TOPIC 8

Regulation and the buying process

LEARNING OBJECTIVES

In this topic we are focusing on the regulations with which the lender or intermediary must comply at key stages in the mortgage application process. You will then have considered the buying process from the perspective of the buyer, the solicitor and the lender, giving you a good picture of the interactions and responsibilities of the different participants.

By the end of this topic, you should have an understanding of:

- the key regulatory stages in the mortgage application process;
- real-time and non-real-time financial promotions and the rules that apply to each;
- the purpose and nature of initial disclosure requirements;
- the circumstances in which a mortgage may be sold on an execution-only basis;
- the information that must be provided at the pre-application and application stages;
- the information that must be provided at the start of the contract.

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IMPORTANT

The focus of this topic will be on MCD regulated mortgages, which are entered into on or after 21 March 2016. Mortgages before that date are referred to as regulated mortgages and are subject to the original MCOB rules for servicing and variations.

However, firms have the flexibility to apply MCD disclosure requirements to pre-21 March 2016 mortgages in order to avoid running parallel processes. We will briefly cover the main rules applying to regulated (non-MCD) mortgages at the end of each section (where applicable).

THINK . . .

Before you begin work on this topic, think back to your studies on conduct of business requirements for UK Financial Regulation. You will find that you are already familiar with some of the information in this topic, which discusses regulation specifically in relation to the mortgage application process.

For instance:

- What different stages in the application process are identified in MCOB?
- What is a financial promotion?
- What does the acronym ‘ESIS’ stand for?

8.1 What are the key regulatory stages in the mortgage application process?

From a regulatory point of view there are key stages in the application process where regulatory requirements must be met, as outlined in Figure 8.1. We will work through these stages step by step.

FIGURE 8.1 KEY REGULATORY STAGES

Financial promotions, ie marketing of mortgages (MCOB 3A)

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Initial disclosure: meeting the adviser to discuss needs and circumstances to identify a suitable mortgage (MCOB 4 & 4A)

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Providing advice (MCOB 4) and lending responsibly (MCOB 11 and 11A)

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Making an application (MCOB 5 and 5A)

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Receiving a mortgage offer from the lender (MCOB 6 and 6A)

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Disclosure at the start of the contract (MCOB 7)

8.2 Marketing of mortgages (MCOB 3A)

FINANCIAL PROMOTION

An invitation or inducement to engage in an investment activity, which includes mortgages.

The FCA MCOB rules refer to the marketing of mortgages as financial promotions, which can be solicited or unsolicited and take various forms, including telephone calls, mailshots, websites and newspaper or TV advertisements. The rules apply to financial promotions for qualifying credit (regulated mortgages) or home reversion plans.

CHECK YOUR UNDERSTANDING 1

What is the difference between solicited and unsolicited promotions to customers?

Financial promotions are not allowed unless they are carried out by an individual (or firm) authorised by the FCA, or the content has been approved by an individual (or firm) authorised by the FCA. In most cases an authorised firm would allocate responsibility for approving financial promotions to a specific team, such as marketing.

Some types of promotion are exempt from the rules. In the main, these are promotions that only contain general information about the firm and its main business, without offering any inducement to take up a particular mortgage or service. All financial promotions for qualifying credit or home reversion plans must be clear, fair and not misleading.

8.2.1 Non-real-time financial promotions

All non-real-time credit promotions must conform to the following:

- **Company details** – the company name and address, or a telephone number or email address where the full address is not available.
- **Clarity** – the promotion must not disguise, omit, diminish or obscure important items, statements or warnings; and must ensure any comparisons or contrasts are presented in a fair and balanced way.
- **Risk of repossession** – a statement about the risk of repossession if the borrower does not keep up mortgage payments.

NON-REAL-TIME FINANCIAL PROMOTION

Any promotion that does not include interactive dialogue – SMS, email, faxes, letters, adverts, etc.

- **Annual percentage rate of charge (APRC)** – the APRC must be included if the promotion contains price information, and must be clearly distinguishable from any other rates shown. The APRC is designed to show the true cost of borrowing over the term and is expressed as an average annual interest rate. It takes into account the interest charged, plus any additional fees payable.
- **Interest rate** – the interest rate and whether it is variable or fixed, together with details of any charges included in the total cost of credit.
- **Credit** – the total amount of the credit.
- **Term** – the term of the mortgage, where applicable.
- **Instalments** – the amount and number of instalments, where applicable.
- **Total** – the total amount payable by the borrower.
- **Example** – a representative example to illustrate the points above. An example will only be regarded as 'representative' if the firm can reasonably expect that at least 51 per cent of people who respond to the promotion and those who enter into the contract advertised would actually be charged the APRC quoted (or a lower amount).

