charge against the property) to make them fully performing so allowing borrowers with assistance time to stabilise their finances and find and adopt a permanent solution.

2.4.6 Addresses Unsecured Debt solving this difficult and substantial issues as well as coping with 2nd and subsequent charges.

2.4.7 Allows a flexible exit based upon individual circumstances such as to fully resume the mortgage, enter into a shared equity mortgage rescue, require the sale of the house with possible rent back or move into more appropriate accommodation.

2.4.8 Provides for enough time (five to seven years if needed) to solve problem.

2.4.9 Ensure assistance is interest free with no hidden charges.

2.5 Much effort has been put into establishing a mortgage safety net in the face of the most challenging home loans market in the past 20 years but it is unclear as to how many people are really being helped. Government estimates that over 200,000 households are assisted by cash flow support[49] conflict with March 2009 data from the FSA[50] indicating that 399,000 loans (215,000 regulated first mortgages) are already in systemic arrears of which only 116,000 are subject to some form of assistance.

2.6 Focus groups run by Home Saver with frontline professional case workers suggest this overall assessment is optimistic. For example:

2.6.1 Receiving an answer to a forbearance request from a lender can take over 60 days, during which time charges and interest are still being rolled up.

2.6.2 Some lenders have a very aggressive approach to repossession.

2.6.3 "Benefits traps" can and do accentuate household difficulties in the face of unemployment.

2.6.4 Distressed households can be reluctant to come forward.

[49] Announcement by CLG Housing Minister John Healey 22 June 2009.
[50] FSA Statistics March 2009.

2.7 The government's capital based mortgage rescue is complex and time consuming to execute Lenders are bearing significant costs including balance sheet provisions, increases in risk weighted assets which restrict lending flows, arrears function costs and reputation costs.

2.8 Government is also bearing significant costs by funding the mortgage rescue scheme, paying for Income Support Mortgage Interest and funding guarantees for the Home Owner Support Scheme, insuring some non performing lender assets and some Residential Mortgage Backed Securities.

2.9 Independent research confirms that mortgage arrears are directly related to income shocks (eg unemployment), living cost rises (eg interest rate rises/food/energy price rises), debt and inability to remortgage out of trouble.

2.10 Unemployment is forecast to grow strongly[51] and interest rates forecast to rise in the medium term. Remortgaging properties in negative equity or with high loan to value ratios is challenging, and energy prices are again on the rise. Continued rising mortgage arrears will be an inevitable consequence.

2.11 There is urgent need to implement a comprehensive not for profit self funding arrears and repossession scheme giving access to all, that is based upon a cash flow approach. Home Saver provides such a scheme.

3. Recommendations

3.1 The Government recognise that mortgage arrears and hence repossessions will grow strongly in response to rising unemployment and that further support measure are required.

3.2 That the Government commit resources to evaluate the costs and benefits from a comprehensive "Top Up" cash flow based mortgage rescue scheme that:

- 3.2.1 Assesses a households income expenditure and assets to establish ability to pay.
- 3.2.2 Seeks to cure unsecured as well as secured debt.
- 3.2.3 Adopts a top up approach to keep mortgages fully performing.
- 3.2.4 Is open to all UK residential mortgage holders for mortgages in their own name without restriction.

3.3 That special attention be given to the potential systemic benefits to the financial system from adopting a comprehensive mortgage rescue scheme open to all

3.4 That the scheme be designed in such a way as to help limit lender provisioning to protect balance sheets and Tier 1 Bank Capital

3.5 That the scheme be designed in such a way as to help free risk weighted assets and help improve lending flows

3.6 That such a scheme be used as a bottom up cash flow underpin to help raise financial confidence and so help to reopen residential mortgage securitisation markets

3.7 That such a scheme be self funding and not require additional public spending:

- 3.7.1 Initial funding to come from non residential mortgage lending institutions who will benefit from the systemic increase in asset values such a scheme would imply.
- 3.7.2 That the balance of funding be made on the basis of a comprehensive compulsory mortgage levy estimated to be around 25 basis points on all residential mortgages.

3.8 That the only long terms state involvement (over and above engaging in the design and helping fund pilot studies etc) be a state guarantee to the mortgage protection fund and that the fund be actuarially maintained such that the guarantee be held as a zero value contingent liability.

3.9 That lenders gear up their arrears functions to handle the current challenge

3.10 That urgent attention be given to gaps in the benefits system that accentuate the risk of mortgage arrears and possessions

3.11 *We believe that implementing a scheme such as Home Saver would address recommendations 3.1 to 3.8 above.*

4. Need Is Already Large And Will Grow Significantly

4.1 Repossessions have already risen from a low point of below 10,000 a year to the current predicted 65,000 per annum.

4.2 Although the most respected forecast for house repossessions comes from the Council for Mortgage Lenders has recently been reduced from 75,000 to 65,000 for 2009[52] looking further forward and drawing on former HSBC economist Dr Ian Shepherdson view to the June 2009 Chartered Institute of Housing Annual Conference "repossessions will reach between 100,000 and 120,000 per year by 2011."[53]

[51] David Blanchflower former Bank of England MPC member June 2009; OECD forecasts June 2009.
[52] Council For Mortgage Lenders 22 June 2009.
[53] Property Wire June 2009.

4.3 The Council for Mortgage Lenders also forecasts 360,000 cases in arrears by end 2009.[54] These statistics do not reconcile to the FSA statistics as they are reported on a different basis. It is our view that the FSA data gives a more accurate picture.

4.4 In March 2009 FSA reported 399,000 residential loans in arrears. The method of calculation adopted by the CML means there are risks of substantial under reporting when there are low interest rates.

4.5 Looking at experience from the 1992 recession we believe that arrears cases from primary lenders may hit in excess of 500,000.

4.6 Continuing rises in unemployment and the potential for future interest rate rises will mean a substantial increase in the need

4.7 We believe that repossessions and arrears:

4.7.1 Started from a low base in around 2004 that reflected some basic level of borrower failure.

4.7.2 This then grew strongly through to end 2007 as the result of over indebtedness no longer being able to be cured by remortgaging as debt income ratios were already too high.

4.7.3 The process accelerated with the credit crunch as mortgage finance started to dry up for borrowers looking for high loan to value deals, whilst at the same time house price falls drove borrowers into either negative equity or higher loan to value segments, so restricting remortgage opportunities for ending fixed term/interest deals, meaning this group immediately faced relatively higher interest rates (as they were moved onto standard variable rates) and could not escape through remortgaging.

4.7.4 This led to a substantial rise in mortgage arrears; which was slowed by the deep cuts to interest rates in late 2008/early 2009.

4.7.5 Looking forward likely arrears drivers will be:

4.7.5.1 Increases in unemployment.

4.7.5.2 Increases in interest rates.

4.7.5.3 Renewed increases in energy.

4.7.5.4 Continued failure for borrowers with high loan to value mortgages to be able to remortgage onto lower rate deals.

4.8 We fully endorse housing charity Shelter's recent statement warning "the Government and mortgage lenders against complacency—and call[ing] on them to start preparing for a second wave of arrears and repossessions that could hit the UK within the next two years."[55]

4.9 We believe that there is urgent need for a comprehensive scheme of sufficient size to deal with the projected need. Home Saver offers such a potential scheme.

5. Systemic Issues Relating To Mortgage Finance

5.1 Despite recent talk of "green shoots" economic forecasters are mixed in their opinions as to whether or not economic recovery has started.[56] Events since 2007 have demonstrated the critical role of mortgage finance (whether US or UK based) in driving capital market events.[57]

5.2 There is evidence that the initial market failure in the securitisation markets has led to restrictions in mortgage credit that have in turn:

5.2.1 Restricted house purchase demand leading to reduced selling prices.

5.2.2 Reduced selling prices have moved an estimated 15% of UK households into negative equity whilst moving all borrowers onto higher loan to value ratios. Geographic mapping reveals local hotspots.

5.2.3 Engendered rises in loan to value coupled with lenders restricting deals to lower loan to value ratios with subsequent difficulties in remortgaging as borrowers come off fixed rate deals

5.2.4 Led to a substantial number of borrowers coming off fixed rate deals to then face a move to normally much more expensive standard variable rate.

5.2.5 Households facing higher payments, if already financially stretched, going into arrears with subsequent dangers of repossession.

5.2.6 Remortgaging out of trouble no longer an option

5.2.7 Reductions in interest rates having helped ameliorate the move to standard variable rates, will have a reverse impact as and when interest rates start to rise again.

[54] Council For Mortgage Lenders 22 June 2009.
[55] Shelter Press Announcement 22 June 2009.
[56] See for example the recent report from the OECD on UK Economic prospects.
[57] For example in the UK Northern Rock and in the USA the sub- prime crisis.

5.3 The handling of mortgage arrears have significant systemic effects as follows:

5.3.1 *Lenders need to provide for the cost of anticipated losses* against both lender capital (eroding Tier one capital reserves) and profit so reducing lender profits.

5.3.2 *Lenders need to staff up* to provide effective arrears management functions which adds to their overall overhead costs.

5.3.3 *Nonperforming loans carry a higher risk weight under Basel II* so requiring more capital and impacting lending flows.

5.3.4 *Basel II/FSA Risk Weighting Rules* forbid lenders from subsidising securitised mortgage books[58] whilst securitisation trust deeds in some cases are claimed to prevent lender support and forbearance.

5.3.5 *We believe that a comprehensive top up based mortgage rescue scheme such as Home Saver that ensure mortgages fully perform and that is open to all has an important role to play in healing and restoring us to a virtuous circle.*

6. Evaluation of Schemes To Help Borrowers

6.1 The government has both continued, extended and introduced a number of initiatives to address strains in the housing market. We comment on a number of them below.

6.2 *Lender Forbearance/Debt Management Plans* such as reduced interest rates, move to interest only, freeze charges, allow payment holiday and are often linked to unsecured payment plans. Frontline case worker comments from our recent focus groups include:

6.2.1 *"many of the major lenders are being more accommodating but the sub-prime sector are often going for Possession Orders when they are 2nd chargee and the main lender is being accommodating. There are two or three names commonly appearing on court lists these last few months. They are unbending in negotiation attempts. That is, until the court takes a more lenient view."*[59]

6.2.2 In respect of forbearance a *"30-day hold on further action is a mere frustration as banks are taking up to 60 days to respond to hold letters".*[60]

6.2.3 *"Interest and charges accrue until offers of repayment can be made—so while the banks take up to 60 days to respond to correspondence, charges continue to accrue from ALL a client's creditors because the offers of repayment cannot be made until the Financial Statement is complete."*[61]

6.2.4 *"It has not become apparent that forbearance is being extended from three month's arrears to six, as suggested by the Prime Minister. I have yet to see a six month example. Early days though."*[62]

6.2.5 *"The biggest problem faced in my experience is non-response to correspondence from a huge lender enabling no progress on the production of a Financial Statement; consequently, no agreement can be reached speedily with the mortgage lender. Meanwhile non-priority creditors continue adding further charges and interest and clients start receiving court papers or threats of action."*[63]

6.3 *Interest Rate Reductions* have reduced the mortgage payment burden on borrowers, this will reverse when interest rates start to rise again.

6.4 *Government Mortgage Rescue Scheme* includes both a buy to rent and equity share option. It has strict entry criteria and restricting help to a limited number of households. Whilst welcome and operationally well implemented, this ethical if somewhat cumbersome scheme needs in our view to be strategically linked as an exit route to other "cash flow" based mortgage rescue initiatives. Such an extension to the existing scheme should be important to the long term housing strategy.

6.5 *Government Home Owner Support Scheme* provides for a government guarantee on up to two years interest roll up. The scheme offers little beyond lender forbearance and risks adding further debt burdens for vulnerable customers as there is no interest forgiveness. A scheme such as Home Saver would replace this

6.6 *Government Asset Protection Scheme* insures lender assets above specific loss levels. Whilst this scheme has only been engaged by two lenders and details of the exact assets are not yet clear, it is assumed that some UK residential mortgages assets will be included. A comprehensive scheme such as Home Saver would underpin these assets and negate the need for this insurance to be applied to UK based residential mortgage assets.

[58] Set out in FSA Handbook section BIPRU 9.6.1.
[59] Source: Frontline court desk worker June 2009.
[60] Source: Frontline case worker June 2009.
[61] Source: Frontline case worker June 2009.
[62] Source: Frontline Court Desk Worker.
[63] Source: Frontline Case Worker.

6.7 *Government Asset Backed Guarantee Scheme* either guarantees repurchase of asset backed securities with owner bearing loss or guarantees against losses on asset backed securities at the end of their life. Such guarantees, most especially the repurchase guarantee, are intended to help reopen securitisation markets, but in our view require the cash flow underpin offered by a scheme such as Home Saver to be effective.

6.8 *Income Support Mortgage Interest* supports borrowers within certain limits and since recent government extensions kicks in after 90 days lasting for two years. The rules are complex and in some cases leave gaps. Our focus groups advised where the main income earner in a childless couple loses their job, then they are entitled to contribution based job seekers allowance for six months . After this if their partner is working more than the prescribed hours, benefit ceases. At the same time income support mortgage interest is not payable if the remaining earner works more than 25 hours a week and finally childless couples have no entitlement to working tax credit if they work is for less than 30 hours per week. The rules need to be simplified and aligned to the rest of the benefits system.

6.9 *Court Desks/Revised Court Protocol (non mandatory)* have required lenders to exhaust all other possibilities prior to seeking repossession. A series of publically funded court desks provides court support to people under repossession proceedings. We believe that these are helpful practical measures that contain but unlike Home Saver do not cure.

6.10 *Payment Protection Insurance* offered by commercial providers usually pays for a number of months on unemployment or other income interrupting event. It represents a substantial commission stream for lenders, currently only covering 17% of borrower. It has been subject to questions of miss-selling. Both ISMI and PPI would benefit from a baseline comprehensive mandatory insurance levy (such as proposed by Home Saver) offering borrowers a secure safety net.

6.11 *We believe that a comprehensive scheme such as Home Saver would provide the strategic framework within which to reengineer other existing schemes over time so as to drive optimum economic and social benefit from mortgage rescue.*

July 2009

Written evidence submitted by the Finance and Leasing Association (FLA)

Introduction and Summary

1. The FLA is the leading trade association for the second charge mortgage market, representing over 85% of the industry. Second charge lenders include subsidiaries of some of the major banks and building societies, together with other independent financial organisations. We welcome the opportunity of providing evidence as part of the Treasury Committee's Inquiry into Mortgage Arrears and Access to Mortgage Finance.

— Second charge mortgage lenders are committed to helping customers in financial difficulty. Possession is only taken as a last resort, once all other reasonable alternatives have been exhausted. This approach is reflected in the low level of repossessions, around 1,500 in 2008. Early indications for 2009 show a relatively flat picture, but rising unemployment, could perhaps push the figure to 2,000.

— The second charge mortgage market is highly regulated via the Office of Fair Trading under the Consumer Credit Act 1974, and by FLA's binding Lending Code, supplemented by the industry's new Good Practice Guidance issued with Government approval last year. Together, these ensure that borrowers with debt problems are treated fairly and sympathetically and every attempt is made to agree an acceptable repayment arrangement. Moving regulatory responsibility to the Financial Services Authority would produce no benefit for borrowers, who would actually lose important protections such as Time Orders, which require additional forbearance on the part of lenders.

— Support for Mortgage Interest (SMI) should be payable on all second charge mortgages (as it is for first charge mortgages). This would have a real impact in alleviating mortgage arrears and preventing possession.

— Second charge mortgages play an important role in helping consumers to consolidate their existing debts, at lower and more affordable rates of interest. This provides real support for customers struggling with their finances. But the market faces a funding crisis. The lack of wholesale funds available to lenders has caused the market plunge by 90% in the last year, with no sign of recovery. If funding continues to be restricted in this way, this could have an adverse effect on the level of arrears and possessions in the future, as customers would be unable to reschedule their debts.

— Government lending support schemes currently only cover deposit-taking institutions. Government support for non-deposit taking lenders is now urgently required so as to reopen the wholesale lending markets. For example, amendments to the Government's Guarantee Scheme for Asset-Backed Securities to include the specialist lenders would allow lending to consumers to recommence immediately.

Overview of the Second Charge Mortgage Market

2. Second charge mortgages play a key role in helping consumers improve their homes in a range of ways, so maintaining the country's housing stock and mitigating the downward trend in property prices. Second charge mortgages can also allow consumers to consolidate their existing debts. This is often at a lower and more affordable rate of interest, which is particularly important for customers struggling with their finances.

3. In 2008, the UK second charge mortgage market wrote an estimated £2.5 billion in new business, representing a fall in new lending of around 50% compared to the previous year. The average balance outstanding on second charge mortgages is currently around £28,000, but new advances are on average £14,000.

4. The second charge mortgage market has been significantly hit by the economic downturn, with new business 90% lower in April 2009 alone compared to April 2008. The major reason for this fall is that specialist lenders are facing severe problems in accessing wholesale funding. For some lenders, the wholesale markets have closed completely. As a result, many lenders have reduced their lending significantly, leaving some customers unable to reschedule their loans to lower and more affordable rates of interest. This could have an adverse affect on the level of arrears and possessions in the future. It will also mean that significant numbers of consumers could be driven into the unregulated market, as a last resort for credit.

5. For 2009, we have estimated that without a solution to the funding problem for these specialist lenders, there will be around £1.4 billion of unmet demand for consumer finance.

Arrears and Possessions: Trends and Forecasts

6. Second charge lenders are committed to helping customers in financial difficulties. All such cases are treated sympathetically and positively. Possession is only taken as a last resort, when all other reasonable options have been explored. This is reflected in the low level of repossessions initiated by second charge lenders. In 2008, there were 1,558 repossessions originated by second charge mortgage lenders. This was 11% lower than our forecast for 2008 of 1,750 repossessions. Our forecast for 2009 is 2,000 repossessions, based on rising unemployment.

7. There are also very strong commercial reasons why second charge lenders only seek possession in the very last instance. When a property is repossessed, the first mortgage, together with any fees and charges levied by the first charge mortgage lender, take a priority share of the proceeds of sale. This could mean that a second charge lender does not recover the full amount of their mortgage. Second charge lenders therefore want to work with their customers to reach alternative payment arrangements, which will keep the customer in their home.

8. In recent months, some second charge lenders have reported arrears levels stabilising. But this could be adversely affected over the next 12 months by the expected growth in unemployment.

Existing Forbearance Measures

9. The second charge mortgage industry is regulated by the Consumer Credit Act 1974 (as amended in 2006) and the FLA's Lending Code. All lenders are licensed under the Office of Fair Trading's Consumer Credit Licensing Regime and must adhere to the legislative requirements for licence holders. The Government undertook a detailed review of second charge lending during 2008, and found no systemic problems.

10. Second charge lenders also comply with the Pre-Action Protocol for Mortgages, published by the Civil Justice Council. Together, these impose detailed requirements on how lenders will assist customers who have fallen behind with their repayments.

(a) *Industry initiatives to help borrowers*

FLA Lending Code

11. The FLA Lending Code was established in 1992. It sets good practice standards for all FLA members, including second charge lenders. These standards cover the full life-cycle of a loan from the loan application stage through to how to deal with financial difficulties, should these arise.

12. Under the Code, our members deal with all cases of financial difficulty sympathetically and positively. They must also act fairly, reasonably and responsibly in all their dealings with a customer. The overriding objective is to work with the customer to agree a reasonable repayment plan they can afford.

13. An independent Board oversees compliance with the Code, and a Disciplinary Panel of the FLA's board deals with egregious cases which might lead to expulsion from the Association. The Financial Ombudsman Service has recently stated publicly that the Code sets the accepted standard for the consumer credit industry.

Good Practice Guidelines

14. In November 2008, the FLA published additional *Good Practice Guidelines* for second charge lenders to apply when they are helping customers with payment difficulties. These Guidelines provide additional protection for borrowers and build on the consumer protection provisions already included in legislation and the Lending Code. They also complement the work the Government is currently undertaking on responsible lending. The Guidelines were welcomed by BIS, the Treasury and the OFT.

15. Prior to the completion of a loan, second charge lenders will have already carried out a comprehensive set of underwriting procedures to ensure that the loan is affordable. Customers will also be advised of what to do if they find themselves in payment difficulties.