Competitor comparisons are only permitted on a like-for-like basis and must not disparage or discredit the competitor, or take unfair advantage of the competitor's reputation.

The firm must keep records of all non-real-time credit promotions for at least 12 months from the time they were last used.

8.2.2 Real-time financial promotions

REAL-TIME FINANCIAL PROMOTION

Any promotion made through a telephone or face-to-face conversation, or other interactive dialogue.

WHEN ARE UNSOLICITED CALLS ALLOWED?

Unsolicited calls ('cold calls') are only allowed where the recipient has an established existing customer relationship with the firm and the relationship is one where the customer can expect to receive such calls. It could be argued that these are not true cold calls at all.

The rules for real-time promotions, including those made by call centres, are as follows:

- **Hours** – they cannot be made at an unsocial hour unless previously agreed. FCA guidance states that an unsocial hour would usually be a Sunday or between 9pm and 9am on any other day. It also includes other days or times when the caller should know that the customer would not wish to take a call for personal reasons, such as religious beliefs or working patterns.
- **Contact** – contact cannot be made on an unlisted telephone number unless the customer has previously agreed.
- **Identification** – the caller must identify themselves and their firm.
- **Check** – the caller must check that the customer agrees to continue with the conversation if the time and method of communication has not been agreed earlier.
- **Terminate** – the caller must terminate the conversation if the customer does not wish to proceed.
- **Content** – the content of the conversation must be clear, fair and not misleading, and not make any untrue statements.

8.3 What is initial disclosure? (MCOB 4 and 4A)

When a prospective purchaser seeks a mortgage, the firm arranging the mortgage must provide the borrower with information about the firm and its status through 'initial disclosure'. As all new mortgages arranged are MCD regulated mortgages, we will focus on the rules applying to them.

The initial disclosure requirements apply to each of the 'relevant markets' in which the firm operates. Relevant markets are defined as:

- regulated mortgages that are not for business purposes; and
- those that are for business purposes.

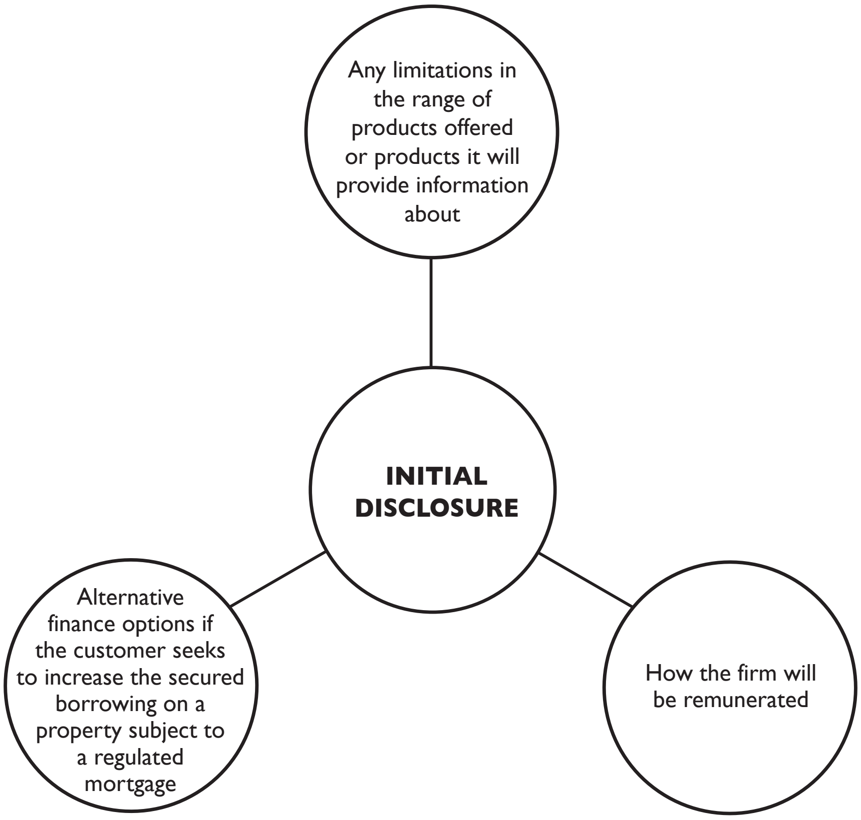
If a firm is offering services to a customer in both the relevant markets, it must describe its services in each market and state, for each market, whether it offers first-charge mortgages, second-charge mortgages or both. Note that lifetime mortgages are not included under the MCOB 4 and 4A requirements because they have their own MCOB rules.

If the mortgage is to be arranged directly from the lender, it is the lender's job to provide the disclosure information. Where the mortgage is arranged through an intermediary, it is the intermediary who must provide the disclosure information.

Although the content is set out by the regulator (as shown in Figure 8.2), there is no prescribed format for the disclosure information and it can be designed by the firm. The information must be presented in a durable medium for MCD regulated mortgages. Durable medium is defined in the FCA Handbook as: "paper; or any instrument which enables the recipient to store information addressed personally to the recipient in a way accessible for future reference and for a period of time adequate for the purposes of the information and which allows the unchanged reproduction of the information stored" (FCA, no date).

The information must be provided before the firm carries out any mortgage arranging or advisory activity.

FIGURE 8.2 WHAT MUST INITIAL DISCLOSURE TELL THE CUSTOMER?



8.3.1 Range of products

In relation to the range of products offered, there are three types of service that the firm can offer to customers (see Figure 8.3); the service to be provided must be clearly indicated to the customer when first making contact.

FIGURE 8.3 THREE TYPES OF SERVICE

Unlimited	Firm selects and recommends from a range of products that represent the whole market
Limited range	Firm selects and recommends from a limited range of products, typically from a panel of lenders
Single lender	Firm selects and recommends only the products of a single lender

Note that 'unlimited' does not mean the firm has to select from every single product on the market – the key is that the products offered should be representative of the whole market. If the firm does meet the criteria but does not offer mortgages available only directly from the lender, it must make that clear, using phrases such as: "We offer a comprehensive range of mortgages from across the market, but not deals that you can only obtain by going direct to a lender."

If a firm does not offer an unlimited product range to its customers, it must list the names of all the lenders whose products it offers. It must also express any limitations in the product range simply and in clear terms, including situations where products or information are only available through certain channels, eg in branch or online.

A firm that only offers products from one part of the relevant market cannot describe its service as unlimited. The FCA gives bridging finance as an example.

8.3.2 The firm's remuneration

The firm must inform the customer of:

- any fees the firm will charge them;
  - there are rules covering the main ways in which fees can be calculated, such as hourly fees or fees calculated as a percentage of another figure, such as the mortgage amount;
  - the principle is that the customer must be given the fee that will apply or, if that is not known at this stage, examples of how such fees work and the potential costs;
- when such fees will be payable (and when reimbursable, if appropriate);
- whether the firm will receive commission or a procuration fee from the lender or a third party; and

- the firm must state the amount of commission or, where the amount is not known at the time of disclosure, state that the actual amount will be disclosed at a later stage in the European Standardised Information Sheet (ESIS) that must be provided before an application is made.

If the firm will receive commission, it must disclose any arrangements for offsetting this against any fees charged to the customer, where applicable.

Fees should be shown as specific cash sums where possible. If the fee cannot be shown as a specific cash sum, in general terms the firm must provide the customer with an indication of the likely fees; the format for providing this information depends on the nature of the fee.

8.3.3 Alternative finance options

Where the borrower is looking to raise further funds on a property that is already subject to a regulated mortgage, the firm must inform them that alternative funding could be obtained through a further advance (unless it knows that the existing lender will not offer that facility), a second charge, a mortgage with another lender or unsecured borrowing. The firm does not have to ascertain the appropriateness of the alternatives.

Where a customer is considering a retirement interest-only mortgage, the firm must inform the customer, orally or in writing, that a lifetime mortgage may be available and more appropriate. There is no requirement to provide advice on the suitability of a lifetime mortgage.

8.3.4 Variations to pre-21 March 2016 contracts

The disclosure requirements for both regulated and MCD regulated mortgages contain a common core of information (MCOB 4), with MCD mortgages firms required to provide specified additional content (MCOB 4A). Should a firm need to provide initial disclosure documentation to a customer wishing to vary a mortgage taken out before 21 March 2016, firms may choose to avoid the potential problems caused by running two systems by providing the disclosure information in a format that meets the MCD requirements.

8.4 Providing advice (MCOB 4 and MCOB 4A)

A borrower seeking a regulated mortgage may:

- be given qualified advice; or
- proceed on an execution-only basis.

Firms can provide *information* (ie generic content that is not tailored to the specific borrower) at an early stage in the process but they are expected to provide advice whenever the sales process involves interactive dialogue. Advice must be given before a contract is arranged or the borrower enters into the contract.

Adequate explanation

When advising on an MCD regulated mortgage, the firm must provide an adequate explanation of the product being recommended. The explanation can be oral or in writing, and must cover:

- the information included in the ESIS – see section 8.6;
- the key characteristics of the product;
- the effect the product would have on the customer (including in the event of the customer defaulting on the repayments);
- the scope of service, fees payable and remuneration, if the advice is given by an intermediary.

RECORD-KEEPING

A firm must keep customer information records used to make a recommendation, as well as the reason why the advice is suitable and any customer decisions made about rolling up fees into the loan. Records must be kept for a minimum of three years from the date the advice was given.