16. If a customer is in financial difficulties, second charge lenders will:

— Clearly explain their procedures aimed at helping their customer.

— Discuss with their customer the options, and their implications.

— Ensure that the customer's individual circumstances are taken into account, for example whether the causes of the arrears are temporary or long-term.

— Provide the customer with a contact point, in case they have any questions and keep in contact with the customer on a regular basis.

— Ask the customer, in certain circumstances, to complete an income and expenditure form setting out their financial circumstances.

— Consider with the customer a repayment plan which is realistic and appropriate, given the customer's circumstances, and which is aimed at helping the customer remain in their home wherever possible.

17. Examples of repayment plans second charge lenders may discuss with their customers include:

— arrangements to repay arrears over a longer period of time;

— changing the date of the second charge mortgage repayment or the method by which payment is made;

— extending the term of the second charge mortgage;

— changing the type of second charge mortgage; or

— deferring the payment of interest due under the second charge mortgage.

18. Second charge lenders will not take court action where a reasonable repayment plan has been agreed and the customer is sticking to it.

19. Among other commitments in the Guidelines is a pledge to try and make contact with any other mortgage lenders who also have a charge over the property. This aims to avoid a situation where two lenders may take possession action, incurring two sets of legal costs which would be met by the borrower. The FLA and CML are also collaborating to improve the exchange of information between first and second charge lenders.

20. A copy of the Guidelines is attached to this submission.

(b) *Legislative requirements to help borrowers*

Consumer Credit Act 1974 (as amended)

21. The CCA 1974 (as amended) places statutory requirements on second charge lenders when dealing with customers in arrears. These are set out below and include both the provision of prescribed information and the requirement to act fairly.

Arrears notices and default notices—Sections 86 and 93

22. When a borrower is two months in arrears with their second charge mortgage, the lender is required to send a formal Notice of Sums in Arrears. Thereafter, the Notice will continue to be sent every six months until the customer is no longer in arrears or when a court order has been granted.

23. Where a lender intends to take possession of a property, Section 87 provides that a Default Notice must be served on the borrower. The Notice must set out that the agreement has been breached, and how this can be remedied.

Time Orders

24. Once a borrower has been served with a Default Notice, they have the option to apply to the court for a Time Order. The Order is aimed at giving customers more time to pay their debts, and would usually be made for a stipulated period based on the borrower's temporary financial difficulty. In agreeing the Order, the court would look at what instalments would be reasonable and at what intervals.

Unfair relationships—Sections 19–22

25. Under the terms of the CCA, a relationship may be deemed unfair to the debtor due to one or more of the following:

— Any of the terms of the Agreement or related agreement.

— The way in which the creditor has exercised or enforced any of his rights under the agreement or any related agreement.

— Anything done or not done by or on behalf of the creditor

26. The fact that a relationship may have ended would not preclude the court from making such a determination. Once an unfair relationship claim has been made, it is for the lender to prove the contrary. Remedies may include repayment of any amount paid by the debtor, together with the reduction or discharge of any sum payable by the debtor.

27. The unfair relationships provisions have been drafted to provide the county court considerable discretion when hearing a borrower's case.

Fitness Test—section 25

28. The CCA 2006 introduced two concepts which have a bearing on responsible lending. These are the consideration of credit competence and evidence of irresponsible lending, which the OFT must consider when assessing whether a lender is 'fit' to hold a consumer credit licence.

29. The OFT is currently preparing guidance on Irresponsible Lending, which will be published in July. It will cover all stages of the credit cycle, including how all lenders must assist borrowers in financial difficulties. The OFT has suggested that the guidance will incorporate issues such as arrears handling, sale and purchase of debts, use of repayment holidays, default charges, and action on default including possession actions.

30. OFT officials have said that the FLA's members will be well-placed to meet the requirements of the guidance because of the forbearance arrangements already set out in the FLA Lending Code.(See paragraphs 11 to 20 above)

Administration of Justice Acts 1970 and 1973

31. In the majority of arrears cases, second charge lenders and their borrowers are able to agree alternative payment arrangements until normal repayments can be resumed.

32. Section 36(1) of the Administration of Justice Act (AJA) allows a lender to bring a possession action within two months of a borrower falling behind with their repayments. But where possession action is the only route, this period is in practice much longer due to the extensive forbearance measures adopted by lenders. However, there may be cases where earlier action is required—for example, where there is evidence of fraud.

33. The AJA provides considerable discretion to District Judges when considering a possession case, allowing them to adjourn, stay or suspend orders for a reasonable period.

34. The AJA, together with subsequent case law governing the possession process, provides considerable consumer protection for borrowers in financial difficulty.

Pre-Action Protocol for Mortgage Possession Actions

35. Second charge lenders also comply with the Pre-Action Protocol for Mortgages, which was introduced by the Ministry of Justice in November 2008. The Protocol requires lenders and borrowers to act fairly and reasonably with each other. It is aimed at encouraging more pre-action contact between the parties to seek an agreement and to facilitate the efficient use of the court's time, where an agreement cannot be achieved.

36. The Protocol recognises and complements the extensive forbearance action already provided by second charge lenders to customers in arrears. It also provides additional protection for homeowners. For example, under the Protocol, a lender should consider postponing the possession action where:

— A claim has been made under a payment protection policy and this is expected to be accepted by the insurer.

— The borrower can demonstrate that reasonable steps have been or will be taken to market the property at an appropriate price and in accordance with reasonable professional advice.

— A genuine complaint has been made to the Financial Ombudsman Service about the potential possession claim.

37. Prior to the introduction of the Protocol, lenders may have sought a suspended possession order from the court to reinforce an alternative payment arrangement agreed with the borrower. Under the Protocol, they will only be able to seek a possession order once all reasonable options have been discussed with the borrower and these have failed to resolve the position.

38. Together, these legislative remedies provide additional protection to consumers facing possession action.

Government Initiatives

39. The second charge mortgage market has been actively involved in discussions with Government on a range of new initiatives aimed at helping borrowers in arrears, including the Mortgage Rescue Scheme and the Homeowner Mortgage Support Scheme. These complement the forbearance measures adopted by lenders and provide assistance for more vulnerable borrowers.

40. We strongly believe that Support for Mortgage Interest (SMI) should be paid on all second charge mortgages, as well as first charge mortgages. This omission presents a significant gap in consumer protection, which could be addressed quickly and, as average balances are low, the cost to Government would be commensurate with the protection provided. The Government could also look to recoup its funding via a subsequent charge over the property, which would be realised on sale.

Impact of the Credit Crunch on Access to Mortgage Finance

41. The credit crunch has had a fundamental impact on the second charge mortgage market and the severity of the impact is illustrated by the 90% reduction in new business from £227 million in April 2008 to £22 million in April 2009.

42. Many second charge lenders depend on the wholesale funding market. These specialist lenders have traditionally relied on finance from banks to originate assets which were then warehoused, and securitised into the capital markets via the issuance of highly-rated securities. The underlying assets have continued to perform well in the market. But these markets have dried up, leaving only a couple of lenders with very limited funding lines still providing new loans in the market.

43. Government support is now essential and urgent. The Guarantee Scheme for Asset Backed Securities to help support the availability of mortgage finance is currently restricted to banks and building societies. The Crosby Review in 2008 concluded that guarantees on residential mortgage-backed securities should be available to all lenders, including non-deposit takers.

44. The criteria for the Guarantee Scheme need to be amended to allow securities backed by second charge mortgages to qualify. The underlying assets in second charge mortgage securitisations have performed successfully and this reflects the historically low levels of default in the second charge market.

45. If these changes were made to the Guarantee Scheme for Asset Backed Securities (ABS), the specialist non-bank lenders would be in a position to resume new lending immediately. This would revive competition and innovation in the market, help reduce credit prices and bring an end to the current impasse. In our view, a full and sustained economic recovery will only take place when the full spectrum of markets are being fully supported and serviced.

July 2009

Written evidence submitted by the Financial Services Authority (FSA)

1. This memorandum is submitted to the Committee as part of its inquiry into Mortgage Arrears and Access to Mortgage Finance in advance of the FSA's evidence session on 7 July. It covers:

- the current situation in the mortgage market, especially in relation to mortgage arrears;
- our role in relation to the regulation of mortgages;
- what we have been doing on mortgage arrears and repossessions;
- access to mortgage finance; and
- the way forward.

A. Mortgage Market—Current Situation

2. Home ownership and mortgage credit play a vital role in individual lives, in the financial system and in the macro economy. Net housing equity (the value of people's houses after mortgage debt) even after the 20% to 25% fall in prices we have now seen, amounts to about £2.4 trillion—easily the largest segment of household sector net worth.[64] Residential mortgage debt of £1.2 trillion in turn accounts for over half of all credit extended by banks and building societies in the UK. Residential mortgage bad debts can therefore have an important influence on the health of the banks and building societies, as well as a serious impact on

[64] ONS, "Capital stocks tables for publication", Table 5.10, Bank of England and FSA calculations.

the households concerned. Trends in property prices and thus in household wealth have a vital influence on consumer confidence and spending. Trends in the availability of mortgage credit also have a significant impact on house prices. Both over the next few years—as the UK pulls through this recession—and over the long term, the role of the housing market is central.

3. In the UK, as in the US, developments in the mortgage and housing markets in the years running up to the financial crisis created significant risks (the slides referred to below are included in the Annex to this memo):

— the UK, like the US, saw very rapid growth of household debt as percentage of GDP, with that growth (slide 1) dominated by mortgage credit, up from about 55% of GDP in 1998 to over 80% by 2007;

— income leverage increased (slide 2) and an increasing supply of mortgages was available at very high initial loan to value (LTV) ratios, as some borrowers and lenders[65] assumed that debt burdens were likely to fall with continuous property price appreciation. And mortgage credit was extended—not to the same extent as in the US, but still significantly—to categories of borrowers that had not previously had access to it and which were exposed to high credit risk. At the peak of the market, higher–risk loans eg sub–prime, buy–to–let, self–certified and high LTV, had come to account for a significant share of the total market; and

— mortgage arrears and repossessions are now rising (slide 3), and are likely to reach similar levels to those of the early 1990s.

4. On 22 June, we published the latest edition of our Mortgage Lending & Administration Return (MLAR) covering the period from 2007 Q4 to the end of 2009 Q1. The key results in terms of arrears and repossessions as at Q1 2009 are as follows:

— Helped by lower interest rates, numbers of new arrears cases in Q1 2009 were 12% fewer at 60,000 compared to the 68,000 recorded in Q4 2008, and are now back to volumes seen in Q3 2008. Even so, this is still 10% more than the typical quarterly volumes of 54,000 seen in the 18 months to mid 2008.

— But with borrowers increasingly struggling to clear their arrears, the total number of loan accounts in arrears has been steadily increasing since early 2007. At the end of Q1 2009 there were 399,000 loan accounts in arrears, an increase of 22,000 or 6% since Q4 2008, and representing a rise of 33% on a year earlier.

— Numbers of new repossessions have grown significantly since Q3 2007, but the sharply rising trend noted up to Q3 last year appears to have moderated in the last two quarters. After 13,469 cases in Q3 2008, numbers fell to 13,115 in Q4 2008, with a 13% rise in Q1 2009 to 14,825 cases. New repossessions in Q1 2009 were nonetheless 62% higher than a year earlier.

Mortgage arrears and repossessions—comparison to the 1990s

5. Although repossessions are now at a similar level to the 1990s cycle (see slide 4) the economic conditions look very different. Between 1988 and 1990, mortgage interest rates rose from about 9% to 14% and stayed there until autumn 1992. That rise produced a very large increase in the percentage of income devoted to mortgage interest which, alongside rising unemployment, played a crucial role in driving the dramatic rise in arrears and repossessions between 1988 and 1992.

6. In addition, data[66] shows that from 1995 to 2005–06 the main reasons for mortgage arrears were loss of income from sickness, unemployment or household changes such as marital breakdown. This is supported by recent Bank of England analysis suggesting that the key determinants of mortgage arrears are unemployment and available housing equity.

7. In this recession, interest rates have fallen dramatically and many consumers with tracker mortgages are benefiting from very low rates of interest. This suggests that other factors are contributing to current arrears and repossession levels. In 2007, mortgage equity withdrawal was significantly greater than in the 1990s, and its fall since the general tightening of credit conditions and the fall in house prices in late 2007 has been much greater. Up until 2007 consumers were still able to remortgage to release equity to continue to supplement discretionary income and finance their debts which is likely to have lowered the number of repossessions in late 2008/early 2009.

8. The sharp drop in house prices, tightening of credit conditions and the demise of the specialist lending market is likely to increase the number of repossessions in the rest of 2009 and into 2010, as highly indebted borrowers heavily reliant on equity withdrawal are no longer able to refinance outstanding debts. As slide 5 shows, non–bank and building society lenders whose business models have typically targeted indebted consumers have seen their share of repossessions increase since the beginning of 2007 relative to their overall market share.

[65] Lenders within the context of this memorandum refers to mortgage lenders and third party administrators.
[66] Report from Survey of English Housing.

9. Many of these consumers also relied heavily on unregulated sources of credit (also now severely restricted) to increase their spending power. Our analysis of repossession orders has shown that even where the original lending decision looked to be affordable, affordability was severely compromised by the overall level of debt secured against their home, including second charges and other forms of unregulated credit. This is one of the reasons we are considering, as part of the Mortgage Market Review work (see paragraphs 41—42), whether we should recommend to the Treasury that our scope should be extended to include second charge lending so that we have overall sight of affordability and responsible lending.

10. Another factor not present in the last recession was buy–to–let mortgages. While real rental returns net of mortgage payments have been negative for most of the period since 2004, many landlords continued to hold onto their properties if the capital appreciation was expected to more than offset the net loss from the rental income. As property prices started to fall, many landlords found that the losses being made on the rentals through falling real rental returns and plummeting house prices meant that the investment was no longer viable. In addition a significant proportion of defaults are occurring on new houses, and prices in this sector have shown little growth since 2005, increasing the probability of default.

11. The upward trend in arrears and repossession remains of great concern particularly as we believe we have yet to see the traditional determinants of default such as unemployment feed through into the figures. It is, however, important to look at the levels of arrears and repossessions in comparison to all mortgages outstanding. According to recent figures published in our Mortgage Lending and Administration Return the proportion of the residential loan book that is in arrears, and hence not fully performing, rose to 3.64% at end Q1 2009, up 0.27% in the quarter and up 1.23% on a year earlier.

B. FSA Role

12. The FSA took on responsibility for regulating mortgage lending, administration, advice and arranging in October 2004. This was limited to first charge mortgages on residential properties and lifetime mortgages. In April 2007, our scope was extended to cover home reversion plans and home purchase plans.

Our rules

13. We have set out the standards we expect firms to meet in dealing with their mortgage customers. Our mortgage regime is designed to deliver the following outcomes:

— Consumers are able to shop around for mortgages;

— Consumers understand whether they are being given advice or information by firms;

— Consumers take out suitable and good value mortgages;

— Consumers better understand the risks and features of the mortgages they take out, including the affordability risks; and

— Consumers are treated fairly over the life of the mortgage, including in arrears or repossessions.

14. Our rules include 11 Principles of Business which are applicable to all firms, including mortgage lenders and intermediaries. The Principles set the high level standard that firms must meet, including Principle 6 which states that:

— *A firm must pay due regard to the interests of its customers and treat them fairly.*

15. In pursuit of our consumer protection and public awareness objectives, our Mortgage Conduct of Business Handbook provides rules and guidance on financial promotion, advising and selling standards, disclosure (at pre–application, offer, and post sale stage); equity release products; responsible lending; charges; annual percentage rate; and arrears and repossessions. These rules apply to mortgage lenders and intermediaries.

16. Our rules on mortgage arrears require lenders to have a written policy and procedures in place designed to ensure that they treat customers in financial difficulties fairly. These include requirements to use reasonable efforts to reach agreement with the customer, adopt a reasonable approach to the time over which any shortfall in payments can be made good and take repossession action only where all other reasonable attempts to resolve the position have failed. They also require that charges imposed on a customer in arrears do not exceed a reasonable estimate of the additional cost incurred (see the section below on *Mortgage arrears and repossessions handling review* for examples of the action we have taken on this issue).

Sale and rent back (SRB) schemes

17. SRB schemes involve individuals selling their home, usually at a discount, and obtaining an agreement to remain in the property for a set period—typically through an assured shorthold tenancy of six to 12 months. In October 2008, the OFT published a SRB market study[67] which recommended statutory regulation of SRB schemes. In June this year, the Treasury announced that it would be extending our regulation of mortgages to include SRB schemes.

[67] http://www.oft.gov.uk/shared_oft/reports/consumer_protection/oft1018.pdf

18. We are taking a two–stage approach to implementing the Treasury's decision. An interim regime came into force on 1 July. Under this regime, firms will need to meet our threshold conditions including the requirement to have adequate resources and to be run by fit and proper people. They will also have to comply with the Principles for Businesses and meet a number of systems and controls and conduct of business rules. This will be followed by a more comprehensive regime, which will start on 30 June 2010 and on which we will consult in autumn 2009.

Second charge lending

19. We do not regulate second charge lending which is the responsibility of the Office of Fair Trading (OFT) under the Consumer Credit Act.

Buy–to–let (BTL) mortgages

20. We do not regulate BTL mortgages. When the Government introduced mortgage regulation through the FSA in 2004, it drew a distinction between owner–occupiers who face losing their home if things go wrong, and BTL landlords, whose properties are investments and who do not face the same risks. Consumer protection regulation, therefore, did not extend to BTL mortgages. However, lenders that advance BTL mortgages are subject to prudential regulation as they are required to hold capital against the mortgages they have advanced.

Social housing

21. Nor do we regulate social housing. Social landlords are regulated by the Audit Commission and the Housing Corporation, the government agency that funds new affordable housing and regulates housing associations in England.

C. FSA Work on Mortgage Arrears and Repossessions

22. Since we took on responsibility for mortgage regulation we have carried out a programme of work designed to monitor the effectiveness of our regulation of mortgage lending, address key issues in the mortgage sector and ensure that consumers are treated fairly and can make informed decisions.

Mortgage arrears and repossessions handling review

23. In late 2007, we became increasingly concerned by evidence, both from our own mortgage effectiveness review and from external reports by charities such as the Citizens Advice Bureau and Shelter, that some mortgage lenders were failing to treat their customers fairly when they fell into arrears. We reviewed the arrears–management policy and practices of a sample of mortgage lenders. We have begun enforcement action against five lenders for failure to adhere to our rules in this area. Several more lenders are being assessed for further investigation, with a view to taking enforcement action.

24. The first phase of the review was launched in December 2007 and considered a broad cross–section of mortgage lenders, including high–street firms, smaller building societies and specialist lenders.[68] In our findings, published in August 2008, we noted that mainstream lenders were largely complying with our requirements. However, there were particular concerns with specialist lenders, including that they:

— operated a "one size fits all" approach, focused too strongly on recovering arrears according to a strict mandate, without reference to the borrower's circumstances;

— were too ready to take court action; and

— had lower standards of systems and controls in place to control mortgage arrears handling, including training and competency arrangements.

25. The review also found issues with lenders in general, including that some:

— could have done more to consider customers' individual circumstances and offer more options to resolve the arrears position;

— imposed charges in circumstances that could result in the unfair treatment of customers; and

— did not exercise sufficient oversight of third parties contracted to carry out mortgage arrears and repossessions handling activities on behalf of lenders.

26. To help lenders assess and improve their arrears–handling practices, we provided feedback to the individual lenders and required them to take action to address the shortcomings. We also published good and poor practice examples on our website, illustrating where lenders were operating at/above or below our minimum requirements respectively.[69]

[68] In the context of our arrears work, the term specialist lender refers to non deposit taking lenders with business models that target indebted consumers/those who cannot provide income verification.