EXECUTION-ONLY

A transaction executed upon a client's specific instruction, where the firm gives no advice and the rules on assessing appropriateness do not apply.

8.4.1 Execution-only business

Although firms are expected to provide advice in most cases, the FCA has made it easier for firms to provide options to consumers without it being deemed advice. This makes a firm's execution-only offering easier to use. In cases where a firm has provided customers with product information in line with MCOB requirements, it can carry out execution-only sales for those customers, as long as the information provided does not steer the customer towards execution only.

There are rules governing the situations in which customers may proceed on an execution-only basis at their own request, including those who wish to vary the terms of an existing contract.

Execution only is permitted when:

- there is **no interactive dialogue** between the firm and the customer during the sale, eg website and postal applications, as opposed to instant messaging and social media; or
- there is **interactive dialogue but the customer is in one of three categories** and has elected to proceed on an execution-only basis:
  - — high-net-worth (HNW) customers;
  - — professional customers (who must select the product they wish to arrange);
  - — the loan is solely for business purposes; or
- there is **interactive dialogue but the firm's contribution is limited** to:
  - — factual information about a regulated mortgage or application and administration processes;
  - — the provision of an ESIS or a mortgage illustration;
  - — an explanation that it has not assessed suitability and that the protection of an advised sale will be lost; or
- the **customer has rejected advice**, identified the product they wish to purchase and has elected to proceed on an execution-only basis.

When a firm accepts an execution-only sale it must keep a record of the sale, including the information provided, confirmation from the customer, and any rejected advice offered, for three years from the start of the contract.

High-net-worth customers

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CHECK YOUR UNDERSTANDING 2

From your studies in Topic 2, can you remember the FCA criteria for a borrower to be classed as an HNW customer?

a) Minimum annual net income of £300,000, or minimum net assets of £3m.

b) Minimum annual net income of £3m, or minimum net assets of £300,000.

c) Minimum annual net income of £30,000, or minimum net assets of £3m.

Lenders may adopt a different approach to HNW customers from that used for most retail customers, based on three main factors:

- disclosure – lenders can use a tailored approach, which primarily focuses on the wording used;
- advice – interactive sales may be conducted on an execution-only basis;
- responsible lending – lenders can be a little more flexible in the assessment of affordability.

When lending to an HNW customer, the lender requires evidence that the customer has:

- rejected advice;
- identified the product they wish to purchase;
- positively chosen to proceed on an execution-only basis.

It also requires written confirmation from the customer that they understand the consequences of losing the protections of the rules on suitability.

Professional customers

CHECK YOUR UNDERSTANDING 3

From your studies in Topic 2, can you recall the criteria that define a professional customer?

a) For how long must they have worked recently in the home finance sector?

b) What must their professional position require?

c) Of what must the firm reasonably believe they are capable?

As long as the firm is satisfied that it has evidence that the customer meets the criteria for a professional customer, and that the customer has selected the product they require or rejected advice given, it can deal with the customer on an execution-only basis.

Regulated mortgages for business purposes

CHECK YOUR UNDERSTANDING 4

From your studies in Topic 2, can you recall the key difference that distinguishes a regulated mortgage for business purposes from a regulated mortgage for a personal borrower?

a) One of the purposes of the loan, remortgage or further advance is to raise additional money for the use of a small business.

b) The sole purpose of the loan, remortgage or further advance is to raise additional money for the use of a small business.

c) The sole purpose of the loan, remortgage or further advance is to raise additional money for the use of a large business.

Raising funds through a regulated mortgage to fund the purchase of, or work on, a buy-to-let property is not classed by the FCA as being for business purposes.

Customers who may not proceed on an execution-only basis

Apart from loans to HNW or professional customers, or mortgages solely for business purposes, a firm **cannot** arrange an execution-only sale if:

- the purpose of the loan is to exercise a statutory 'right to buy' a home; or
- the main purpose is to raise funds for debt consolidation; or
- the mortgage is a shared equity arrangement – shared equity being where one person buys a share in a property with a mortgage, and the remaining proportion is held by a third-party provider, who will receive a proportionate share of the proceeds when the buyer eventually sells the property. Shared equity is covered in Topic 25.

Customers in the situations listed above, together with those considered to be 'vulnerable customers' (see section 2.6.2), must receive advice. However, in the interests of freedom of choice, customers can choose to reject the advice offered and purchase a different product on an execution-only basis (MCOB 4.8A.12 – Exception: rejected advice).

Although execution only is not generally available to those exercising their statutory right to buy, or those wishing to consolidate debts, those customers can vary the terms of an existing arrangement on an execution-only basis if the new arrangement does not involve extra borrowing other than to cover product or arrangement fees.