[69] http://www.fsa.gov.uk/pages/About/What/thematic/mortgage_arrears/examples/index.shtml

27. We continued to maintain our focus on arrears handling and in November 2008, Jon Pain (our Managing Director, Retail Markets), wrote to the chief executives of all mortgage lenders and administrators to remind them of their responsibilities under our Mortgage Conduct of Business rules. We required senior management to review their current arrears policies and management practices and procedures. We specifically asked them to review a sample of cases to assess whether our requirements are being met and to revert to us with their findings.[70]

28. In line with our commitment to continue to scrutinise lenders' treatment of customers in arrears, we have followed up the responses to the letter in a number of ways. This includes:

— requiring a number of lenders to make further changes to their policies and procedures—we have set review dates to follow this up with them; and

— continuing to focus on arrears handling and collections as part of our ongoing supervision of lenders.

29. Phase two of our review began in early 2009 and focused more specifically on areas identified as problematic in phase one, in particular specialist lenders to the impaired credit market who are no longer lending, and third party administrators (TPAs) contracted to handle mortgage arrears and repossessions work on behalf of lenders. It also looked at arrears charges and the treatment of borrowers whose mortgages have been securitised.

30. We published our results from phase two on 22 June this year.[71] We found that poor practice had been prevalent among some specialist lenders and TPAs including:

— an approach focused too strongly on recovering arrears without reference to the borrower's individual circumstances;

— being too ready to take court action;

— imposing arrears–related charges unfairly;

— specialist lenders not exercising sufficient oversight of contracted TPAs; and

— terms in securitisation covenants which could lead to inequitable treatment of borrowers in arrears.

31. All the lenders we investigated had made recent changes to policies and procedures and there were signs of greater awareness of the need to treat customers fairly. This included providing a greater range of options to distressed borrowers. However, we did not see evidence that this had yet translated into better outcomes for customers in arrears.

32. We are requiring all firms from our sample to take action to remedy particular failures identified. In addition, we are formally investigating a further four lenders, with a view to taking enforcement action. We have also published a more detailed briefing for mortgage lenders, which includes practical examples designed to help lenders improve their mortgage arrears and handling practices.[72] We have also updated the fees and charges section of the good and poor practice examples we published following the first stage of the review in August 2008.

33. We will feed the findings from the project into the wider Mortgage Market Review (see below) which we are carrying out and we will use them to identify areas where in the longer term we may need to change our rules. This may include changes to our rules on fees and charges, on the relationship between lenders and third party administrators and on the interaction between securitisation and arrears handling.

Consumers

34. To help consumers in arrears to decide what steps to take we have published a wide range of mortgage material on our Moneymadeclear website. This includes, the "*What to do when you can't pay your mortgage"* guide, which offers practical help for people who are struggling with mortgage repayments and states the options available to them.[73] We require lenders to send this guide to consumers who fall into arrears.

Civil Justice Council pre–action protocol

35. On 19 November 2008, the Ministry of Justice introduced a pre–action protocol which sets out the steps that mortgage lenders are expected to take before bringing a repossession claim to the courts.[74] This is currently applicable to England and Wales only. Lenders are now required to demonstrate to the courts that they have investigated all alternatives before resorting to repossessions. We welcome the pre–action protocol which complements our requirements for the fair treatment of customers in payment difficulties in our Mortgage Conduct of Business sourcebook

[70] http://www.fsa.gov.uk/pages/Library/Communication/PR/2008/142.shtml
[71] http://www.fsa.gov.uk/Pages/Library/Communication/PR/2009/080.shtml
[72] http://www.fsa.gov.uk/pages/About/What/thematic/mortgage_arrears/examples/index.shtml
[73] http://www.moneymadeclear.fsa.gov.uk/pdfs/mortgage_cantpay.pdf
[74] http://www.justice.gov.uk/civil/procrules_fin/pdf/protocols/prot_mha.pdf

D. Access to Mortgage Finance

36. Our analysis shows that despite a tripling in lending between 1998 and 2008 from £400 billion to £1,200 billion of mortgage balances outstanding (slide 6), home ownership during that period has remained stagnant (slide 7). This is because most mortgage lending occurred for the purpose of equity withdrawal or buy–to–let mortgages (slide 8).

37. The reduction in gross mortgage lending in the last 12 months is almost entirely due to a reduction in remortgaging activity (as borrowers opt to stay on lenders' standard variable rates or cannot remortgage more cheaply due to a decline in their equity). Lending for house purchases has increased throughout 2009 and net mortgage lending has remained positive throughout the past 18 months.[75] We have taken steps to reduce the unintended procyclicality effects of the Capital Requirements Directive. We have applied a flexible approach to help reduce the risk that capital requirements under the Basel II framework do not increase sharply during the economic downturn thereby restricting lending, while also ensuring sufficient capital is held. However, even if banks have sufficient capital to hold against new lending there is still a need to fund this and, in the absence of a significant increase in the savings ratio or a thawing of the wholesale funding markets, this remains difficult.

38. It should be noted that, while we will form a view of the sustainability of a firm's business model and the appropriateness of its systems and controls to support this (and we will act where we have concerns in these areas), it is not our role to dictate business volumes to firms. That remains a commercial decision.

Asset Backed Securities Guarantee Scheme

39. Before the financial crisis broke in August 2007, the securitisation markets played a key and fundamental role in the capital markets. At its peak, the securitisation markets funded approximately one third of all UK Mortgages. The closure of the securitisation markets has had a significant impact on the availability of funding for the UK housing and mortgage market. Given the significance of the securitisation market, the Treasury and the FSA worked closely with market participants to design the Asset Backed Securities (ABS) Guarantee Scheme which was launched in the April Budget. This scheme provides either a credit or a liquidity guarantee on Residential Mortgage Backed Security (RMBS) backed by eligible mortgages originated after January 2008. The scheme is intended to provide confidence to the RMBS market to encourage investor appetite and thus improve banks and building societies access to capital markets funding and to help support lending to credit worthy borrowers in order to promote robust and sustainable markets over the long term. The ABS Guarantee Scheme was met with a positive reaction from issuers and investors on its launch.

Liquidity

40. We are currently conducting a comprehensive review and restructuring of our liquidity regime. We have published three Consultation Papers on strengthening liquidity standards (December 2008, April 2009 and June 2009). Our proposed policy will increase the cost of lending to certain consumers, which will align this type of lending activity with the increased liquidity risks associated with it. Our new policy will also require firms to quantify the liquidity costs, benefits and risks in relation to all significant business activities and to incorporate them in their product pricing and performance measurement. This will ensure that the risk–taking incentives of individual business lines—including mortgage lending—are properly aligned with the liquidity risk to which a firm is exposed as a result of such activities. In addition we anticipate that our new liquidity policy will result in a check on unsustainable expansion of bank lending during favourable economic times.

41. As noted in the *Turner Review*, we believe that our liquidity policy will imply less aggregate maturity transformation than would otherwise occur, and this must in theory carry some economic cost. The crucial trade–off—as with the costs of higher bank capital—is between a small net cost to the economy during "normal times" and the benefits of the reduced probability of extreme adverse events. Assessing and comparing these potential costs and benefits is extremely difficult. However, given the scale of the economic fallout from the financial crisis, a reasonable judgement is that a significant tightening of regulatory constraints on liquidity (and thus on aggregate system–wide maturity transformation) is justified in order to reduce risks to future financial stability.

E. Looking Forward

42. In our *Business Plan* for 2008/09 we committed to reviewing our mortgage conduct of business regime. Our work on assessing whether the regime has delivered the right outcomes for consumers suggested that changes to our rules in this area alone would not be sufficient. We, therefore, expanded the scope of the work to encompass a comprehensive review of the wider mortgage market, with a view to achieving two outcomes: a market that is sustainable for all participants (consumers, intermediaries, lenders and investors); and a flexible market that works for customers. The review cuts across the economic cycle and identifies issues that arose during the boom before the financial crisis broke, with the aim of implementing a suitable regulatory framework before the next upswing of the cycle. We will develop a view on the future shape of this market

[75] http://www.bankofengland.co.uk/publications/other/monetary/TrendsJune09.pdf

and on how our approach to regulation should evolve. Our review covers the complete value–chain in the market (eg lenders, intermediaries, consumers and investors) and all aspects of regulation, including prudential, conduct of business, and financial crime. We are also considering whether any read–across to the mortgage market is appropriate from the proposals in our Retail Distribution Review.

43. In the *Turner Review*, we raised the issue of whether we should consider limits on maximum loan–to–value (LTV) or loan–to–income (LTI) ratios. We will address this, along with the issues identified in the Mortgage Market Review, in a Discussion Paper (DP) to be published in autumn 2009. The DP will also assess:

— whether we should recommend to the Treasury that our scope should be extended to buy–to–let and/or second charge lending;

— whether we should change our rules to require income verification for all mortgages or should encourage lenders to lend responsibly through our capital requirements;

— the extension of the approved persons regime which would mean that all mortgage advisers and arrangers would be individually vetted and registered; and

— the role of responsible borrowing and whether further consumer education is required.

44. The European Commission is working on measures to promote responsible lending and borrowing and is planning to present policy measures in the autumn, as well as creating a regulatory framework on credit intermediation. We will contribute fully to these discussions.

45. Ensuring that consumers in mortgage arrears are treated fairly will remain a high priority for the FSA, and firms can expect continued focus and scrutiny in this area, including more use of outcomes testing, as part of our normal supervision process.

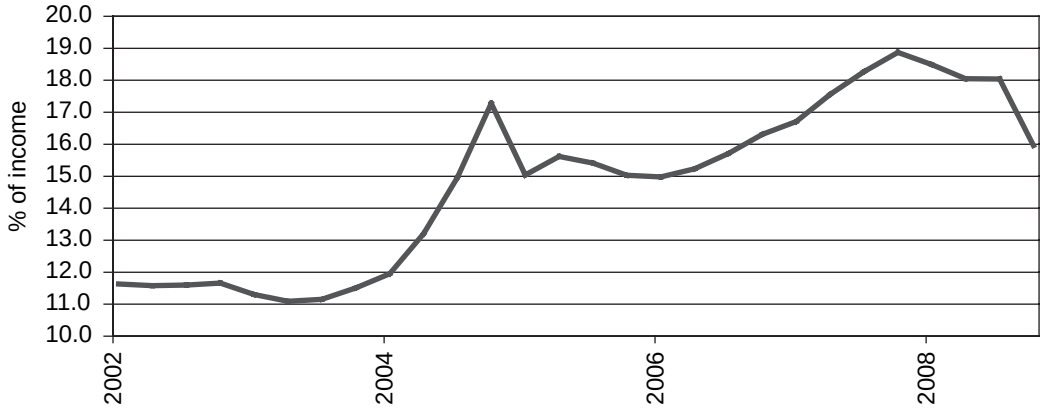
2 July 2009

Annex

Slide 1

Slide 2

Median mortgage interest payments as a percentage of income

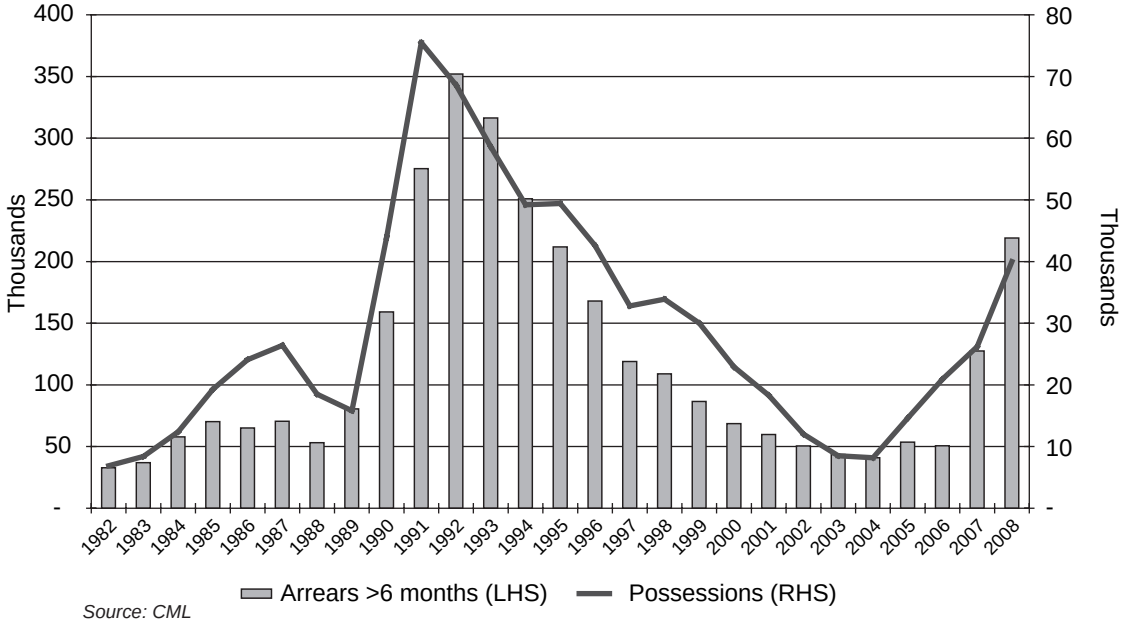


The long term average of mortgage interest as a percentage of income is 15.8% for the period since 1974

Source: CML Regulated Mortgage Survey

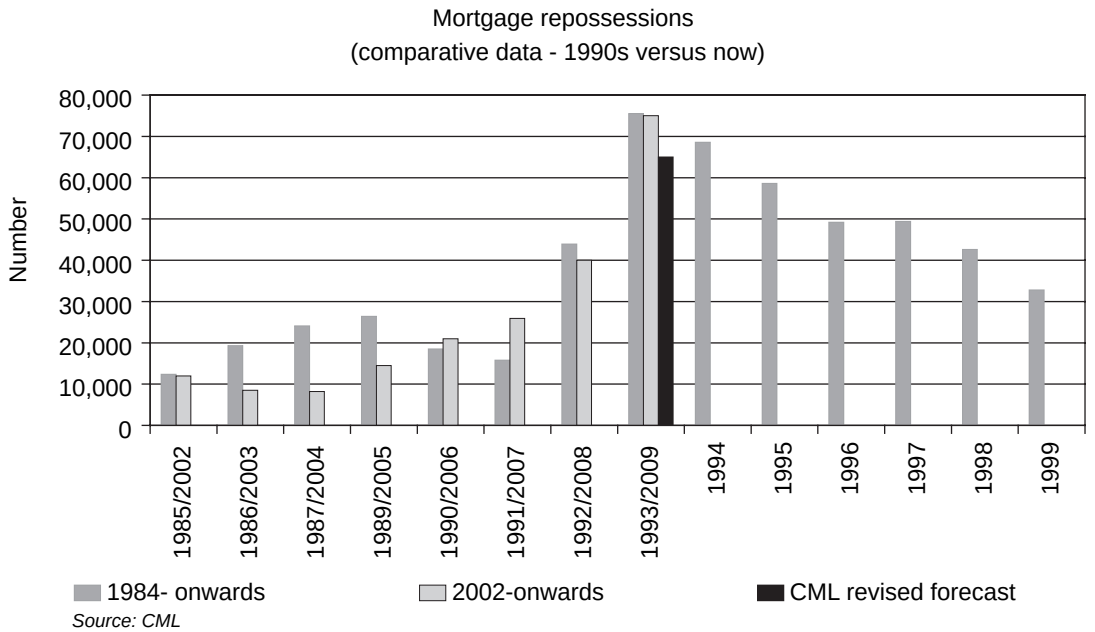
Slide 3

UK mortgage arrears and repossesions



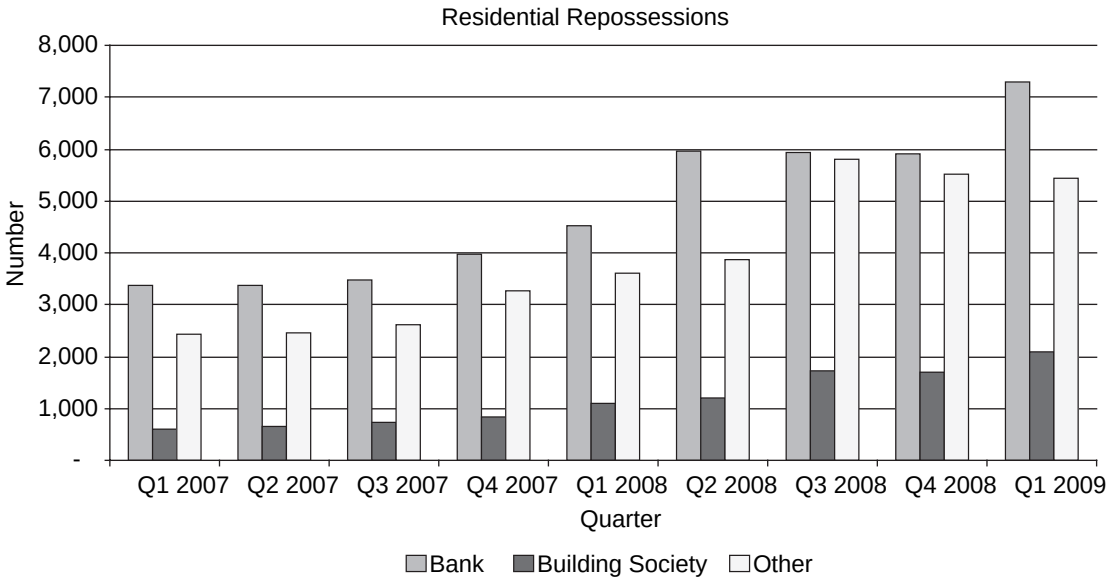
Source: CML

Slide 4



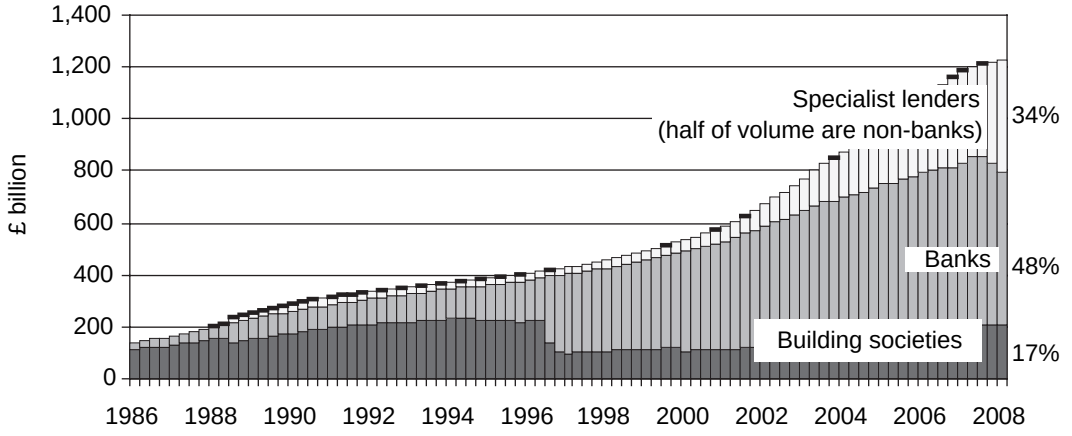
Source: CML

Slide 5



Slide 6

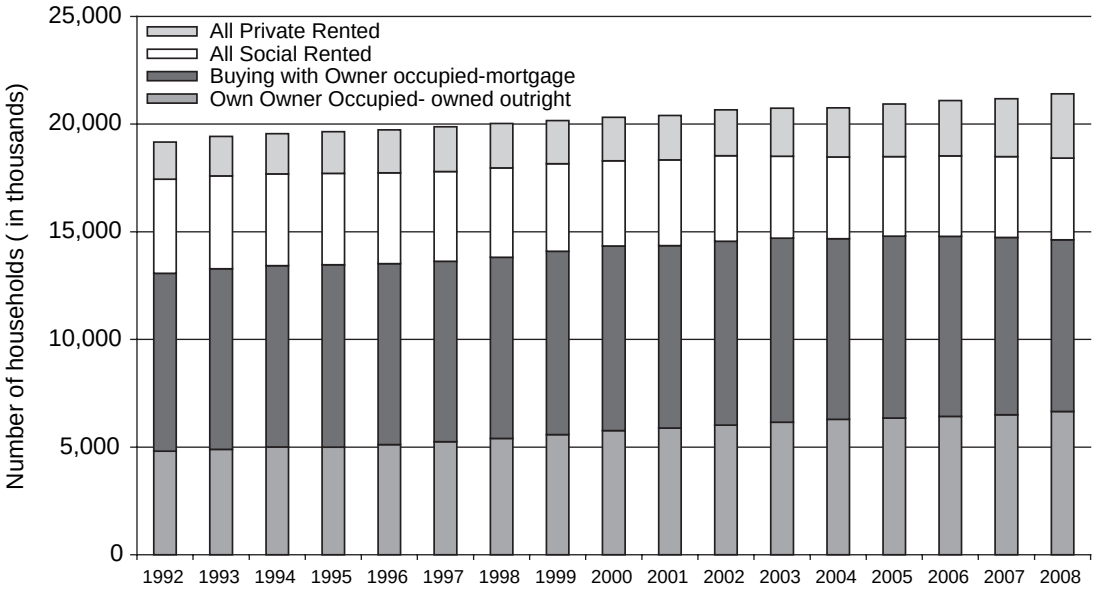
Mortgage balances outstanding, by type of lender