VULNERABLE CUSTOMER

Someone who is especially susceptible to detriment as a result of their personal circumstances, particularly when a firm is not providing appropriate levels of care.

✓

CHECK YOUR UNDERSTANDING 5

Based on the information provided, which of the following is most likely to be able to arrange a mortgage on an execution-only basis without receiving qualified advice?

a) Richard, who is an experienced mortgage adviser and wishes to arrange a further advance on his own property.

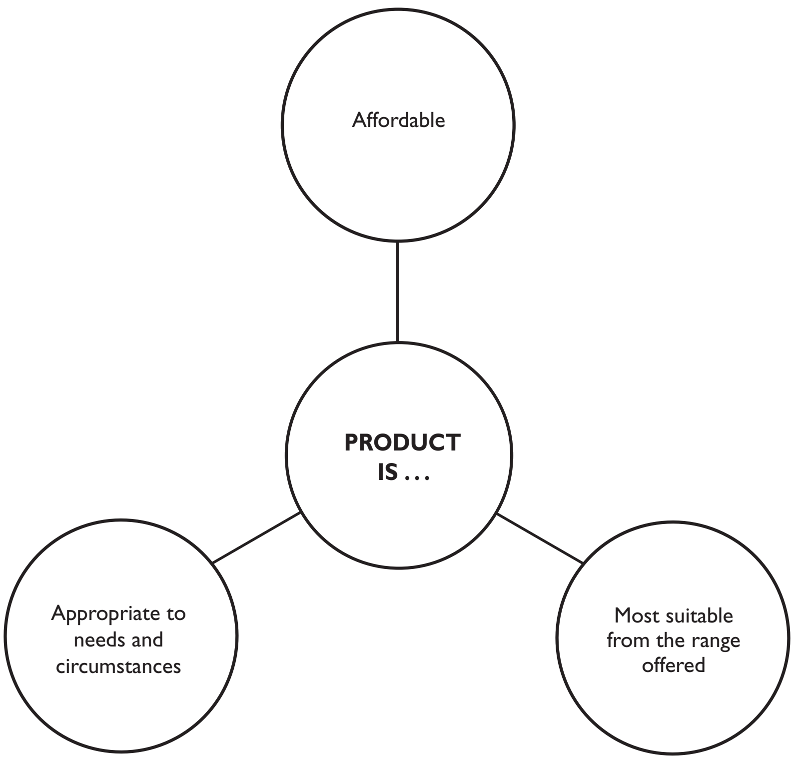
b) Shannon, who wants to buy her flat under a statutory right-to-buy scheme.

c) Niall, whose wife died last month and is seeking to relocate closer to his children.

8.4.2 What are the suitability requirements?

With advised sales, the firm must take reasonable steps to ensure that any personal recommendations are suitable for the client. This requires the adviser to gather information about the customer that will help them to assess which mortgage, if any, is suitable for the customer's needs and circumstances. The underlying requirements for a product to be deemed suitable are summarised in Figure 8.4.

FIGURE 8.4 SUITABILITY REQUIREMENTS



Where the firm offers more than one product that is appropriate to the borrower's needs and circumstances, and advises the borrower to take out a product other than the cheapest, it must explain why it is recommending the more expensive product. 'Cheaper' is defined as having a total amount payable that is lower than the other product.

RECORD OF THE RECOMMENDATION

A firm or adviser recommending an MCD regulated mortgage must provide the customer with a record of the recommendation made on paper or in another durable medium. This requirement can be met by providing an illustration or ESIS.

WHAT HAPPENS IF NO PRODUCT IS SUITABLE?

If there is no product within the range offered by the firm that is appropriate to the customer's needs and circumstances, no personal recommendation should be made. It is not acceptable to recommend a product from the range on the basis that it is the 'best fit' available.

RECORD-KEEPING

A firm must keep records demonstrating suitability, including information gathered relating to the customer's needs and circumstances, why the recommendation was suitable and any customer choices, such as adding fees to the loan.

The record must be kept for at least three years from the date of the advice.

8.5 What is responsible lending? (MCOB 11 & 11A)?

Lenders are required to meet the requirements of MCOB 11, which covers responsible lending. Before entering into the mortgage contract, or changing the terms of an existing contract that could affect affordability, the lender must be able to show that account has been taken of the borrower's ability to repay the mortgage. Examples of changing the terms of a mortgage include extending the term into retirement, changing from repayment to interest-only, or adding or removing a borrower.

A record must be kept of the information used by the lender in reaching a decision that complies with the responsible lending rules. The record will include the affordability assessment and, for interest-only mortgages, the reason for agreeing to the mortgage, the customer's repayment strategy and the result of the mid-term review required to check whether the repayment strategy is still on track and appropriate.

The record must be kept for the term of the mortgage. This contrasts with suitability records, which must be kept for three years.