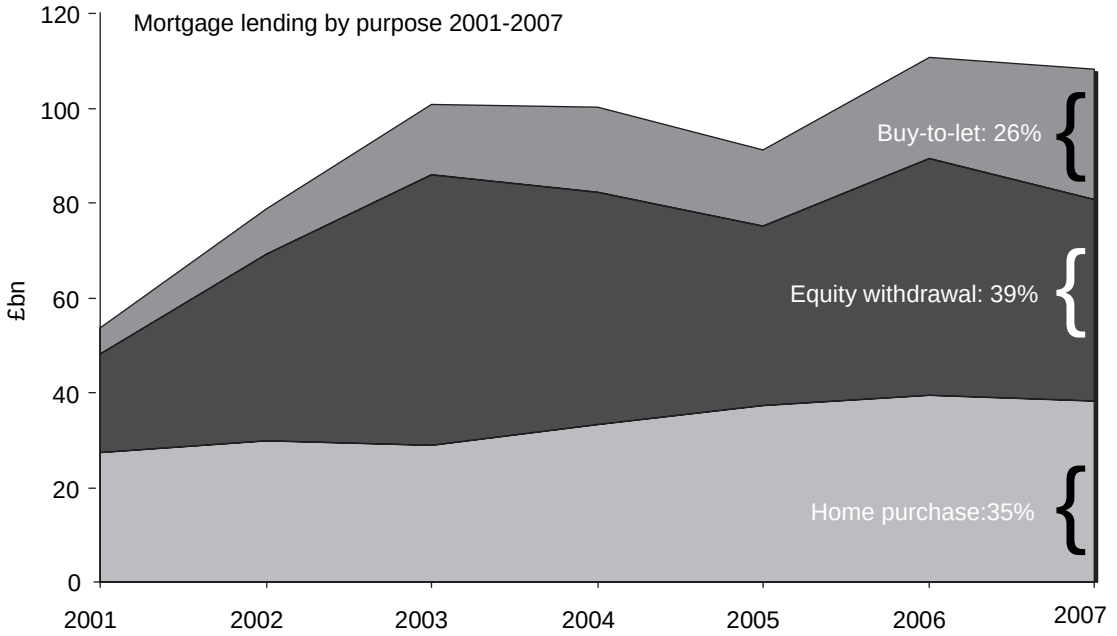
Source: Bank of England, tables LPQVTXI, TXJ, TXK, UFO, UFP

Slide 7

Home Ownership Characteristics of UK households



Slide 8



Source: Bank of England, CML, FSA calculations

Written evidence submitted by Shelter

Shelter welcomes the Committee's inquiry into mortgage arrears and access to mortgage finance. As a result of the housing market downturn and recession there are hundreds of thousands of households dealing with—or on the precipice of—arrears and repossession. While there has been significant progress in recent months, with increased lender forbearance and the introduction of a range of government prevention initiatives, there is undoubtedly much more to do to prevent a worsening situation over the next 18–24 months.

1. *The current number of homeowners in mortgage arrears and forecasts for the trend in mortgage arrears over the medium-term*

2. *The number and characteristics of homeowners who have had their properties repossessed, the number in the process of having their homes repossessed, as well as forecasts for the trend in repossession levels over the medium-term*

Statistics show that arrears and repossessions are already the worst they've been since the peak of the last recession in 1991, and all indications are that numbers will continue to rise as arrears and repossessions move from marginal to mainstream borrowers.

- First quarter 2009 CML stats:
  - 205,300 mortgage loans with arrears of more than 2.5% of the mortgage balance (12% increase on fourth quarter 2008).
  - 12,800 repossessions (23% increase on fourth quarter 2008).
- CML forecasts for 2009:
  - 360,000 mortgages will be in arrears of more than 2.5%.
  - 65,000 repossessions.
- Over the last year Shelter has seen a 250% increase in calls to our free helpline on mortgage arrears, and an 85% increase in calls on repossession problems.
- Economist Ian Shepherdson predicted two weeks ago that repossessions would reach 100,000–120,000 in 2011.
- The characteristics of those most likely to have their homes repossessed are: a) those at the lower end of the income range at which home ownership is possible; b) those made redundant or who have had their income reduced; c) those experiencing relationship breakdown; d) vulnerable households, first time buyers, and the self-employed; and e) those who lack basic financial capability and with significant other debts.

— Evidence from Shelter clients and conversations with lenders indicate that those who have been first to fall this time round have been marginal borrowers—especially with high loan to income (LTI)/loan to value (LTV) mortgages from recent years.

— Anecdotally we are now seeing more mainstream borrowers struggling as unemployment feeds through—economic modelling from Oxford Econometric Forecasting suggests that job loss is perhaps the most important reason for mortgagors moving into arrears and subsequently having their property possessed. The long-run arrears and possessions rates to unemployment is around 3:1 ie a 10% sustained increase in the unemployment rate will eventually raise both arrears and possessions by 30%.

— We are also seeing more clients who are self employed or contract workers—loss of income rather than unemployment as such affects this group and they are likely to have more difficulty accessing benefits.

These figures are alarming enough, but there are a number of factors which could combine to generate a more serious "second wave" of arrears and repossessions in 2010–11:

— Interest rate rises: Shelter's forthcoming research from the University of York[76] has concluded that substantial reductions in bank base rates have been a significant form of arrears and repossession prevention to date, and rising interest rates are very likely to lead to rising arrears. However, lenders interviewed for this research saw the likely upward trajectory of interest rates as a "*predictable but unexplored*" issue.

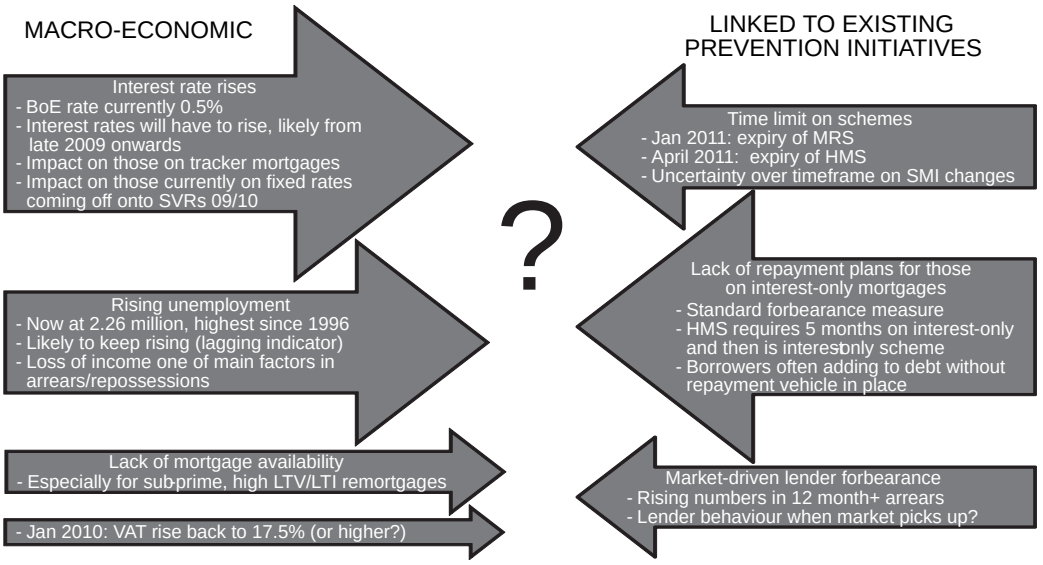
— Rising unemployment: Loss of income is one of the major triggers for falling behind with mortgage payments. Unemployment is now at 2.26 million, and as a lagging three million and possibly more. Over a quarter of respondents (27%) to Shelter's recent sub-prime borrower survey[77] said they expect to experience a significant loss in income over the next six months due to reduced working hours, redundancy or unemployment, and over a third of all respondents said that if they had a significant drop in their income for six months they would be unable to fully meet their mortgage payments each month.

— Lack of mortgage availability: In our sub-prime borrower survey, 18% of respondents said that they would be coming to the end of their fixed rate mortgage deals in 2009. Given the sharp contraction in mortgage lending, particularly in the sub-prime sector, many borrowers may be unable to secure remortgages at affordable rates, and will be forced into arrears through a hike in monthly payments.

— Time limit on schemes: Shelter's York research concludes that the time limited nature of the current initiatives suggests that government and lenders should already be considering the exit process to avoid a spike in repossessions in 2011–12.

— We were interested to note that both CML and IMLA concurred with this assessment of the impact of future interest rate rises and rising unemployment in their oral evidence.

Factors which may contribute to second wave of repossessions in 2010/2011



[76] Ford, J and Wallace, A, *Uncharted territory? Managing mortgage arrears and repossessions,* Shelter, forthcoming 2009.
[77] *Survey of Sub-Prime Borrowers: Results and Recommendations,* Shelter, May 2009.

3. *The treatment, and the approaches taken, by mortgage lenders towards homeowners in arrears and/or at risk of repossession, including issues relating to the treatment of homeowners by financial institutions specialising in mortgage lending to sub-prime borrowers*

While there has certainly been a significant improvement in practices towards homeowners in difficulty among many lenders, Shelter is still seeing a variation in practice—and particularly in the practice of sub-prime lenders—which means that some borrowers are particularly vulnerable to harsh or unfair treatment: the lender lottery:

— Variation in behaviour among lenders: Earlier this year the advice sector undertook research on mortgage and secured loan arrears with advisers and borrowers.[78] Among borrowers surveyed, while 57% of those in mortgage arrears were satisfied with the way they were treated by their lender, 27% of those in mortgage arrears said their lender offered them no help when told about their repayment problems. In Shelter's sub-prime survey, a fifth of those falling behind with their payments reported that their lender had *not* been in contact with them. Of those who had been in contact with their lender, experience varied significantly—38% rated their lender's willingness to renegotiate a new payment plan as poor/very poor, compared to 27% who rated it as good/excellent. Similarly, 48% reported the range of options discussed with their lender as poor/very poor, compared with 21% who said this was good/excellent.

— Particularly poor practice among sub-prime lenders: In Shelter's sub-prime survey, a fifth of those falling behind with their payments reported that their lender had *not* been in contact with them. Of those who had been in contact with their lender, experience varied significantly—38% rated their lender's willingness to renegotiate a new payment plan as poor/very poor, compared to 27% who rated it as good/excellent. Similarly, 48% reported the range of options discussed with their lender as poor/very poor, compared with 21% who said this was good/excellent.

— Market-driven lender forbearance: Shelter's York research provides evidence that lenders' increased forbearance has been driven to a large extent by the consideration of avoiding potential losses from a declining market, rather than by regulatory supervision and enforcement. When the housing market picks up, lenders may revert to less sympathetic practices and repossess in far greater numbers than they are currently doing.

4. *Adherence to, and the effectiveness of, Financial Services Authority (FSA) rules and guidance for mortgage lenders on repossession policy and treatment of consumers in arrears as well as the FSA's regulatory approach in this area*

5. *Adherence to, and the effectiveness of, codes of conduct, protocols and statements of good practice issued by industry bodies in this area*

As outlined in the section above, there are still significant variations in lender behaviour towards borrowers in difficulty, and a number of practices—particularly among sub-prime lenders—that clearly contravene FSA rules and guidance. Shelter believes that there have been serious weaknesses in the FSA's regulatory approach to date, and that overall the FSA has been slow to act to tackle non-compliance.

— Length of time on mortgage arrears review: We are alarmed at the length of time the FSA has taken to undertake its thematic mortgage arrears review—the first phase was published in August 2008 and the second phase in June 2009, during which time approximately 40,000 more households were repossessed.

— Leniency with which FSA has treated lenders: In our view, the FSA has adopted a carrot rather than stick approach which has left borrowers at the mercy of unscrupulous lenders for far too long. After the first phase, which found serious weaknesses in the way some lenders were handling arrears and repossessions, the FSA called for lenders to treat customers fairly and published examples of good and poor practice, but *took no enforcement action* against specific lenders. The second phase found continued weaknesses and the FSA has finally referred four firms for enforcement.

— No naming and shaming: The FSA refuses to publicly name these firms therefore borrowers who have been—or may be in the future—poorly treated have not been empowered with the knowledge to challenge this directly with their lenders. This is not the case, as was argued by lender representative bodies in their oral evidence, of maintaining anonymity while suspected breaches are investigated—the firms referred for enforcement have been found categorically in breach of FSA regulations, and we see no reason not to name them while they are undergoing enforcement action. This lack of transparency in the regulatory regime is a significant barrier to securing improved practice and behaviour across all lenders.

— Lack of consumer redress: Even where the FSA is now taking enforcement action, it is not doing any work to introduce consumer redress for those borrowers who were mis-treated by lenders, and who may have suffered significant financial loss as a result.

[78] *Mortgage and secured loan arrears: Adviser and Borrower Surveys April 2009*, AdviceUK, Citizens Advice, Money Advice Trust and Shelter, April 2009.

— Principles rather than rules-based regulation: The principles-based regulation in MCOB (Mortgage Conduct of Business) and TCF (Treating Customers Fairly) leaves far too much flexibility for lenders to interpret how they choose, which means that consumers are not treated consistently and have no way of establishing what is "fair" practice and what is not.

— Mortgage market review: We desperately need a more robust regulatory regime and tougher enforcement practices, and we look to the FSA's forthcoming mortgage market review to signal a step change in the relationship between lenders and the regulator.

— Need for industry guidance to be codified into regulation: In its oral evidence to the Committee, CML stated that its industry best practice guidance was intended to break down the high level principles contained in MCOB, and that this guidance was "widely used" across the industry. In this context, we see no reason why the FSA shouldn't introduce equivalent practice as a statutory requirement in an amended regulatory regime, to ensure that all borrowers benefit from consistent fair practice across the industry, and that this is not just "widely" but *universally* used by all lenders.

— Clarification of "debt counsellors": Following a number of comments about "debt counsellors" used (and indeed charged for) by lenders, we would like to clarify that, in many cases, these do not refer to providers of debt advice but rather field collection agents. In its thematic mortgage arrears review work the FSA commented as follows: *"Firms should not give the impression they provide debt advice or counselling if they do not. Some firms are still referring to their staff or agents who visit customers in their home to discuss arrears and repayment plans or collect money on behalf of the lender as "debt counsellors". We have previously stated that it is good practice to refer to this function by a title that accurately describes the role, for example, "field collection agent" not "debt counsellor". …. We have noted that some firms have changed the title they use for this function, but in some cases the new title still suggests that counselling will be provided. We ask firms to use an appropriate title for this function in order to be clear, fair and not misleading about the services they provide."*

6. *Issues of concern around the operation of sale and lease-back schemes*

Shelter has seen many clients exploited by private sale and lease-back schemes. We campaigned hard for regulation and welcome the introduction of the FSA interim regime. We will be closely monitoring the evidence to ensure that the FSA regulates quickly and robustly, and are keen to see a move towards the full regulatory regime as soon as possible.

— *Problems with private sale and lease-back schemes:*

  — The OFT report in 2008[79] estimated that there were upwards of 1,000 private sale and lease-back firms (plus more individuals), who had completed over 50,000 transactions to date

  — Transactions often involve significant loss of equity in the home, with sales typically at 15–20% or more (sometimes up to 40%) *below* market value

  — Leaseback arrangements are almost always on assured shorthold tenancies, with a minimum six month contract. Shelter has seen many clients who have come to the end of their six month contract and then been evicted by their landlord

  — We have also seen a number of cases where the buyer/landlord fails to keep up with mortgage payments on the home, and the home is subsequently repossessed and the tenants (former owners) evicted

  — Limited information provided up front (or in writing—transactions are often based around verbal agreements over a very short time period) means that consumers are often hit by additional fees and charges and higher rent once they are past the point of sale, at which point there is very little they can do

  — In our experience, sale and lease-back companies generally don't offer or signpost to independent advice on alternative options which may be better for the consumer.

— *FSA interim regime*: This came into force on 1 July. Shelter welcomes this regime overall, however we are concerned that the provision requiring an independent valuation has been removed, which we believe removes some security for the borrower that the valuation is open and transparent.

— *FSA role*: The FSA must regulate effectively and enforce quickly where companies are not complying; we emphatically don't want a repeat of the slow progress that we have seen on mortgage arrears regulation.

— *Full regime*: We are also keen for this to be introduced as soon as possible.

[79] *Sale and rent back: An OFT market study*, Office of Fair Trading, October 2008.

7. *The success of those Government schemes in existence before the financial crisis to support homeowners facing difficulties with mortgage payments and/or at risk of repossession, as well as the effectiveness of initiatives introduced since the financial crisis began*

Shelter welcomes the fact that Government has acted quickly to introduce help for homeowners in difficulty, and there are merits in each of the schemes introduced. However, the need for these new initiatives illustrates the inadequacy of the existing safety nets, and we have some outstanding concerns about the temporary nature and complexity of the schemes introduced.

— *Support for Mortgage Interest (SMI)*: On the whole Shelter believes the changes to SMI have been effective, especially the reduction in the waiting period from 39 to 13 weeks, but we would like to see a fundamental review of both state and private safety nets for the long-term.

— *Homeowner Mortgage Support Scheme (HMS)*: We welcome the principles underpinning HMS, but it has been administratively complex to bring in. There remains specific confusion around the details for comparable schemes, and it is imperative that all lenders that have not already done so sign up to the government's HMS scheme, or offer comparable support, to ensure all borrowers benefit from the same protection.

— *Mortgage Rescue Scheme*: We welcome the principle of the scheme, and believe it has the potential to help vulnerable households, but we are very disappointed that only six households have one through the scheme as at the end of May, and would like to see more done to address both the delays in the process and the lack of consumer awareness about the scheme.

— *Long term*: The inadequacies of the existing system, including the complete failure of mortgage payment protection insurance (which is only taken up by c.20% of borrowers, and generally not those who are the most vulnerable), point towards the need for a fundamental review of both state and private safety nets for the long term.

— *Advice*: Many of those struggling with their mortgage payments don't seek advice early enough, and can often struggle to access advice quickly because the advice sector is at capacity. We recommend that additional funding for early stage advice is provided, with a particular focus on increasing access among sub-prime homeowners.

8. *The impact of the credit crunch on access to mortgage finance and the terms on which such finance is offered for first time homebuyers.*

Shelter is acutely aware of the need to ensure that existing borrowers continue to have access to affordable lending, particularly as they come off fixed rates. However, we are not convinced that we should be rushing to get back to former levels of lending to first-time-buyers; it is vital that we move towards sustainable lending and borrowing, even if this means the mortgage market takes longer to get going.

— *Existing borrowers*: According to Which?, approximately 1.5 million borrowers are due to come off fixed rate mortgages by the end of 2010. In particular for those who are the most marginal borrowers—with the highest LTV ratios (and may even be in negative equity)—it is vital that there are sufficient affordable mortgages available that re-mortgaging doesn't push them over the edge and towards arrears and repossession.

— *First time buyers*: We need to ensure that we move towards sustainable lending over the longer term, including a more cautious approach to LTV and LTI. We must learn the lesson that the irresponsible lending of the past was a significant causal factor in the current crisis.

July 2009

Written evidence submitted by the Association of Mortgage Intermediaries

EXECUTIVE SUMMARY

1. The Association of Mortgage Intermediaries (AMI) is pleased to have this opportunity to contribute to the Treasury Committee inquiry on mortgage arrears and access to mortgage finance. We have specifically addressed the issue of access to mortgage finance, and are submitting AMI's recent publication—"Mortgage Market Fiscal Stimulus"—in support of our written evidence.

2. The current economic conditions are unquestionably making it harder for consumers to access mortgage finance, especially first-time buyers who have to find additional funds upfront, to get their first foot onto the property ladder. Tightening of lenders' loan-to-value (LTV) criteria, leading to greater requirements for deposits from consumers, have made the initial costs of purchasing a home more expensive. This has resulted in a significant fall in transaction levels and stagnation in the residential property market.

3. Home ownership as a percentage of the total housing stock, which rose and continued to increase during the 1980s, is now starting to decline, reaching levels of 68% in 2008. Gross mortgage lending has also declined. In Q1 2009 it was £33.3 billion—this is down from £75.2 billion in Q1 2008, and £83.9 billion in Q1 2007. In February this year lending was £9.9 billion, the lowest monthly lending figure since February 2001—the predictions for the remaining part of 2009 further reinforces this decline.

4. The withdrawal of foreign banks and the collapse of valuable "specialist" markets such as subprime, have left vulnerable consumers with exceptionally limited, or in some cases, no access to funding.

5. Additionally the number of mortgage products has fallen from 60,000 in 2007 to under 4000 in 2009, and the number of mortgage brokers is also set to halve over the same period.

6. However consumers need access to good independent mortgage advice today more than ever to ensure they obtain the product most suitable for their individual circumstances. Consumers who buy direct on a non-advised basis tend to purchase higher margin products than those who consulted an intermediary. If consumers are not to be penalized by paying more for a mortgage than they need to, lenders should be encouraged to respect consumers' desire for advice and work with the intermediary community.

7. AMI proposes a range of measures to address the current problems with access to mortgage finance. These include the re-invention of Mortgage Indemnity Guarantees as a means to encourage lenders to offer higher LTVs above 70%, as well as introduction of a Tax Free Savings account to help buyers obtain the capital required for a deposit on a home.

Introduction

8. The Association of Mortgage Intermediaries (AMI) is the trade association representing over 75% of UK mortgage intermediaries. Over 70% of all mortgage transactions are originated by the mortgage intermediary community, including 58% of regulated contracts. Historically 67% of all mortgage borrowers deal with an intermediary as part of completing a loan, with 82.5% of First Time Buyers (FTBs).

9. Intermediaries active in this market act on behalf of the consumer in selecting an appropriate lender and product, to meet the individual consumer's mortgage requirements.

10. However the confidence that once underpinned the mortgage sector has been gradually eroded over the past 18 months, caused by on-going decline in house prices and increasing negative media coverage.

11. Home ownership has started to decline, gross lending has declined, the collapse of "specialist" markets such as subprime and buy-to-let have left vulnerable consumers with exceptionally limited access to funding and the majority of potential first-time buyers have been consigned to renting.

12. What is abundantly clear is that the mortgage market has entered uncharted territory. With mortgage funding and consumer confidence reduced, the need for fiscal stimulus is only too apparent.

13. There is currently limited capital within banks and building societies. Higher LTV has a higher risk weighting, needing more capital, which limits lenders capacity to lend.

The Impact of the Credit Crunch on Access to Mortgage Finance and the Terms on which such Finance is offered for First Time Homebuyers

14. These are difficult times for the mortgage market. The credit crunch has had a severely negative impact on access to mortgage finance and the terms on which such finance is offered particularly for first time homebuyers.

15. The facts speak for themselves. Lending power has been consolidated from over 200 lenders to just six lenders of any scale, while access to funds has greatly diminished—gross lending is predicted by the Council of Mortgage Lenders (CML) this year to be at a low of £145 billion and net lending is less than £20 billion. Availability of products has also decreased—in 2007 there were over 60,000 products, this has now dropped to around less than 4000 products. Along with the limitation of mortgage products, there is less innovation in product design, almost no sub-prime lending and very little buy-to-let lending, meaning more consumers are being forced to rent as they simply cannot access the necessary mortgage finance.

16. While we understand policymakers unwillingness to ease up the sub-prime market, the longer we go on in this climate where people have significant indebtedness and no way to sort out costs, the more likely it is they will be driven to illegal lenders who are unregulated and uncontrolled. Alternative sources of lending are also limited—the secured loan market and access to flexible finance has fallen from £6 billion to £300 million per annum. We are seeing significant regulatory scrutiny in the secured loan market at the moment and whilst we fully appreciate there is the strong need to create a stable financial world, regulators need to be careful of damaging an important industry before we actually get there.

17. FTBs have been particularly badly hit by the credit crunch and the subsequent tightening of lending criteria. Banks have removed higher LTV products and require much higher deposits, meaning the majority of FTB's are simply priced out of the market. The Government initiative on new build has unfortunately failed to capture peoples' hearts and minds.

18. The home mover market is also vital to the return of a thriving mortgage market. It is now estimated that one-third of home owners have less than 30% equity in their property. While base rates and lenders Standard Variable Rates (SVR's) are low, this is not an immediate concern. However, when base rate rises and consumers are unable to re-mortgage—due to high LTV's, high SVR's and lack of available funding—consumers will find themselves on potentially unaffordable arrangements.

19. Whether a FTB, home mover or someone looking to remortgage, consumers need good independent advice today more than ever. However as a result of the credit crunch access to independent mortgage advice has diminished. In 2007 there were around 30,000 intermediaries—now there are around 18,000 although this may drop to 15,000 if the current conditions continue. For those intermediaries still in business they face a further challenge of lenders more actively marketing their direct sales, bypassing the intermediary channel altogether.

20. This is move which adversely affects consumers. There is an obvious demand from the consumer for high quality mortgage advice, especially during difficult economic times, and our members endeavour to fulfil their clients' needs against an ever-changing backdrop.

21. AMI's report "The Value of Mortgage Advice" shows clear evidence of the ways in which independent mortgage advice adds value to the outcomes achieved by the prospective borrower. These can be demonstrated in terms of cost savings (such as in product availability and rate payable) or in terms of the quality of advice given and the overall levels of satisfaction with the mortgage process. The positive effect of advice from the intermediary is reflected in the levels of satisfaction with the advice received by borrowers and in their willingness to recommend their adviser. Our research proves that those consumers who used an intermediary benefited from a lower mortgage payment by as much as £1,830 per year.

22. Consumers who buy direct tend to purchase higher margin products than those who consulted an intermediary, as FSA figures reveal. If consumers are not to be penalized by paying more for a mortgage than they need to, lenders should be encouraged to respect consumers' desire for advice and work with the intermediary community.

23. The bigger picture involves looking at how to carefully re-open the market. While politicians, FSA, HMT are talking the same talk, there is a disconnect between them in terms of actual outcomes. We therefore need to find a way through the current travails. The mortgage market needs more joined-up action from Treasury, Bank of England and FSA if we are to re-open the market. We can say this because we were the first trade body to publish proposals to fix the Credit Crunch—even before some in the market had woken up to the problem.

24. The market is not frozen because of a "demand" issue—consumers want houses and need loans. They are going to intermediaries who can't find the supply of lending. We need to give consumers back a well-supplied mortgage market which is fair and reasonable without being irrationally exuberant.

25. In particular we need to focus on helping First Time Buyers—and First Time Sellers—the people who are the life-blood of the mortgage market. AMI recently published a Financial Stimulus Plan, a copy of which is attached to this submission, designed to address the key issues in mortgage finance. It is a very good set of proposals, which in quieter political times would have made its own headlines.

26. A proposed measure which specifically addresses the current lending issues is the re-invention of Mortgage Indemnity Guarantees (MIG), a measure which we believe could encourage lenders to offer higher LTV's above 70%, thus assisting both the supply and demand within the mortgage market

27. Historically, Mortgage Indemnity Guarantees (MIGs) were single premium insurance policies designed to protect lenders against financial loss in the event a property was repossessed. Although the borrower would pay the MIG premium, it was essentially the lender that was protected. However it enabled borrowers to borrow higher Loan-to-Values (LTV), typically above 75%, and limit the potential liability for the lender.

28. Previous criticisms of MIGs focused on their cost and lack of consumer benefits. MIG's were generally expensive and carried high profit margins for lenders, subsequently consumers lost trust in the product and its benefit. AMI propose the re-engineering of MIG, as a benefit paid for by the borrower for the benefit of the borrower. It is possible that in the current climate few insurers may want to take on the risk of insuring MIG policies due to the high risk of default. However we would propose that the Government meets with insurers and ourselves, to test the idea and gauge industry response. If this proves insufficient, we would propose that the Government partially underwrites the policy in a secondary capacity, so lessening the risk to insurers. AMI itself has evidenced substantial interest from lenders in the return of a "new MIG". We propose Government examines the Canadian model which has proved highly successful.

29. Additionally we propose that the MIG should include a "no negative equity guarantee", which ensures that consumers will never be required to pay back more than their property is worth, if the property fell into negative equity.

30. If appropriately introduced, lenders will be able to offer higher LTV's supporting specifically the first-time buyer market, who typically have lower deposits and need more financial assistance. Perhaps more importantly this will also aid the home mover market, who may have built up equity in their property, and seen this fall along with the price of their home. Employment of MIG on higher loans would allow lenders to give this a lower capital rating thereby allowing a greater volume of lending to such consumers.

31. Another measure designed to address the finance issue for First Time Buyers is a scheme to help them obtain the capital required for a deposit on a home. As mentioned previously, one of the key evolutions within the mortgage market has been the removal of higher % LTV mortgages. Subsequently a greater need

for significant deposits of up to 25%—to take advantage of the best available interest rates—has emerged. Action is therefore required by Government to assist first-time buyers to meet the upfront costs associated with taking the first steps onto the housing ladder.

32. One way of achieving this could be through the introduction of a Tax Free Savings account, perhaps run by National Savings and Investments (NSI). Such a scheme would support buyers to obtain the capital required for a deposit on a home, and in turn encourage young adults to save over a longer period of time, with a view to buying a property in the future. A similar scheme also has the potential to be run by banks or building societies, who could offer consumers a guaranteed mortgage if they fulfilled certain saving requirements over a designated time period.

33. The scheme, which would benefit from tax exemption, should be based on the existing Individual Savings Account (ISA) structure, to ensure it is exempt from both income and capital gains tax. To encourage potential buyers to save as much as possible, the total annual ISA limit of £10,200 should be made available, it should also be possible for the account holder, or another person such as a relative or employer, to contribute to the account. The government would provide tax relief for those who use their savings plan as the deposit for a home. This would be relatively easy to monitor, and the tax relief could be added as a 20% addition to the value of the savings plan at such time when the property is purchased. Withdrawals must be used to fund the purchase of a home and the buyer must be required to live in that home for a set period

34. This would also make it more attractive to young people, many of whom don't understand the concept of tax relief on contributions. This understanding would develop, if assured the government would be adding 20% to their savings when their first home is purchased.

35. Such proposals would also have long term benefit amongst young people, rewarding a more sensible approach to home buying, rather than relying on high levels of borrowing. This in turn will have a wider impact on assisting to boost the housing market during a downturn.

July 2009

Written evidence submitted by the National Federation of Property Professionals (NFoPP)

Executive Summary

1. The National Federation of Property Professionals (NFoPP) welcomes the Treasury Select Committee short inquiry into mortgage arrears and access to mortgage finance. Our evidence focuses on the availability of lending and the crucial first time buyer market, and we argue:

- While there are encouraging signs of a return to demand in the housing market, these are still well below levels when the market was at its peak. Moreover, there are still significant consumer concerns about lending and the level of approvals. NFoPP research conducted among 1,860 respondents in June 2009 shows:
  - nearly one quarter felt that the lack of available mortgages was preventing them from purchasing property at the moment; and
  - a majority (57.6%) felt that if the banks were to start lending again it would make a "big difference" to the property market.
- More assistance for first time buyers is needed. Government and lenders must do more to encourage first time buyers on to the property ladder in order to reverse the current downturn in the market. The NFoPP calls on the Government to review stamp duty. In our view the Government should consider abolishing the measure outright, or introduce a more flexible alternative.

Introduction

2. The NFoPP has a combined membership of just under 14,000 practitioners. It is made up of different member organisations, including the National Association of Estate Agents (NAEA) and the Association of Residential Letting Agents (ARLA), who are the UK's leading professional bodies in the sales and letting sectors of the property market. Our over-arching aim is to promote the highest standards of professionalism and integrity among those working within the property industry, and to encourage members of the public to proactively seek out our members when involved in any kind of property transaction.

3. This submission incorporates the views of the National Association of Estate Agents (NAEA) and the Association of Residential Letting Agents (ARLA), and focuses primarily on the final issue raised by the Committee: *the impact of the credit crunch on access to mortgage finance and the terms on which such finance is offered for first time buyers.*

4. The NFoPP welcomes the opportunity to provide comment to the Committee on these issues, and would be very willing to share our understanding by giving oral evidence to the Select Committee.

Access to Mortgage Finance

5. Low interest rates will increase confidence in the market but will not increase mortgage approvals per se. Bringing buoyancy back to the market lies not only with low interest rates but crucially also in new lending. The NAEA has called on all the major lenders to commit to passing the interest rate reductions onto the consumer.

6. The recent interest rate reductions, coupled with the mortgage assistance measures announced, act as a firm commitment to restoring health to the market. However, as we argue below, government and lenders must do more to encourage first time buyers on to the property ladder in order to reverse the current downturn in the market.

7. Signs from the high street indicate that confidence is indeed returning. Indicators have been promising for the last couple of months on the demand side. Our agents report an upturn in the number of people registering for property, although this is still much lower than when the market was at its peak. The latest monthly market survey of the National Association of Estate Agents found that the average branch had 299 house hunters on its books in May —up from 265 the previous month and 247 in May 2008. The average branch had 69 properties on its books. Moreover for the second month running estate agents also reported a more successful selling period. The average branch sold 10 properties, a 30% increase on the same time last year and double that sold on average in August 2008.

8. There are indications that property investors in the buy-to-let market are also slowly being attracted back into the sector. The ARLA Members' Survey of the Private Rented Sector (PRS) for the second quarter of 2009, drawn from 730 offices across the UK, indicated that nearly twice as many ARLA members reported that landlords are buying more properties. ARLA members also reported that the interest rate cuts of late last year are beginning to bear fruit for the PRS: half (50%) say that they think the cuts are tempting investor landlords back to the market because of the minimal interest to savings rates. The recent rise in buy-to let activity could be as a result of increased average weighted rental returns too: houses are up from 4.8% to 5.1%. Flats are also up from 4.9% to 5.0%. Unsurprisingly, rental returns for houses in prime central London were far lower than the national average at 4.7% but returns for flats remained consistent across the UK.

9. However, for many this encouraging upturn in demand could ultimately turn out to be unrequited. Savills Private Finance found that 30% of mortgage applications are currently being turned down against 20% in 2008. NAEA is investigating this further and will provide more evidence in due course, but from one agent in the south-east we note his concern that 45 property sales on his books are waiting for confirmation due to delays in mortgage underwriting.

10. Individual experiences are reflected in detailed NFoPP consumer research. In a survey conducted among 1,860 respondents in June 2009, we found that:

- nearly one quarter felt that the lack of available mortgages was preventing them from purchasing property at the moment; and
- a majority (57.6%) felt that if the banks were to start lending again it would make a "big difference" to the property market.

11. Ultimately any issues around mortgage approval delays will be of concern. Mortgage underwriting involves accepting the financial risk with a mortgage application. By necessity it involves assessing the likely performance of an applicant in the light of the experience of a similar cohort of applicants in the past and the value of the property being offered. Evidence from our members on delays in this process suggests that high street confidence is not shared by actuaries, giving an insight into their actual appetite for risk.

12. We suggest that the Committee questions in detail the dynamics of mortgage approvals to give its assessment of the current situation.

Support for First Buyers

13. First time buyers are central to a properly functioning housing market but the lack of mortgage finance is particularly impacting on this group. High loan-to-value mortgages are being withdrawn and the consequent rise in the amount being demanded in deposit means it is becoming increasingly difficult to gain a foothold on the housing ladder.

14. The Government has provided temporary relief by the suspension of stamp duty for homes up to the value of £175,000. However, a long term solution is needed by the end of the year. This is because stamp duty acts to distort the housing market. The way in which the tax is levied, the so-called "slab" structure, leads to a sharp rise in the amount of duty payable as the price of a property moves from one band to the next. If a home moves beyond £250,000, for example, the rate of duty jumps from just 1% to 3%. This has led to distortions to the market with figures suggesting that a significant decline has taken place in the number of properties sold at prices just above the thresholds, rather than there being a smooth distribution of house prices as there should be in a well functioning market. Moreover, it is iniquitous in different parts of the country. Regional house price differences lead to a geographical inequality in terms of who bears the burden of the duty, and falls more heavily on the south of England where prices are higher.

15. Stamp duty places a disproportionately heavy burden on first time buyers, which is of particular importance in the current climate where new buyers in the market are finding it difficult to gain a foothold on the housing ladder. The temporary increase in the threshold to £175,000 has improved this situation recently with 74% of first time buyers not paying the duty in December 2008, according to figures from the Council of Mortgage Lenders. The research shows, however, that without this increase in the threshold only 40% of first-time buyers would have been exempt. This highlights the need for an extension to the temporary nil-rate threshold.

16. First time buyers are more likely to be near their credit limit, particularly in the current lending environment. This means they are less able to extend their borrowing to cover the additional cost of the duty. Moreover, stamp duty is not index-linked to rise with inflation. This has meant that duty has been paid by increasing numbers of first time buyers.

17. The NFoPP calls on the Government to take decisive action on stamp duty, which effectively acts as a tax on aspiration. In our view the Government should consider a viable long-term solution by either abolishing the measure outright, or in the alternative:

— suspend stamp duty for the duration of the housing downturn, with a commitment to review the existing system;

— reform the system moving from the distortion of the "slab" system to a more progressive "slice" system or system that, like other taxes, is index-linked to inflation, or

— raise the starting threshold for this tax well above the current £175,000 limit to ensure that as much is done as possible to assist first time buyers into the market.

18. In our 2009 Budget submission the NFoPP called on the Government to actively encourage lenders to provide high loan-to-value mortgages to enable first time buyers to enter the market. The NFoPP recognises that high loan-to-value mortgages carry additional risk for the lender, so calls on the Government to actively promote the use by lenders of Mortgage Indemnity Guarantees (MIGs) or Mortgage Insurance on properties with a high loan-to-value ratio.

19. In the current economic climate, with historically low rates of saving and high deposits being demanded as part of mortgage lending criteria, the Government should do all it can to support access to homeownership for first time buyers. The NFoPP calls on the Government to work closely with lenders to ensure that lending criteria are appropriate and that sufficient lending is available to those who are looking to buy a house for the first time.

2 July 2009

Written evidence submitted by Volterra Consulting

1. Executive Summary

1.1 This evidence provides forecasts regarding the level of arrears and possessions in the UK mortgage market. These are based on a simple, intuitive model of arrears and an economic scenario adapted from consensus forecasts. The model suggests a peak of arrears in mid 2010 of approximately 350,000 mortgages. Estimates for the number of repossessions are 67,000 in 2009, followed by 90,000 in 2010.

1.2 We acknowledge the inherent uncertainty in making forecasts of this nature. The economy may evolve differently to the economic scenario under which these predictions are made. Also the estimated relationships that are reflected in the model may shift and change through time. Nevertheless it is useful to have a considered, evidenced-based view as a starting point. The purpose in submitting this evidence is to provide such a starting point.

2. Background and Aim of this Paper

2.1 This evidence is submitted by Matt Salisbury, Associate Director, Volterra Consulting. At Volterra Consulting we regularly produce analysis and forecasts of defaults, arrears and possessions in the mortgage market for large banks and building societies.

2.2 Arrears rates and repossessions in the UK mortgage market vary considerably with movements in the economy. During the last recession the number of mortgages six months or more in arrears rose from 80,000 in 1989 to a peak of 352,000 in 1992, with the movement in the number taken into possession moving from 15,800 in 1989 to 75,000 in 1991.

2.3 Even at the time of writing, when we have been in recession for over a year, forecasting the levels of mortgage arrears that will result from the current recession is an exercise fraught with uncertainty. Although we do have useful data on arrears from the last recession, changes in the mortgage market over time and the different nature of the current recession to that of the early 1990s mean great care must be taken in making forecasts.