The lender must establish and operate a written policy outlining the factors it will take into account in assessing the borrower's ability to repay the mortgage.

8.5.1 Income and expenditure

Lenders are required to obtain reliable evidence and verification to confirm that the income declared by the applicant is correct, and the lending decision should be based on that evidence. The rules specifically prohibit self-certification, where the applicant declares their own income and no evidence is sought to confirm their declaration. Instead, lenders must obtain evidence of income and it must be from a source independent of the customer, rather than from the customer themselves.

We will look in more detail at affordability in Unit 4.

8.6 Pre-application disclosure (MCOB 5 & 5A)

Pre-application disclosure is the information that must be provided before the customer completes an application for a regulated mortgage contract. The principle is that the customer should be in a position to make an informed decision. This means that they must be given sufficient information, specific to their case, to be able to make that decision. Illustrations and ESIS documents must only contain the information required by MCOBs and be separate from any other information given to the customer. The information must be specific to the customer's circumstances, the property and the required mortgage.

8.6.1 MCD regulated mortgages

The information provided must follow a prescribed format through an ESIS.

The following key information is required:

- The period for which the ESIS remains valid.
- The lender and contact details. Whether the firm has recommended a specific mortgage or provided information on a mortgage based on the customer's responses to questions so that they can make their own decision.
- The intermediary firm – name and contact details, where applicable. Whether the firm has recommended a specific mortgage or provided information on a mortgage based on the customer's responses to questions so that they can make their own decision. The exact amount of any commission or procuration fees paid to the intermediary by the lender or, if the amount is not yet known, a range of representative examples.

- Main features of the loan, including:
  - the amount and currency of the loan;
  - if the loan is in a foreign currency and the value of the loan in the borrower's home currency, and the potential impact of a fall in the borrower's home currency;
  - loan duration, type, interest rate and the total amount to be repaid;
  - the amount to be repaid per pound (or other currency) borrowed;
  - the amount owed at the end of the term, in the case of interest-only borrowing;
  - the property value, the maximum loan to value available or the minimum property value required to support the borrowing.
- Interest rate and other costs – the APRC applicable and an explanation of the costs used in the calculation. Where an exact cost is not known, the firm must provide an indication of the amount if possible, or, if not, how the amount will be calculated and specify that the amount provided is only an indication.
- Frequency and number of payments.
- The amount of each instalment, with a warning that the borrower's income could change and they need to consider whether they could still afford the repayments. Also, where applicable:
  - interest-only mortgages – the need to make separate arrangements to repay the mortgage at the end of the term, and add the cost of the arrangements to the mortgage payments;
  - variable rate mortgages – a warning that the interest rate could change and payments may fluctuate, with an example of the cost of an increase;
  - foreign currency mortgages – a warning that payments could vary if the value of the home currency changes, with an example of a 20 per cent fall in the currency;
  - details of tied savings products or deferred interest loans.
- Illustrative repayment table (where applicable), showing the breakdown of interest, capital and other costs for each payment, and the outstanding capital after each payment.
- Additional obligations which the borrower must comply with as part of the mortgage conditions.
- Early repayment – the borrower's right to repay the loan (or part of it) early, the conditions that would apply, and any early repayment (exit) charge.

- Flexible features (where applicable) – whether the mortgage can be transferred (ported) to another property, or the mortgage can be transferred to another lender. Any other features offered as part of the arrangement that are not covered elsewhere in the document.
- Other rights of the borrower – the availability and length of the reflection period.
- In the case of a retirement interest-only mortgage to release capital, the firm must inform the customer that taking out the mortgage may affect their tax and state benefit position, provide information on restrictions as to who may live in the property, and state that the customer should consider taking advice on the issues before applying. This information can be included in the illustration or as a separate document provided at the same time.
- Complaints – where to find the complaints procedure, and timescales for making a complaint. Reference to the Financial Ombudsman Service for unresolved complaints.
- Non-compliance with the commitments linked to the loan – the financial and/or legal consequences for the borrower. The need to contact the lender as soon as possible in the event of payment difficulty. A warning that the property may be repossessed on failure to maintain payments.
- Supervisor – the contact details of the FCA as the supervising authority.

If the advice is given by an intermediary, it is their responsibility to ensure that the information in the ESIS is accurate. The adviser must also explain to the customer the importance of reading and understanding the illustration. The lender cannot take any action to commit the borrower to the contract (application fees, etc) until the borrower has had time to consider the information.

FACTFIND

The detailed content of the ESIS is available in MCOB 5A Annex 1.

The ESIS must be provided to the customer as soon as possible after they have supplied the necessary information on their needs, financial situation and preferences, and in good time before they are committed to any mortgage offer or contract. In practical terms, this means before an application is made.