2.4 This paper presents a view of mortgage arrears through the current recession. This view is driven by an econometric model based on statistical performance and informed by intuitive reasoning.

3. Model Outputs

3.1 The model used is based on three core elements:

— Equity—an estimate of the proportion of housing value that is owned by householders.

— Affordability—an estimate of the general level of the cost of servicing mortgage debt as a proportion of income.

— Unemployment

Additionally, a factor measuring the increase in unsecured debt levels is also included.

3.2 The aim in producing this model was to build a relatively simple model based on intuitive factors. Although many other factors were considered, with some adding to the statistical power of the model, all were rejected either on statistical or intuitive grounds. The benefits of a relatively simple and intuitive model are that it is more likely to be robust and allows us to more carefully consider the model outputs in the light of the current recession.

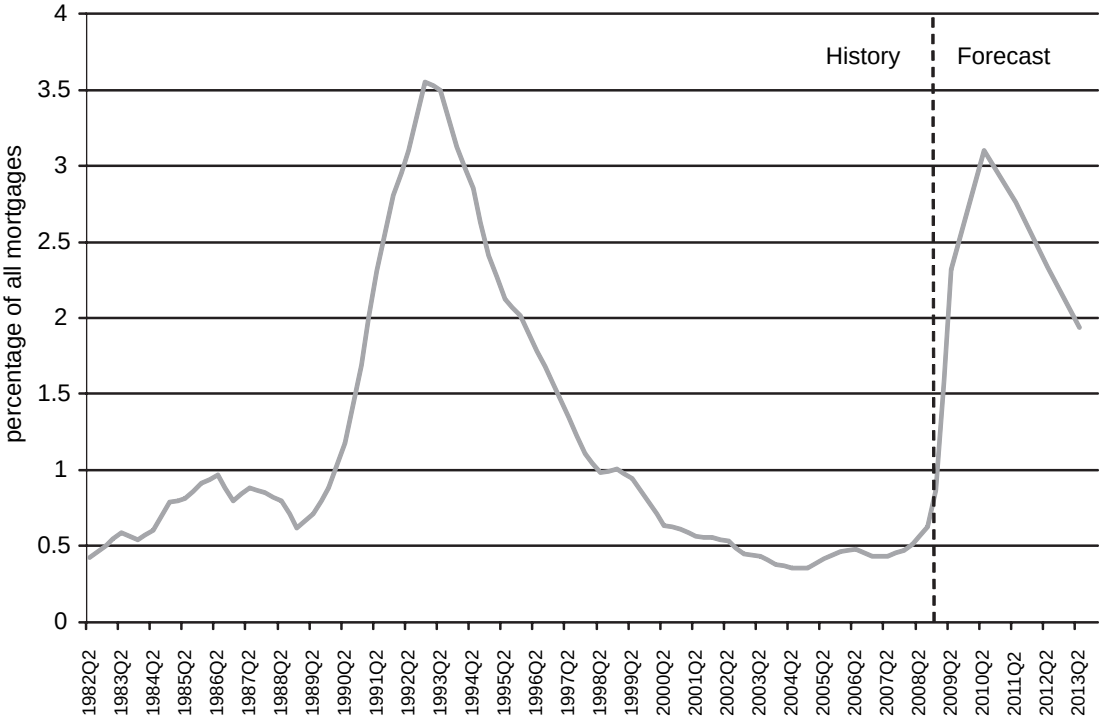
3.3 Despite keeping the model as simple as possible and using a minimal number of inputs, the model explains the fluctuations in the past data very well, with all factors contributing to the explanatory power of the model in an intuitive manner. The model also passes standard diagnostic statistical tests.

3.4 The economic scenario that we input into our model to produce a forecast were based around the average of independent forecasts produced by the treasury, June 2009 edition (http://www.hm-treasury.gov.uk/d/200906forecomp.pdf) where possible. This was the case for unemployment, house prices and interest rates. Additionally forecasts were required around the growth in lending (mortgage and unsecured), which we assumed would fall in the short term before returning to more normal levels in the medium term.

3.5 The results are shown in the figure below, with the peak in mortgage arrears occurring in mid 2010 at around 3% of all mortgages. With the number of mortgages standing at approximately 11.5 million, this implies a number just short of 350,000 mortgages six months or more in arrears.

Figure 1

PERCENTAGE OF ALL MORTGAGES SIX MONTHS OR MORE IN ARREARS



Source: Council of Mortgage Lenders, Volterra Projections

3.6 In the long run the ratio of the number of properties taken into possession in a period to the six months plus arrears stock has been around a quarter. In 2007 and 2008 this ratio moved above the long run average. It is unlikely that the pass through from arrears to possession will remain as high, particularly given stated government policy and the severe forced sale discounts that lenders now face should they elect to crystallise their loss on delinquent accounts in the current climate. Assuming that the pass through from

arrears to repossession over the course of the recession is at the long run average level, the model implies and estimated 67,000 repossessions in 2009 and 90,000 in 2010. The Council of Mortgage Lenders most recent forecast for the number of repossessions in 2009 is 65,000.

3.7 The pass through from arrears to possession through the current recession may take on a pattern unlike any shown in the past data, however. Depending upon the state of the housing market, lenders may choose to strategically hold back from repossession even where they know that the borrower will not be able to pay off the loan. This would be in order to re-coup more of the asset value when the market does recover. This may happen to a greater extent than in the past due to the sheer size of the falls in house prices in recent times. Obviously there is also the government role in holding back repossessions. The effects of holding back repossessions may be to increase the stock of arrears and reduce possessions, meaning banks would carry larger impairment provision funds for longer through the current recession than has been seen in the past.

3.8 These numbers are based on a scenario where unemployment does not approach the levels experienced in the last recession and peaks in 2010. A case worth considering is that where unemployment peaks larger and later (unemployment has peaked some time after the largest output falls in post-war UK recessions). If unemployment hits levels around those of the last recession and the peak occurs in 2011, the level of arrears is estimated at 440,000. Again assuming the same pass through to repossession, the associated number of repossessions is 109,000.

3.9 As with any model, there is a considerable degree of uncertainty regarding how accurate predictions will be through time. Econometric models are prone to breaking down as unique turns of events lead to outcomes playing out differently to anything which could have previously been envisaged. Nevertheless it is necessary to have a considered and preferably evidence based view from which to begin to consider the issue. The purpose in producing these model results is to provide such a starting point.

July 2009

Written evidence submitted by Dr Ronald R Heywood BA(Hons)(Law) MA LLD PhD and Dr William M Ramsden LLB (Hons), LLM (ALP), MA (C-L), PhD (C-L), LLD, FRSA, ACIArb

1. The Respondents welcomes this opportunity to submit evidence to the Treasury Select Committee concerning mortgage and secured loan arrears.

2. Both Respondents have worked and practised in the area of housing Law Advice, Assistance, Advocacy, representation and training for many years based in the North West of England. They have between them previously worked within the Citizens Advice Service, Shelter, the Law Centre movement and private practice. That work has extended to frequent representation under housing Duty Possession days at local County Court. Dr Ramsden is a Barrister.

3. The background is such that during 2008, mortgage and secured loan repossessions claims rose sharply, which was highlighted by the number of cases coming before the local Courts.

4. As the credit crunch took effect it was clear that unemployment began to rise with the economic downturn, there is evidence of arrears problems extending across a wider range of the population.

5. During 2009, arrears continued to rise significantly and repossessions also continued to rise strongly But the number of possession claims (ie cases being taken to court) fell significantly. This positive evidence suggests that very low interest rates and the government measures introduced in late 2008 and early 2009 have had the overall effect of making court action less likely, though people continue to lose their homes.

6. We are going to address certain legal powers of the Courts and also the difficulties this poses in relation to default charges imposed by Lenders.

The Powers of the Court to Deal with Mortgage Arrears

7. Over the last 35 years, the percentage of UK homes which are owner-occupied has risen from just under 50% to over 70%. The expansion of home ownership and the current recession means that more people could be exposed to the risks of arrears and repossession.

8. There has been a protocol for mortgage possession cases introduced under the Civil Procedure Rules. However, our experience has shown that it is often not complied with.

9. The legislation which protects home owners with mortgage arrears from losing their home, however, has not been updated since the 1970s.[80] There are also a number of anomalies in the current legislation relating to first and second charge mortgages.

10. Essentially the Acts gives the Court power to adjourn, stay, suspend or postpone the date for giving up possession if it is likely that the arrears of instalments and interest can be paid within a reasonable period of time.[81] Since a Court of Appeal decision[82] there is a general presumption that the starting point for the reasonable period of time is the remaining period of the mortgage.

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[80] Administration of Justice Acts 1970–1973.
[81] S 36 Administration of Justice Act 1970 and s 8 Administration of Justice Act 1973.
[82] Cheltenham and Gloucester Building Society v Norgan [1996] 1 WLR 343; [1996] 1 All ER 449.

11. Frequently we have been able to either negotiation or obtain suspended orders from the Court to aloe Borrowers to stay in their homes for a modest sum in relation to the arrears.[83] However, in order for this to be able to be exercised the Borrower must first be able to pay the monthly instalment and if not then this power is not available.

12. There are, however, examples where this is not the only power (but in many instances it is). If the amount borrowed is under the financial limit for a regulated agreement under the Consumer Credit Act 1974 then the borrower can apply for a time order which allows the court to reopen the whole agreement, and reduce the interest on the loan to allow the borrower to pay less than the contractual monthly instalment. Unfortunately with most first mortgage situations this is not available as they are clearly well above the limit for the agreement to be a regulated agreement.

13. One difficulty that Borrowers frequent face is that the Lenders effectively thwart and curtain the benefit of the order made by the Court and effectively prevent the Norgan principle[84] applying. This is the imposition of default charges. There is a particular problem in relation to this in the subprime market as the monthly default charges can range between £30 to £115.00.

14. To take some examples. Mrs A fell into arrears of £1,600. The agreement was not a regulated agreement. The Court made an order for possession and suspended provided Mrs. A paid the current monthly instalment together with £25.00 per month towards the arrears. However, notwithstanding the Order the Lender applied default charges of £50.00 every month resulting in an increase in her indebtedness of £25.00 per month even though she was complying with the order. The effect of this would mean that she would never pay off the balance if the Court order was followed!

15. In another example Mr B had fallen into arrears of £2500. Again this was not a regulated agreement. The court again made a suspended order proving for payment of the current monthly instalment together with £50.00 per month. However, once again default charges were applied on this occasion of £115.00 per month meaning that the debt increased by $65.00 per month. This meant after 12 months of making the payments without fail the arrears, according to his Lender had increased to £3,280!

Default charges and other charges

16. These are only two instances of default charges but many cases come before the Courts that have been dealt by us where there are default charges ranging between the two extreme example that have given. The net result means that the imposition of such chares undermines totally the legislation and ultimately Parliament and the orders made by the Court.

17. However, there are other default charges besides those encountered as the monthly charge. One example that we have encountered in cases already in litigation is that certain Lenders require the payment of a fee typically in the region of £50–£60 before they will discuss the matter with any type of adviser.

18. This is even though they have taken the initiative and issued the proceedings already. Frequently persons who are facing problems with mortgages have often found themselves on vastly reduced incomes due to the economic downturn or indeed on fixed incomes due to having to claim state benefits. For them or organisations representing their interests to be required to make such payments before any negotiations take place is quite frankly scandalous.

19. It now seems to be the case that many Lenders are not negotiating directly with the borrower, unless the Borrower sees one of their debt counsellors. Home visits are usually arranged for this and typically these visits cost £100.00 or more.

20. This has been the case even when the Borrower or their representative such as us have been in active negotiations with the Lender. There have been Lenders, who have charged £35.00 per telephone call and letters and some of these have made numerous calls on one day!
The way some of the subprime Lenders deal with collections is bordering on or is indeed harassment of a debtor.[85]

21. Mr. C had a mortgage where arrears had arisen of just over 1 month's payment. He managed to maintain the monthly payments so the arrears did not increase. He would receive regular phone calls from the Lender concerned and on some occasions there were 6 calls in one day. One occasion a payment had been made then there were further calls from the Lender the following working days putting pressure on him to make more payments which he could not afford.

22. The Government's white paper, "A Better Deal for Consumers: Delivering Real Help Now and Change for the Future" published yesterday is therefore to be welcomed if default charges are addressed fully.

[83] Such as £25.00 off the arrears per month.
[84] *Ibid.*
[85] Section 40 Administration of Justice Act 1970.

Sale and Rent Back

23. We have been involved in a number of these cases and this type of case often gives cause for concern. In effect, what occurs is that it allows the borrower to sell their home to a private landlord at a discount and allow them to remain there paying rent as a tenant.

24. Often individuals who are in a financially comprised position are often found to be very vulnerable indeed, and it is our belief that not only does the borrower sell their home for much less than they are worth, but the tenancy granted is frequently an assured shorthold tenancy of a limited period.

25. In effect, the tenancy offers little security of tenure. Moreover the rent is often well above the typical market rent for a property given is size and location. If rent arrears do arise then the landlord is extremely quick in taking steps to recover possession leasing to homelessness, which has happened in a number of cases.

26. What attracts many individuals is the entitlement to Housing Benefit. However, it is far from straightforward as to whether the individual will receive this given the very specific rules where the person has previously owned a property. There have been cases in our experienced where Local Authorities have refused to pay,

Tenants of Landlords

27. This has become an increasing problem and arises in two ways. However, the primary reason is the Landlord has not paid the mortgage and often the Lender does not know that there are tenants in the property.

28. If the mortgage or loan was taken out whilst the tenancy was in existence then generally the tenant's right of occupation will override those of the lender on the basis that the tenant's right of occupation overrides those of the Lender.[86]

29. However, the most frequent situation is where the tenancy came into existence after the mortgage and the lender has not agreed to the letting. In most instances this means that the tenant has little protection even though they are the interested party and can only obtain a suspension of an order or warrant of possession for a short period of time. There have been some examples. However, where the court has been prepared to give more forbearance, especially where the tenants were in a position to pay all the arrear and make the mortgage payments.[87]

Submissions

30. We support the decisive and coordinated approach which the government has taken to put in place a mortgage safety net to help people stay in their homes. However, people are still losing their homes, and many are still falling through the gaps.

31. Our evidence suggests that court procedures and regulatory rules need to be tightened up.

32. It is also necessary to reconsider and implement improvement in the statutory regulation of secured lending, while retaining and extending current vital protections for consumers under the Consumer Credit Act, and to ensure responsible lending.

33. The law on first mortgages has remained the same since 1970, and it is our view that court should have the same powers to protect homeowners, whether or not the loan is a first or a subsequent charge and should be the same as those contained in the Consumer Credit Act 1974 (as amended) which of course include giving the court the power to make Time Orders on all mortgages or secured loans. This would allow the borrower to ask the court to reopen all mortgage agreements and reduce the interest rate for temporary periods of financial difficulty to allow the borrower to pay below the contractual amount.
Extension of the Unfair Credit Transaction test in sections 140A and B of the Consumer Credit Act 1974 to all mortgages and secured loans to ensure that the court can look into unfair treatment by the lender and take this into account in their decision.

34. It is essential that the debt management scheme provisions of the Tribunals Courts, and Enforcement Act 2007, are fully implemented which would enable debtors to make affordable repayments to their creditors, which are binding and would restrict creditors' rights to enforcement action.

35. There is clear evidence of unfair default charges being levied, and we believe regulators should consider firmer action against companies, which act in this way. We believe that firms who make these charges should be named and shamed. Firms within groups of banks with a large public interest shareholding should be expected to lead the way. In addition, both regulators should rule decisively that no customer in debt should be charged for having a conversation or correspondence with a company representative with a view to coming to an affordable payment arrangement which avoids the customer losing their home.

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[86] Para 2, Schedule 1 to the Land Registration Act 2002.
[87] Abbey National plc v Yusuf (1993) June 1993 Legal Action 12.

Written evidence submitted by the Money Advice Trust

Executive Summary

1. The Money Advice Trust (MAT) welcomes this timely inquiry into mortgage arrears and consumer access to mortgage finance. In our response we draw the Committee's attention to the following key findings and recommendations:

- The majority of money advice clients whose homes are repossessed move to the private rented sector and post-repossession continue to need: debt advice, money guidance and emotional support.
- Money advisers report that since the introduction of the mortgage arrears pre-action protocol:
  - there has been an overall improvement in mainstream first charge lenders' arrears management practices; but
  - this improvement has not been as evident within the sub-sector offering secured loans.
- We welcome the Government's response to concerns around the operation of sale-and-rent-back schemes, but urge that consideration is given to the introduction of powers to assist those consumers with existing sale-and-rent-back deals.
- Whilst acknowledging the recent improvements to support for mortgage interest, we highlight concerns over holes in this safety net for low-income mortgage borrowers and urge a full review of current provision with the aim of arriving at a more fully accessible safety net for sustainable home ownership.
- We welcome the recent Government mortgage rescue and homeowner mortgage support initiatives and make recommendations for improvements to these scheme.

Introduction

2. MAT is a charity formed in 1991 to increase the quality and availability of free, independent money advice in the UK.

3. We work in partnership with government, the private sector and the UK's leading money advice agencies to:

- support individuals and businesses with unmanageable debt (MAT runs National Debtline and Business Debtline);
- increase the availability of free money advice to people with debt problems;
- improve the quality of money advice; and
- improve the efficiency and effectiveness of its delivery.

4. We welcome the Treasury Committee's inquiry into mortgage arrears and access to mortgage finance. This is a very timely investigation as the effects of the recession are being felt with increasing intensity by clients of the free, independent advice sector. We hope that the information we have collated below will be of assistance to you in your investigation.

5. AdviceUK, Citizens Advice, MAT, and Shelter are in the process of researching the effect of various government and industry mortgage arrears initiatives. Findings from the first round of surveys were published on 15 May. This first piece of work reported on a survey conducted amongst nearly 400 advisers working for Citizens Advice Bureaux, National Debtline and Business Debtline, Shelter and independent advice centres and examined at their experiences of helping borrowers with mortgage and secured loan arrears.

6. A companion survey was conducted by National Debtline advisers and reported on 500 clients with mortgage arrears who were surveyed throughout April 2009.

7. Key findings from both surveys are highlighted in our response below.

The current number of homeowners in mortgage arrears and forecasts for the trend in mortgage arrears over the medium-term

8. We would draw the Committee's attention to the CML's revised forecast for repossessions in 2009 which is available via the link below.

http://www.infohub.moneyadvicetrust.org/resource.asp?r_id=409

The number and characteristics of homeowners who have had their properties repossessed, the number in the process of having their homes repossessed, as well as forecasts for the trend in repossession levels over the medium-term

9. We believe that with the recent focus on avoiding repossession, the plight of the newly repossessed has been somewhat overlooked, and we therefore welcome its inclusion in the terms of reference of the Committee's investigations. The Committee is no doubt already aware that there is a piece of research work underway, which will report to the Home Finance Forum and is supported by CLG, CML and Shelter.

Several lenders will also be assisting the work. The research is aimed at improving understanding of what happens to households that are repossessed and will provide information regarding the household characteristics and other demographic features of households being repossessed.

10. The advice sector's joint research on the effect of the government and industry mortgage arrears initiatives (referred to in the Introduction), looked at what happens to money advice clients whose homes are repossessed. It was found that the majority move to the private rented sector and need support with their money problems. Advisers were asked to report on the three most likely outcomes for their clients following repossession:

— 80% reported that their clients move into the private rented sector;

— 51% report that their clients apply to the local authority and are accepted as homeless; and

— 46% report that they move in with family and friends.

11. Advisers were asked about specific help that their clients may need following repossession and were required to select up to three responses. They reported as follows:

— 82% of clients needed debt advice;

— 51% needed financial capability advice or money guidance; and

— 42% needed emotional support.

The treatment by, and the approaches taken, by mortgage lenders towards homeowners in arrears and/or at risk of repossession, including issues relating to the treatment of homeowners by financial institutions specialising in mortgage lending to sub-prime borrowers

12. We would draw the Committee's attention to the December 2007 Citizens Advice report "*Set up to fail.*" This valuable report has in many ways opened up the debate about differences in behaviour amongst the various sections of the lending industry. Its findings continue to mirror the experience of National Debtline clients.

http://www.citizensadvice.org.uk/index/campaigns/policy_campaign_publications/evidence_reports/er_consumerandebt/set_up_to_fail-2

13. The advice sector joint research on the effect of the government and industry mortgage arrears initiatives (referred to in the Introduction) produced the following key findings:

— Advisers reported overall improvements in the arrears management practices of mainstream lenders since the introduction of the pre-action protocol (although there were variances within sub-sectors of the lending industry).

— Advisers reported that the mortgage pre-action protocol had impacted positively on judges' practices in court.

14. Key findings of the National Debtline client survey (a companion to the sector-wide adviser attitudinal survey) highlighted the differences between the policies and procedures followed by first mortgage lenders and those offering secured loans. These included:

— 59% of those in mortgage arrears said their lender offered them affordable help when told about their repayment problems; whereas only

— 38% of those in arrears with their secured loan said their lender offered them help when told about their repayment problems.

Also:

— 57% of those in mortgage arrears were satisfied with the way they were treated by their mortgage lender; whereas only

— 34% of those in arrears with their secured loan were satisfied with the way they were treated by their mortgage lender.

The full report can be found by following the link below.

http://www.infohub.moneyadvicetrust.org/resource.asp?pub_id = 204&rPath = pub&r_id = 381

15. As part of this piece of work, a county court duty desk survey is currently underway. Also a follow-up adviser attitudinal survey and a further NDL client survey will be conducted later in the year. These will be reported on together.

Adherence to, and the effectiveness of, Financial Services Authority (FSA) rules and guidance for mortgage lenders on repossession policy and treatment of consumers in arrears as well as the FSA's regulatory approach in this area

16. We welcome the recent FSA action against firms for poor mortgage arrears handling. The full FSA report can be found by following the link below.

http://www.fsa.gov.uk/pages/Library/Communication/PR/2009/080.shtml

17. However, we still have concerns that there is a worrying difference in attitude between mainstream first charge lenders and sub-prime lenders. Also, the FSA MCOB rules do not apply to secured loans that come under the Consumer Credit Act 1974. As the research referred to above indicates, there is a marked difference between consumers' experience of secured loan lenders as opposed to first charge lenders.

Adherence to, and the effectiveness of, codes of conduct, protocols and statements of good practice issued by industry bodies in this area

18. We welcome the CML good practice guidance contained within the "Industry guidance on arrears and possessions to help lenders comply with MCOB 13 and TCF principles". This can be found by following the link below.

http://www.cml.org.uk/cml/policy/issues/1629

19. We also welcome the FLA "Good practice guidelines for second charge mortgages". This can be found by following the link below.

http://www.fla.org.uk/fla/consumerfinance/GuidelinesforSecondChargeMortgageLenders.riv

20. We are not aware of any research being carried out into the effectiveness of these statements of good practice. We would welcome such a development.

21. As we have stated above, the advice sector is carrying out joint research on the effect of the Government and industry mortgage arrears initiatives. This includes research into the effectiveness of the mortgage pre-action protocol.

Issues of concern around the operation of sale and lease-back schemes

22. We are very pleased to see the speedy response by Government to the concerns highlighted in the OFT Market Study on sale and rent back schemes. We welcome the FSA interim regulatory scheme from 1 July 2009. This allows consumers to make complaints to the Financial Ombudsman Service regarding firms that have interim authorisation from the FSA.

23. However, we remain concerned that these rules will not be able to operate retrospectively, so consumers with existing sale-and—rent-back deals have no recourse. Whilst we appreciate that firms who fail to register with the FSA from 1 August 2009, will be committing a criminal offence if they continue to operate, again, there will be no recourse for individual consumers in this situation.

The success of those Government schemes in existence before the financial crisis to support homeowners facing difficulties with mortgage payments and/or at risk of repossession, as well as the effectiveness of initiatives introduced since the financial crisis began; and

24. We are having difficulty identifying Government schemes that supported homeowners in difficulty with mortgage arrears prior to the downturn, other than Support for Mortgage Interest (SMI).[88]

SMI

25. The introduction of a 39-week waiting period for those on qualifying means-tested benefits was, in our opinion, a backward step and resulted in hardship, stress and in some cases homelessness for some of the most vulnerable members of our society. We therefore welcomed the improvements to SMI introduced earlier this year, including the reduction length of the waiting period.

26. The impact of the current configuration of the scheme remains to be determined in relation to homeowners claiming benefits who may not have sufficient savings to cover the first 13 weeks' mortgage payments or those with larger mortgages. Also, the retention of the standard interest rate used to work out interest payments could continue to disadvantage those who pay higher than average interest rates on their mortgage (typically sub-prime). However, the temporary freeze on the standard interest rate at 6.08% will go some way to mitigating this problem.

27. We would point out however, that in the advice sector, joint research on the effect of the government and industry mortgage arrears initiatives referred to above, indicates that the impact of these changes appears to be mixed. In the adviser attitudinal survey:

— 46% of advisers reported no real difference in lenders' practice following the changes to SMI; yet

— 30% report that lenders are less likely to proceed with possession action through the courts following the changes.

28. We urge a full review of SMI to consider how best a more fully accessible safety net for sustainable home ownership could be offered. The review could involve exploring the scope for introducing something along the lines of a "mortgage credit", which in line with existing credits could potentially be available to anyone with reduced income on a taper basis and not just those who fell below a fixed threshold. This would mirror what already happens to tenants who receive housing benefit. We would also support a modification to ensure that SMI covers the actual interest paid rather than a standard rate of interest for all.

[88] Previously known as Income Support for Mortgage Interest.

29. In our view, it is too early in the day to make an accurate assessment of the impact of the Homeowner Mortgage Support (HMS) scheme and the Mortgage Rescue Scheme (MRS), and we would therefore limit our comments to the following:

MRS

30. NDL advisers were reporting that the bar on those with negative equity was a significant barrier to scheme entry. We therefore welcome the change that has now been made to allow those with negative equity to enter the scheme.

31. The MRS is a long and complex process. We welcome the recently announced plans to set up a new central team to fast-track urgent home repossession cases and strongly recommend that further consideration is given to the introduction of greater transparency and a more streamlined application process.

HMS

32. Although the numbers of those entering HMS is currently very low, we feel that the lead-up to delivery of this initiative has stirred up debate amongst lenders over issues of forbearance and that this has been extremely beneficial. We have evidence of lenders who, although not signed up to HMS, are offering forbearance schemes that were not in place before. We strongly recommend that the success of HMS should be viewed in the widest possible sense to take into account these wider spin-offs.

33. Generally, there continue to be problems in encouraging borrowers to take advice sooner rather than later. There is still a perception amongst a large number of borrowers that mortgage arrears inevitably lead to repossession, and that this may be delayed if they keep quiet and stay out of the way of the lender. There is a need for a programme of high profile advertising (including in broadcast media) to highlight the importance of-contacting lenders at the earliest opportunity; seeking good-quality, free, independent money advice at the earliest opportunity. Wider promotion of the various initiatives available to help borrowers in financial difficulty is also needed.

The impact of the credit crunch on access to mortgage finance and the terms on which such finance is offered for first time homebuyers.

34. This is not an area we are able to comment upon. We would refer the Committee to the FSA quarterly statistics on mortgage lending for more information.

http://www.fsa.gov.uk/pages/Doing/Regulated/Returns/IRR/statistics/index.shtml

July 2009

Written evidence submitted by the Royal Bank of Scotland

1. Summary

1.1 RBS arrears and repossession rates compare favourably to industry averages due to our focus on responsible lending and the fact that we treat repossession very much as a last resort.

1.2 Many of our customers are currently benefiting from lower interest rates making it easier for customers to sustain their mortgage repayments. However, pressures on household incomes caused by a continued increase in unemployment levels will increase the number of homeowners in arrears.

1.3 We want to do all we can to support our customers through these challenging times. As a result last December RBS pledged not to initiate repossession proceedings for a full six months after a customer first falls into arrears. This is double the amount of time recommended by the Government but we felt it was important to give our customers some breathing space during what is a very worrying time. No other high street lender has pledged to do the same, so far.

1.4 We also feel it is very important that customers in this situation are given the opportunity to seek advice from independent money advice organisations before any steps are taken. This pledge will remain in place until at least the end of 2009.

1.5 We would encourage our customers to come to us as soon as possible to talk about their financial problems. This is essential so that we can work together to find a solution that is right for them. Our objective is to support the customers to stay in their homes—it is not in our interests to repossess unless we absolutely have to and we only do it where all other options have been exhausted.

1.6 We actively support and make referrals to the various Government schemes for struggling homeowners: Support for Mortgage Interest, Homeowner Mortgage Support and Mortgage Rescue.

2. Introduction

2.1 As a result of the recapitalisation, RBS made a commitment to maintain the availability and active marketing of competitively priced mortgage lending and have devoted £9billion to mortgage lending across the UK in 2009. We are doing our bit.

2.2 RBS offers a wide range of mortgages and also support several shared equity schemes that meet our lending criteria and which help first time buyers and key workers. Since the recapitalisation we have launched several market leading rates.

2.3 Whilst our market share increased in 2008, overall lending levels were inevitably lower than 2007 because demand for mortgages was low, a trend we have seen continue into 2009. The reasons for this include that forecasts of further house price falls are putting purchasers off buying.

3. RBS Mortgage Arrears

3.1 RBS arrears have increased since the first half of 2008, although the increase has slowed in recent months as many of our customers are currently benefiting from lower interest rates. This, coupled with the more favourable inflationary climate, has made it easier for customers to sustain their mortgage repayments. We also believe that the advice sector's efforts in educating customers in financial difficulties to give priority to making their mortgage payments may have helped.

3.2 RBS arrears rates compare favorably to industry averages. At the end of 2008, only 1.50% of RBS mortgages were in arrears of over 3 months compared to the industry average of 1.88% as published by The Council of Mortgage Lenders (CML). This is due to our focus on responsible lending, the fact that we have not undertaken subprime mortgage lending and have not offered self certification mortgages since 2004.

3.3 The forecast for mortgage arrears in the short to medium term is linked to the wider economy. In its quarterly inflation report published in May 2009, the Bank of England forecast inflation to remain below target for the foreseeable future. "It is more likely than not, that CPI inflation will be below the 2% target in the medium term" it said. This would suggest that interest rates would also be kept low which will help our customers. However, pressures on household incomes caused by a continued increase in unemployment levels will increase the number of homeowners in arrears albeit we expect a time lag before the full impact is seen.

3.4 The CML are forecasting the volume of customers in arrears by 2.5% or more of their outstanding balance to almost double between 2008 and 2009 (up from 182,600 to 360,000). We believe that RBS arrears rates will not accelerate as fast as the CML forecasts, taking into account the profile of our mortgage book.

4 Repossessions

4.2 In 2008, we repossessed 1,133 properties out of a total of 40,000 market repossessions. This equates to 2.8% of total market repossessions, considerably less than our c. 6% share of mortgage balances outstanding. RBS repossession levels have been relatively stable recently and we expect repossessions for the first half of 2009 to be in line with the levels experienced in the second half of 2008.

4.2 Our low repossession rates can be attributed to the high credit quality of our book and the stress we place on ensuring repossession is very much a last resort (see section 5 below for further information).

4.3 36% of our possessions in 2008 were vacant possessions, where the customer had either voluntarily handed their keys back or had abandoned their property. Where customers do wish to vacate and sell their property, we will seek to support them through the process.

4.4 In the case of forced repossessions, the customer will have had a history of missed or partial payments for more than 6 months and in practice 12 months may have passed before the property is repossessed. Typically this situation will be caused by factors such as a drop in income, a change in personal circumstances eg relationship breakdown, or affordability problems caused by other significant personal obligations such as over-indebtedness with other lenders.

4.5 Customers whose properties are repossessed tend to have an average original loan to value (LTV) that is higher than the average LTV of our mortgage book and a high proportion of repossessions relate to flats.

4.6 As with mortgage arrears, the possessions outlook is linked to the wider economy and we do anticipate an increase in the short to medium term. The CML are expecting 2009 new repossessions to be 62.5% higher than 2008 levels, up from 40,000 to 65,000. While we are expecting an increase, RBS own repossessions rates should continue to compare favourably and we believe that any increase will be at a slower rate than the CML projections.

5. Treatment and Approaches taken Towards Homeowners in Arrears and/or at Risk of Repossession

5.1 We want to do all we can to support our customers through these challenging times. We contact customers as soon as we are aware there is a problem and encourage customers to speak to us so we can jointly resolve matters. We work with each customer to understand their income and expenditure in detail and to determine which options may help their specific circumstance, including payment holidays, extended term and temporary reduced payments. Repossession is always a last resort.

5.2 Last December RBS pledged not to initiate repossession proceedings for a full six months after a customer first falls into arrears. This is double the amount of time recommended by the Government but we felt it was important to give our customers some breathing space during what is a very worrying time. No other high street lender has pledged to do the same, so far.

5.3 We also feel it is very important that customers in this situation are given the opportunity to seek advice from independent money advice organisations before any steps are taken. This pledge will remain in place until at least the end of 2009.

5.4 If the customer is unable to meet acceptable repayments and there is no realistic prospect of an improvement, alternative options will be considered including a voluntary sale of the property. Where we do repossess a property, we will endeavour to obtain the best sales price possible taking into account market conditions and the continuing increase in amount owed.

5.5 We actively support and make referrals to the various Government schemes for struggling homeowners: Support for Mortgage Interest, Homeowner Mortgage Support and Mortgage Rescue.

5.6 We would encourage our customers to come to us as soon as possible to talk about their financial problems. This is essential so that we can work together to find a solution that is right for them. Our objective is to support the customers to stay in their homes—it is not in our interests to repossess unless we absolutely have to and we only do it where all other options have been exhausted.

6. FSA Rules and Guidance on Repossession Policy and the Treatment of Customers in Arrears

6.1 RBS Group companies in the UK adhere to the Financial Services Authority (FSA) rules on arrears and repossessions contained in Chapter 13 of the FSA Mortgages and Home Finance: Conduct of Business Sourcebook ("MCOB 13").

6.2 We understand the FSA is considering the effectiveness of its rules as part of its Mortgage Market Review, which is due to be the subject of an FSA Paper in the autumn. RBS welcomes this Review but believes that many of the FSA's MCOB rules are still fit for purpose. We believe that a continued focus on requiring firms to achieve the right customer outcomes as well as effective prudential supervision of firms is the best solution.

6.3 The FSA rules in MCOB 13 do not cover buy-to-let mortgages or second charge lending. We believe that FSA regulation should be extended in future to cover these areas, using appropriately tailored rules.

7. Conduct, Protocols and Statements of Good Practice issued by Industry Bodies

7.1 Many of the requirements in the mortgage Pre-Action Protocol in England and Wales, introduced in November 2008, were already enshrined in the FSA MCOB 13 rules and were, therefore, already being applied by lenders in relation to FSA-regulated mortgages.

7.2 RBS welcomes the guidance provided by the CML on arrears and repossessions including the recent guidance for buy to let mortgages which will apply from 1 September 2009. We believe these are useful additions to the FSA rules and guidance and help consumers to understand what to expect from their lender.

7.3 RBS believes that self-regulation has an important role to play and can offer many benefits including an ability to make changes more rapidly when required.

8. Government Schemes to Support Homeowners facing Difficulties with Mortgage Payments and/or at Risk of Repossession

8.1 As mentioned above, we actively support and make referrals to the various Government schemes for struggling homeowners: Support for Mortgage Interest, Homeowner Mortgage Support and Mortgage Rescue.

8.2 Prior to the financial crisis, the only nationwide Government scheme available to struggling homeowners was Support for Mortgage Interest (SMI). This scheme had limited effectiveness as it applied only to mortgages up to the value of £100,000 and after 39 weeks of unemployment. For most consumers, this time delay was too long to protect their homes from repossession.

8.3 We welcome the changes that were made to this scheme at the start of the year, namely a reduction in the period for which homeowners have to wait to be paid from 39 weeks to 13 weeks, and an increase to £200,000 in the maximum size of mortgages eligible for the scheme. Where a recently unemployed customer meets eligibility criteria and has applied for SMI, we will grant a minimum 3 month repayment holiday to support them.

8.4 The Homeowner Mortgage Support and Mortgage Rescue schemes are intended for cases where a lender has exhausted all possible forbearance techniques. As RBS have a range of options to help homeowners experiencing repayment difficulties, always treat repossession as a last resort, and the proportion of our mortgage customers in arrears is lower than average, there are a limited number of customers we can apply these schemes to.

9. Impact of the Credit Crunch on Access to Mortgage Finance

9.1 Despite the current economic climate, we are very much open for business. RBS have committed to doing £9billion worth of incremental mortgage lending in 2009.

9.2 While we reduced our maximum Loan to Value (LTV) for mortgages to 90% in October 2008, we are actively lending to first time buyers and have committed to maintaining a competitive range of mortgage products with offers up to 90% LTV.

9.3 Furthermore we support the Government's shared equity schemes (and Welsh and Scottish government measures) which help buyers who would not otherwise be able to purchase a property on the open market.

9.4 For the period January to May 2008, our monthly average first time buyer lending was 14.4% of total new mortgage business. This figure was virtually unchanged for the same period in 2009 at 14.1%, demonstrating our commitment to supporting First Time Buyers.

July 2009

Written evidence from the Financial Services Consumer Panel

Introduction

1. The Financial Services Consumer Panel is pleased to have this opportunity to contribute to the Treasury Committee inquiry into mortgage arrears and access to mortgage finance.

2. In our submission we have focused on the two specific aspects of the Inquiry's Terms of Reference where we have the most expertise:

— adherence to, and the effectiveness of, Financial Services Authority (FSA) rules and guidance for mortgage lenders on repossession policy and treatment of consumers in arrears as well as the FSA's regulatory approach in this area

— adherence to, and the effectiveness of, codes of conduct, protocols and statements of good practice issued by industry bodies in this area.

FSA Regulation

3. Consumers have not been well served by the mortgage market excesses of recent years. We appreciate that no borrower was forced into submitting a mortgage application during the heady days of 2004–07. However, in our view, there was insufficient consideration given by many lenders and by the regulator to the consequences of steadily increasing house prices and the growth of inappropriate mortgage lending.

4. Mortgage lenders seem generally to argue that the existing FSA rules on mortgage arrears—MCOB 13—are fit for purpose. We disagree. We think that there are weaknesses in some areas! For example:

(a) MCOB 13 contains relatively few actual rules that are binding on lenders. We would like to see either more rules or a more explicit statement of what is required from the guidance. For example, MCOB 13.3.4 sets down guidance that firms should give borrowers "a reasonable period of time to consider any proposals for payment'. We think that it would be reasonable for this to be enshrined as an obligation on firms and perhaps with a specified time period rather than merely guidance. That way, borrowers and their advisers would be clearer about what they could expect from firms.

(b) The MCOB rules were written after a period of sustained growth in UK house prices when mortgage arrears were low, and when the vast majority of borrowers in arrears had the opportunity to voluntarily sell their property to repay their debt. With hindsight, there was insufficient regard to ensuring that the rules establish the best balance between the interests of lenders and borrowers for a much more difficult time for the mortgage and housing markets. The forthcoming review of the MCOB regulations provides the opportunity for the FSA to review whether their rules are fit for purpose in bad times as well as good.

(c) There is an immediate need for the FSA to ensure that firms are complying with MCOB 13. There is a feeling that the FSA has been backward in its supervision of the rules, especially of less scrupulous firms in the "sub prime" and self-certification markets. For example, MCOB 13.3.1 requires that all lenders must have a written policy that sets out how they will deal fairly with any customer in arrears. We believe it appropriate that the regulator should collate and regularly review all of these policies to ensure that all lenders are responding appropriately to customers in financial difficulty. The FSA wrote to the chief executives of all mortgage lenders and mortgage administrators[89] in November last year giving them until January this year to ensure that their

[89] http://www.fsa.gov.uk/pages/Library/Communication/PR/2008/142.shtml

customers facing arrears were being treated fairly. However, the FSA found in its own thematic work published last month that poor practice was still prevalent, particularly among specialist lenders and third party administrators.[90]

(d) Second mortgages are not subject to FSA rules, covered instead by the Consumer Credit Act and thereby falling under OFT regulation. There are many commentators who are calling for the FSA to take over secondary lending. Whilst we can see the attraction in simplifying the regulatory responsibility for all residential mortgage borrowing, in many areas, the Consumer Credit Act rules are much more prescriptive than the MCOB rules. Losing the consumer credit rules would remove important and powerful protection for consumers. For example, the time order provisions of the Consumer Credit Act protect borrowers from lenders that seek to recover arrears over an unrealistically short time period. We support the suggestion that the FSA should take over regulation of second charge lending—but only if it also retains the important protections of the Consumer Credit Act.