It must also be given if the customer requests the information (unless the firm is aware that the customer would not be able to obtain the mortgage), or in the case of an execution-only sale to indicate which contract the customer has chosen. If the terms of a proposed mortgage change materially between the provision of the ESIS, the firm must provide a revised ESIS before the application is made. The firm does not have to provide a revised ESIS if the change to the mortgage occurs after an application is made, but any changes must be reflected in the offer document.

If a recommendation is made over the telephone, the illustration must be sent to the customer within five business days.

8.6.2 Non-MCD regulated mortgages

When a customer with a regulated mortgage contract, pre-21 March 2016, wishes to vary the terms or arrange a further advance, the firm must provide them with an illustration that reflects the change. The document, referred to as a key features illustration (KFI) is broadly similar to the ESIS, but there are some differences. The main differences are:

- there is no reflection period;
- the offer is not subject to the MCD 'binding offer' requirement;
- the annual percentage rate (APR) is similar to the APRC but the calculation is slightly different.

As the MCD mortgage disclosure requirements contain broadly the same core information as that required for non-MCD mortgages, the lender may choose to adopt MCD processes to make administration simpler and avoid running two systems.

> **RECORD-KEEPING**
>
> The firm must keep a record of the ESIS or KFI for a period of one year from the date of the customer's application.

8.7 Disclosure at the offer stage (MCOB 6 and MCOB 6A)

Lenders are required to provide certain information to the borrower with the mortgage offer. The disclosure requirements apply only to lenders, although they affect advisers in that advisers need to be able to explain the details provided in the offer documents to their customers. The requirements for regulated mortgages and MCD regulated mortgages are broadly similar, but there some important differences.

8.7.1 MCD regulated mortgages

MCOB 6A details the rules applicable at the offer stage for an MCD regulated mortgage, either as a new mortgage contract or as a variation to an existing MCD mortgage contract.

Binding offer

The lender's final mortgage offer must be binding. This does not prevent a lender from making an offer that is conditional on the borrower meeting certain (lawful) requirements or the lender gathering further information. However, once all the requirements have been met to the lender's satisfaction and it is prepared to confirm the offer, that offer will be binding on the lender.

Note, however, that the requirement for a binding offer does not apply where the borrower is applying to vary an existing MCD contract.

WHAT CONDITIONS MIGHT A BINDING OFFER TYPICALLY INCLUDE?

- That there is no material change to the facts and circumstances on which the offer is based – the applicant's income or employment changing or the condition of the property deteriorating, etc.
- That the borrower has not knowingly provided inaccurate or false information or withheld information.

The lender may choose to provide an ESIS with the offer document, in which case the offer must reflect the details in the ESIS. If a binding offer contains conditions that differ from the ESIS provided at the application stage, a revised ESIS must be provided with the offer document.

Reflection period

When it has issued a binding offer, the lender must allow the borrower a reflection period of at least seven days, although the borrower can waive their rights to the full seven days and accept the offer at any time. During that period the offer remains binding on the lender. The principle of the reflection period is to give the borrower time to compare offers, consider their implications and arrive at an informed decision. Lenders and intermediaries are permitted to communicate with the borrower during the reflection period.

Note that where a borrower is applying to vary an existing MCD mortgage, the reflection period does not apply.

Content of the MCD offer document

There is no prescribed format for the MCD offer document, but the key information includes:

- the period for which the offer is valid;

- when the interest rate will change;
- the consequences of the customer not going through with the mortgage, including any fees already paid that will not be reimbursed;
- that there is no right of withdrawal once the mortgage is concluded;
- the customer's repayment strategy;
- where applicable, information about any retentions or reinspections that the lender may require;
- information about how to complain to the firm about its services relating to the mortgage, and whether or not such complaints can be referred to the FOS.

The following information must be provided either as an integral part of the offer document or as a separate document given with the offer document:

- A tariff of charges that could be incurred on the mortgage contract.
- Details of charges applicable to any current accounts, borrowing or deposit accounts linked to the mortgage.
- If the mortgage contract includes a credit card, the document must explain that the credit card will not provide the statutory rights associated with 'traditional credit cards'.

8.7.2 Regulated mortgages

MCOB 6 applies where the offer has been made to a customer with a view to:

- varying the terms of an existing regulated mortgage contract by:
  - adding or removing a party;
  - making a further advance;
  - switching some or all of the mortgage to a different interest rate option.

The offer document must contain a KFI (as described in section 8.6) and the offer must be based on the information contained in that illustration. The lender may choose not to provide a separate illustration, in which case the offer document must contain all the required information for an illustration. If the lender's final offer differs from the information included in the pre-application illustration, the illustration must be adapted to reflect the actual offer the lender is making.

Content of the offer document

The content of the offer document is broadly similar to the content of an MCD regulated mortgage, but must contain the statement: "You are not bound by the terms of this offer document until you have signed the legal charge and the funds are released for your mortgage". Note also that the lender's offer is not binding on the lender and can be withdrawn for a range of reasons.

As with other elements of disclosure, the core information applies to both regulated and MCD regulated mortgages. Lenders may choose to follow the requirements for MCD regulated mortgages in order to avoid having to run two systems.

RECORD-KEEPING

For both regulated and MCD regulated mortgages, a record of the offer document must be kept for one year from the date the offer was issued to the customer.

8.8 Disclosure at the start of the contract (MCOB 7)

MCOB 7 covers the disclosure requirements at the start of the contract and after it has started. In this section we will cover the requirements at the start of the contract. The ongoing requirements once the mortgage is in place are covered in Unit 6.

The lender is required to provide the following information before the first payment is made on a new mortgage, a further advance or a variation to the terms of a mortgage:

- amount and dates of the initial and ongoing mortgage payments;
- the method by which the payment will be collected;
- premiums and collection arrangements for any mortgage-linked investment/insurance contracts purchased through the firm;
- confirmation of whether the mortgage is interest-only, repayment or a combination;
- if the mortgage is interest-only, a reminder that the customer should check that any repayment vehicle is in place if it has not been provided by the firm;
- what the customer should do if they have payment difficulties or fall into arrears, and draw attention to the tariff of charges;
- confirmation of any linked borrowing and linked deposits; and
- whether the contract allows overpayments or underpayments.

MCOB 12 – Charges

MCOB 12 covers mortgage charges in general, and clarifies the requirements for disclosure of early repayment charges (ERC) in MCOB 5, 7 and 9. The lender is free to calculate the charge in a way that it chooses, but the charge must be a reasonable pre-estimate of the costs of ending the contract early and capable of being shown as a cash amount. In addition, when disclosing the ERC in accordance with MCOB 5, 7 and 9, the illustration must refer to such a charge as an early repayment charge and include:

- when an ERC would be payable;
- the basis of the calculation;
- the maximum ERC payable.

THINK AGAIN . . .

Now that you have completed this topic, how has your knowledge and understanding improved?

For instance, can you:

- summarise the sections of MCOB that apply to each stage of the mortgage application process?
- explain the difference between real-time and non-real-time financial promotions and the rules relating to each?
- summarise the purpose of the initial disclosure stage from the borrower's perspective?
- explain what is meant by 'execution-only business' and when customers are eligible to proceed on this basis?
- summarise the content of a KFI and explain how an ESIS differs from it?
- describe disclosure requirements at the start of the mortgage contract?

Go back over any points you don't understand and make notes to help you revise.

Test your knowledge before moving on to the next topic.

Reference

FCA (no date) *Durable medium* [online]. Available at: www.handbook.fca.org.uk/handbook/glossary/G1286.html

Test your knowledge

?

Use these questions to assess your learning for Topic 8. Review the text if necessary.

Answers can be found at the end of this book.

1) Which of the following is true in all circumstances in relation to unsolicited real-time financial promotions?

   a) They can only be made to existing customers.

   b) They cannot be made at an unsocial hour.

   c) Contact cannot be made on an unlisted telephone number.

   d) They can be made to any person who is on the company's mailing list.

2) Alex is his firm's marketing manager and he has just withdrawn a marketing mailshot, which will not be used again. For how long must his firm keep a copy of the mailshot?

   a) 6 months.

   b) 12 months.

   c) 36 months.

   d) 60 months.

3) For how long must a firm keep a record of an execution-only sale?

   a) One year.

   b) Two years.

   c) Three years.

   d) Five years.

4) A high-net-worth customer can proceed on an execution-only basis if the firm has evidence that the customer meets the criteria, and has selected the product they require or has rejected advice given. True or false?

5) If there is no suitable product for a customer from within the range available, the adviser can recommend the closest fit from those available. True or false?

6) Examples of the APRC shown in a financial promotion must be 'representative'. This means that what percentage of those who respond to the promotion and those who enter into the contract advertised would be charged the quoted APRC?

   a) 45 per cent.

   b) 51 per cent.

   c) 75 per cent.

7) If a recommendation is made over the telephone, an illustration must be sent to the customer within:

   a) five business days.

   b) seven business days.

   c) five calendar days.

   d) seven calendar days.

8) Lenders cannot make provisional offers to borrowers in relation to MCD regulated mortgages. True or false?

9) Chen has applied for an MCD regulated mortgage. Once he receives an offer from the lender, how long will he have to think about whether to accept it, according to MCOB 6A?

   a) No time limit.

   b) Five days.

   c) Seven days.

10) The offer document must include details of the amount and dates of the initial and subsequent repayments due. True or false?