The forthcoming review of the FSA MCOB rules is an opportunity to consider whether some of the. requirements of the CCA should be incorporated within the MCOB rules.

The Mortgage Arrears Pre-action Protocol

5. It is our opinion that there still needs to be better joining up between FSA rules and the primary legislation of the Administration of Justice Act. For some years the Panel has been concerned that District Judges at County Courts were not even aware of, let alone taking account of, the FSA rules when considering applications for possession of mortgaged properties. We are now satisfied that, since the introduction of the mortgage arrears pre-action protocol, judges are at least aware of the FSA rules. However, we are still told that there is a lack of clarity about how much judges can take failure to keep to these rules into account in a possession action. It is worth noting that a Bill will be introduced in the Scottish Parliament in the autumn to build on the protection available through the Mortgage Rights (Scotland) Act 2001 in repossession cases. The Scots believe that there is a need for legal clarity in this area. We look to the FSA and the Ministry of Justice to take steps to bring more clarity to this arena in England and Wales.

6. Repossession proceedings can come to court very quickly and although the mortgage arrears pre-action protocol appeared to be a helpful initiative we consider that it is relatively toothless. The protocol sets down little by way of sanctions in the event that firms fail to abide by its requirements. We would be keen to see the FSA include some elements of the protocol as new rules within the amended MCOB 13

Information and Advice

7. The importance for consumers to get appropriate information and advice if they fall into arrears on their mortgage is acknowledged. The Panel has just completed a research project looking at what people who are having difficulty paying their mortgage do to get help.[91] Seven out of eight (87%) of those finding it difficult to make payments thought their problems were serious, but two in five (41%) of those having difficulty had not tried to get advice in dealing with their problems. Of those who did seek advice, two thirds (65%) went to their mortgage lender, while one in four went to Citizens' Advice (CAB). Consumers' experience of lenders' advice was mixed: some felt their mortgage lender was unhelpful and inflexible, whereas others felt their provider had done all they could reasonably do to help them.

8. It appears that the most significant driver for those who do not seek advice is not a lack of awareness of or difficulty in accessing advice services per se, but rather consumers' perception of the advice sector and their own situation. This leads many consumers to decide that seeking advice is either unnecessary or inappropriate for them. More needs to be done to change consumers' behaviour and their perception of what already exists. There is an urgent need for more investment in publicising and supporting sources of information and advice in this area. In particular consumers in difficulty should be encouraged to get advice early, before the problem becomes a disaster for both parties. Debt advice agencies must not be seen as a last resort when all else has failed.

9. Whilst there has rightly been a great deal made of the importance of giving mortgage customers every opportunity to repay any arrears we feel that there should also be wider acknowledgement that repossession can sometimes be in the longer terms interests of the consumer.

10. If someone cannot afford the interest payments on their loan their debt will increase. If they struggle to make whatever payments that can be negotiated at the same time as their debt is increasing experience is that within 6 months to 2 years they see that they are better off giving up, realising whatever equity that may still be available, and moving to rented accommodation (where they may be eligible for Housing Benefit or local authority rehousing).

11. If a borrower cannot afford to make full interest payments within, say, six months, it is important that they are encouraged to consider whether the future interests of them and their family are best served by the sale of the property or that some mortgage rescue scheme (for example allowing the borrower to remain in

[90] http://www.fsa.gov.uk/pages/Library/Communication/PR/2009/080.shtml
[91] http://www.fs-cp.org.uk/pdf/researchjun09.pdf

their property under some different kind of tenancy/ownership eg, with the aid of a Housing Association or Local Authority) is put in place. It is therefore essential that borrowers can access high quality advice that is independent and impartial.

ROLE OF THE CONSUMER PANEL

12. The Panel was established by the Financial Services and Markets Act to provide advice to the FSA. The Panel's terms of reference as set out in our annual report allow it to comment and seek to influence the financial landscape beyond that which is regulated by the FSA. Examples include policy proposals by H M Treasury, the OFT, the Personal Accounts Delivery Authority and the impact of European developments on UK consumers. Further information about the Panel can be obtained from the Panel's website http://www.fs-cp.org.uk/

July 2009

Written evidence submitted by the National Landlords Association

EXECUTIVE SUMMARY

1. The National Landlords Association (NLA) is the UK's leading representative body for private residential landlords with close to 20,000 members.

2. Landlords are key consumers of financial products including specialist mortgages which accounted for approximately 30% of all mortgage lending in 2007.

3. There is a distinction between types of landlord in respect of exposure to financial risk and the market;

— Relatively recent market entrants with smaller portfolios, generally less than ten properties. These landlords tend to have considerable exposure to market forces and are therefore vulnerable to the downturn. In particular they tend to be leveraged to a larger extent and therefore more reliant on available mortgage products. In the coming months most of these landlords do not expect to make further acquisitions and many expect to suffer arrears.

— Large and established portfolio landlords, generally with greater than 20 properties. This group are leveraged to a far lesser degree and are therefore unlikely to be greatly affected by the unavailability of varied mortgage products. Consequently they also possess greater capital reserves and are therefore less exposed to falling property values.

4. Due to the economic downturn landlords are experiencing difficulties in relation to their letting businesses. Specifically:

— *Limited LTV*. Lenders are limiting available finance to 70–75% LTV for BTL products. Landlords are being required to put much more money down in relation to property purchases.

— *Lending criteria*. Criteria have become much stricter; lenders are requiring a great deal more information about a landlords financial security than was previously the case.

— *Interest rates and fees*. Arrangement and administration fees have increased considerably and now represent between 1 and 4% of the mortgage value. While the Bank of England rate is historically low the rates being offered in respect of BTL are on average 4% above base.

— *Interest only mortgages*. Many lenders are no-longer offering interest only mortgages to landlords as such their monthly costs are much higher incorporating capital repayments. It is likely that rental payments alone may not cover the average combined repayment mortgage meaning that other revenue streams may be required.

— *Mortgagee valuations*. Lender valuations are decreasing values and therefore making obtaining sufficient finance for purchases more difficult.

The Market—the Landlord's Perspective

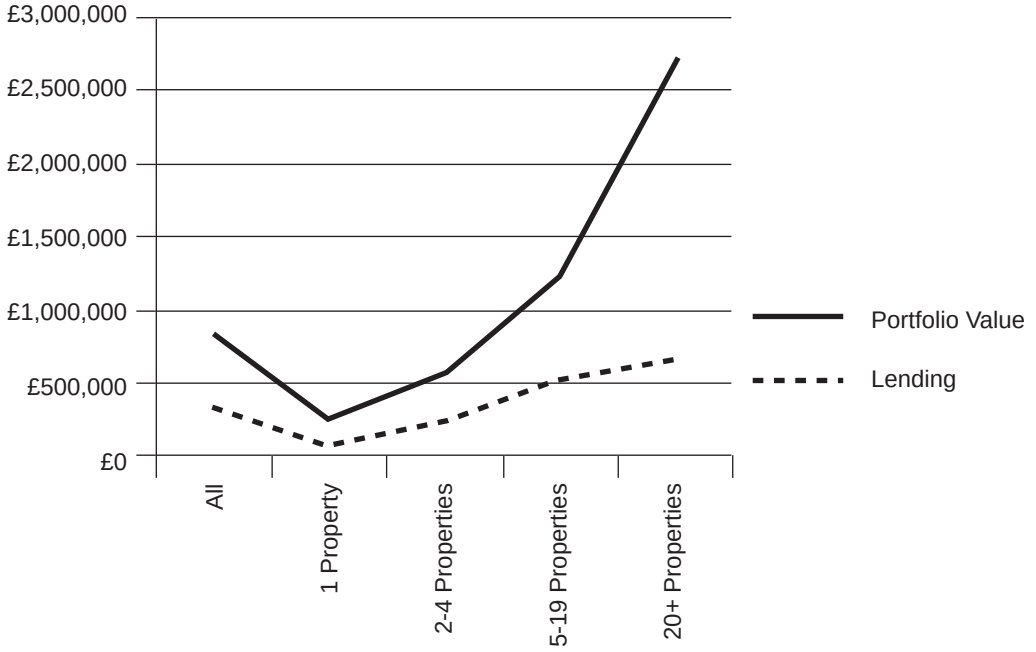
5. As is usually the case the housing market has been significantly impacted by the economic downturn and in common with many other industries the private-rented sector (PRS) has had to adapt to changing economic conditions over the course of the last 18 months. However the PRS has evolved a great deal since the last recession with the introduction of specialised mortgage products and the emergence of the "buy-to-let landlord". As such the market is being forced to react in ways that it has not had to before due to levels of exposure which were not present prior to the growth in buy to let in the late 1990's and beginning of the 21st century.

6. In order to assess the specific impact of the economic downturn upon landlords and the PRS it is important to understand the demographics associated with the sector and the variance which exists amongst landlords. When referring generally to landlords we encompass a very wide range of business and investment models which should perhaps be viewed apart in relation to certain strata. For instance the mean average portfolio value for a private residential landlord is estimated at approximately £818,327 however 56% of

landlords possess a portfolio worth less than £500,000 and 7% owning less than £100,000 of rental property. It is therefore very difficult to define the average landlords or make definitive assumptions about his or her exposure to the economy and financial markets.

7. Research data suggests that in relation to current market exposure it is useful to categorise two broad groups of landlords based on portfolio size; roughly those with 1-14 properties and those more established portfolio landlords with in excess of 15 properties. In relation to this general stratification it can deducted that larger portfolio landlords have a lower level of exposure to fluctuations in the economy . This is largely due to their lower reliance on lending . For example research illustrates that portfolios across all landlords are leveraged on average at 38% loan-to-value (LTV). However when this figure is broken down it transpires that landlords with more than 20 properties have an average LTV of only 25% compared to those with approximately two to four properties average LTV of 42.5%. As illustrated by figure 1 as portfolio size and subsequently value increases lending as a proportion of value declines.

Figure 1



8. It is also important to note that the above graph excludes those landlords with no reliance on mortgage finance, who own their portfolios outright. It is estimated that 39% of landlords have no outstanding mortgage finance on their rental properties and therefore no exposure to fluctuating finance availability and costs.

9. Assuming that exposure to mortgage finance represents a key factor in relation to the impact that the changing economic climate will have on private residential landlords it can be interpreted that more established landlords with less reliance on mortgage finance will find it easier to continue their business during such times. This is reflected in evidence of reported profitability, figure 2.

Figure 2

Profitability (%)

	Enough Profit to save	*Enough profit to live on*	*Enough profit to supplement my income*	*Break even*	*Small loss*	*Large Loss*
All Landlords	24	13	40	18	5	1
1 property	16	3	40	25	14	2
2–4 properties	19	10	48	19	3	1
5–19 properties	31	23	33	12	1	0
20 properties	52	29	13	6	0	0

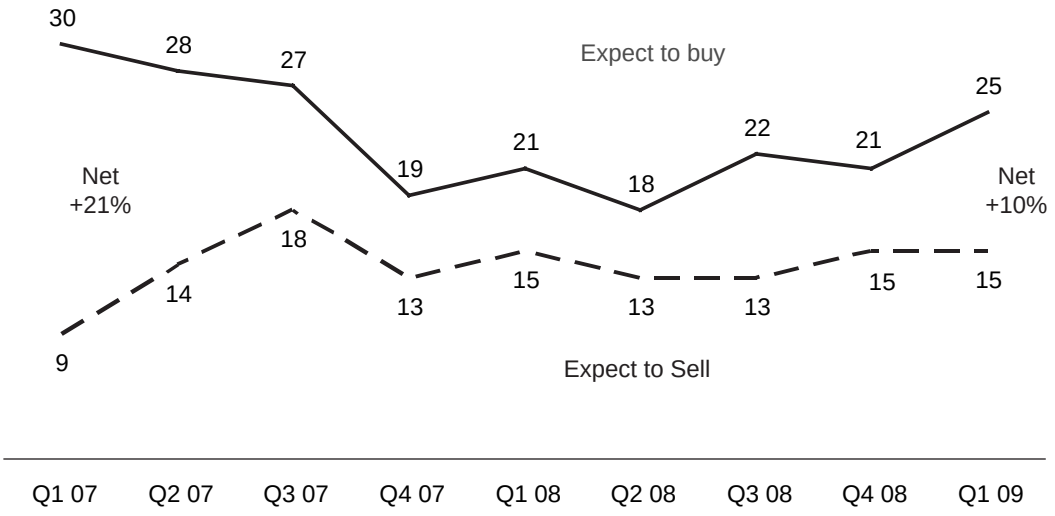
10. As figure 2 illustrates larger landlords are much less likely to be experiencing a loss, or just breaking even, than smaller landlords and are very likely to be making a significant profit. This data would suggest that this is a difficult time for new or recent entrants to the PRS and those with a portfolio of limited size, but not necessarily evidence of market failure.

Market Prospects

11. It is estimated that the PRS will experience a property stock growth during the next quarter, although this growth is expected to come almost exclusively from established portfolio landlords. There has been a downward trend in relation to market growth since Q1 2007 within this sub-group, however figures for Q1 2009 suggest a return to stronger growth with a projected net 10% of established landlords growing their portfolios (Figure 3).

Figure 3

Established Landlords expecting to transact in next 3 months



12. In light of the effect the economic downturn on their tenants and in particular increasing unemployment landlords are reporting increasingly lengthy void periods which impact upon their ability to meet their financial obligations. Less than half of all landlords (49%) report no void periods in the last 12 months while 37% state that their tenants (collectively) have missed in excess of 15 days rent in the last year. Disturbingly this has led to 16% of landlords who experience voids missing at least one mortgage payment and 11% resorting to using short term credit to meet mortgage commitments as a result of lost rental income.

Availability of Finance

13. The relative growth of the PRS over the last two decades owes a great deal to the liberalisation and diversification of available mortgage finance and in particular the introduction of the buy-to-let mortgage in the mid 1990's. Throughout the "boom" of the late 1990's and first years of the 21st century finance was comparatively easy to come by for the purposes of residential property investment and mortgagees felt secure in offering high LTV products on the basis that property appreciation would ensure a degree of equity should difficulties arise throughout the term of the loan. With the onset of the credit crunch and ensuing downward trend in property values the status quo has altered presenting landlords with difficulty in obtaining financial products.

14. Market observers now estimate that 95% of the specialist buy-to-let mortgage products available in 2007 are no-longer available. Furthermore those financial products which are available for landlords have associated with them far stricter lending criteria and relative costs. For example a number of landlords have recently contacted the NLA in relation to the high application costs of certain products, in one instance the company in question had reduced their maximum LTV offering to 75% whilst increasing their buy-to-let application fee to 4% of the loan value. Therefore in order to purchase a £100,000 property a landlord applying for this product would need to raise £25,000 in deposit and pay a further £3,000 application fee in addition to the usual legal and valuation fees connected with property transactions. In many cases this, combined with the increasingly strict lending criteria now common in the PRS, is making residential property investment less desirable.

15. Despite the difficulties many landlords are keen to expand their portfolios in the current market due, in part, to depressed property valuations and as such are seeking mortgage finance to do so. Almost one in four of all landlords state that they are likely to seek new finance in the next three months, and 52% of

established portfolio landlords wish to do so, in order to make a new acquisition or refinance existing stock. It is likely that these landlords will find it difficult to obtain a product on similar terms to which they have experienced in recent years.

Figure 4

Ease of obtaining mortgage finance

Experience (compared to previous attempts)	*Landlords who sought mortgage finance in the last three months (%)—Q1 2009*
Much easier	7
Slightly easier	11
No difference	31
Slightly more difficult	26
Much more difficult	25

As figure 4 above demonstrates 51% of landlords actively seeking finance have found it more difficult to obtain, this represents an increase from 28% in Q4 2008.

16. Landlords are also reporting that lenders' attitudes towards their business have changed in the last 12 months as tighter lending controls have been applied to the buy-to-let market. In turn this has driven down brand loyalty amongst landlords as they appear more likely to shop around for satisfactory products. In particular mortgagees are now requiring significantly higher deposits with many institutions offering no higher than 75% LTV against rental property. High interest rates are also an issue as, despite the historically low Bank of England base rate, many banks are charging in excess of 3.5% over base and prohibitively large arrangement fees. It should also be noted that lending against niche property types has almost disappeared leaving landlords of properties such as houses in multiple occupation (HMO) with very few funding options.

17. Due to fluctuations in the housing market there is anecdotal evidence that valuers are becoming more cautious and as such undervaluing property on the behalf of mortgagees. This is having the effect of further reducing the availability of finance for landlords interested in acquiring stock in relation to the impact which valuations have on LTV offers.

Sale and Rent Back

18. The sale and rent back (SRB) market has existed as a sub-market of the PRS for some time but has gained prevalence in the last few years. At its height, circa mid-2007, the market comprised of approximately 2000 firms and individual landlords offering SRB services, however this figure has declined sharply over the last 18 months. In response to a reduction in the number of suitable financial products available and to some degree the negative public perception of the market NLA estimate that there are currently very few scheme operators actively trading. Furthermore with the introduction of interim FSA regulation from 1 July 2009 the number of firms with permission to offer SRB products and services is likely to fall to less than 50.

19. In general individuals turn to SRB products for a number of core reasons:

— Long term illness affecting individual or close reducing household income and therefore the affordability of home ownership.

— Marital/partnership breakdown leading to the loss of one income stream.

— Over indebtedness.

— Fixed interest rate period comes to end potentially increasing mortgage repayments with a return to standard variable rates (less of an issue currently).

— Owner occupier wants a quick exit from property ownership.

20. The SRB market has a negative public image and is consistently portrayed in the media as an option of last resort predominantly offered by less than ethical companies. While NLA recognise that SRB does represent a certain potential for consumer detriment and acknowledge that there have been some instances of considerable disadvantage we feel that the extent to which this has happened has been overstated. We hold that the vast majority of landlords involved in SRB have operated ethically and professionally.

21. Logically the economic downturn should lead to increased demand for SRB services and as such an expansion of the market. To a certain extent this has been the case as larger numbers of homeowners have found themselves in financial difficulty and sought a way to service existing debts. Conversely as demand has risen the market has not necessarily grown to match need as many SRB operators have experienced increasing difficulty in obtaining sufficient finance in order to make purchases. This has been exacerbated by the removal of most of the suitable mortgage products since the end of 2007.

22. Following an Office of fair Trading (OFT) market study conducted in 2008 and a period of stakeholder consultation on behalf of the Treasury and Financial Services authority (FSA) interim regulation of the SRB market began 1 July 2009 to combat potential consumer detriment. NLA have been very supportive of the approach taken by the FSA in introducing a two stage regime of regulation in order to improve standards and instil consumer confidence in SRB. We believe that the increased disclosure

requirements and requisite transparency will help to improve the negative perceptions of the industry and allow for competition and growth between remaining providers. Unfortunately it is also our view that the requirements of the interim regime and in particular the short time scales involved in its implementation will reduce the number landlords involved in SRB significantly.

23. In relation to the aspects of consumer abuse associated directly with the sale of property to SRB landlords it is likely that, with proper monitoring and enforcement, the regulation as proposed will be sufficient to allow consumers to make informed decisions about their options. As such NLA have welcomed the FSA's involvement, however we believe that the continuation of a tenancy, which by definition must take place as part of an SRB transaction, has been largely overlooked by the Treasury in the design of regulation. It is our view that there is potential for consumer detriment in relation to the premature cessation of tenancies in order to realise capital gain when tenure had been implied during negotiations. As such we would like to see the statutory definition of SRB incorporate greater recognition of the importance of a sustained landlord-tenant relationship in connection with these transactions.

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