TOPIC 9

The role of the mortgage adviser

LEARNING OBJECTIVES

This short topic focuses on the role of the mortgage adviser with the emphasis on providing ethical advice. We will look in more detail at how the adviser assesses affordability and suitability in Topics 10 and 11.

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

- the key stages in the mortgage advice process;
- the principle of giving ethical advice;
- fair treatment of customers as an example of ethical advice in practice.

THINK . . .

Before you start work on this topic, take a moment to think about what you already know about the role of the mortgage adviser.

For instance:

- What are the main steps in the advice process?
- What kinds of issue need to be considered to ensure the fair treatment of customers?
- Can you recall the six fair treatment of customers outcomes from your studies for UK Financial Regulation?

9.1 Introduction

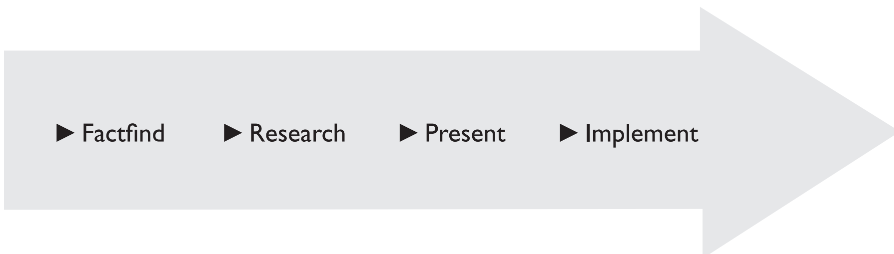
The mortgage market is often baffling for the average potential purchaser. Few people fully understand the complexities of the house-buying process, the mortgages available and the importance of choosing the most appropriate repayment method. This is where the mortgage adviser will play a pivotal part: they can inform and guide the customer towards the most suitable mortgage for their needs.

Advisers are expected to give ethical advice. This means asking appropriate questions to ascertain the customer's attitudes and needs, identifying the customer's full financial situation, verifying information where possible and offering advice and recommendations that best suit the customer. The customer's best interests should always be at the forefront of any advice or recommendations given.

We will look at the key elements of the adviser's role in the advice process and we will consider MCOB rules where they impact on that role. For consistency we will use the term 'adviser' to describe both a lender's adviser and an intermediary (mortgage broker).

The primary requirement of the advice process is that any recommendation should be suitable for the customer's needs. This is also essential for developing and maintaining the customer relationship and the adviser's reputation.

FIGURE 9.1 WHAT IS THE ADVICE PROCESS?



9.2 Compiling the factfind

The adviser should first interview the customer to find out as much relevant information as possible. In most cases, the adviser will need to explain terminology, products and procedures so that the customer can give reasoned and informed answers.

FIGURE 9.2 WHAT WILL THE FACTFIND INTERVIEW COVER?

Intentions
- The customer's intended purchase price and the type of property to be purchased

Income and outgoings
- The customer's income and outgoings to determine how much they can comfortably afford to borrow

Deposit and cash
- The amount of deposit available and other cash available to meet expenses

Employment
- The customer's current employment status and history
  - Eg they might be on a career path that will lead to higher income, perhaps on passing exams or achieving benchmarks; this could help future affordability
  - Or have there been any redundancies or cutbacks at work recently?

Management of finances
- How the customer manages their finances: if their bank account is usually in credit, this shows an ability to manage finances; if it is often overdrawn, it might suggest difficulty with financial management

Budget and rate rises
- The customer's budget and their ability to cope with potential rate rises in the future
  - Particularly relevant where the customer is looking to borrow the maximum available, leaving them with little or no spare income; or where the customer is considering a fixed, capped or discount rate in the initial years because the payments may increase significantly at the end of the initial term
  - Whether they need to start at the lowest possible cost via a discounted mortgage

Early repayment
- The potential/intention for the customer to make early repayments – partial or total

Term
- The customer's feelings about the term of the mortgage

Protection needs
- Protection needs that will arise when the mortgage is arranged – life cover, critical illness cover, mortgage payment protection and so on (assuming the adviser has the appropriate authorisation to advise on these products)

Attitude to risk
- The customer's attitude to risk in relation to mortgages
  - Normally takes the form of a risk questionnaire resulting in a risk profile

The information gathered will establish two key factors:

- how much the potential borrower can afford each month; and
- the type of mortgage they would prefer.

Much of the information will be similar to that required on a mortgage application form, although it might not cover as much detail. The better the quality and accuracy of the information gathered at this stage, the greater the chances of a successful mortgage application. In many cases the adviser will approach a lender before submitting an application to establish whether a mortgage is likely to be agreed. If the initial information given to the lender proves to be inaccurate once a formal application is made, the final decision could be different. This would cause distress to the applicant and embarrassment to the adviser.

9.3 Researching the solution

The next stage is for the adviser to identify the most suitable product to meet the customer's needs, preferences and affordability, as identified through the factfind. The adviser must be able to show clearly how the product that is being recommended meets the client's precise needs and objectives. We will look at affordability and suitability in detail in Topics 10, 11 and 12.

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CHECK YOUR UNDERSTANDING 1

From your studies in Topic 8, can you recall the three categories of service that a firm may offer to a customer when recommending a product?

9.4 Presenting the recommendation

Having decided on the most appropriate mortgage for the customer, the adviser presents their recommendation.

IN BRIEF

ESIS AND KFI

Remember: an ESIS must be provided for an MCD regulated mortgage, which will represent all new mortgages. A KFI must be provided for a regulated mortgage, which will apply to changes to mortgages originally taken out before 21 March 2016.

Ultimately, the decision to go ahead is the customer's responsibility, but this should be an informed decision, which means the adviser should ask the customer to read the information and then explain the key details, rather than leaving the customer to read it later. The explanations should be in language that the customer can easily understand, without unnecessary use of technical jargon. It is vital that the client fully understands why the product is being recommended and that they are encouraged to ask any questions or express any concerns so that these can be addressed properly.

Once the customer is clear on the technicalities, advantages and potential drawbacks of the mortgage, they can make a decision.

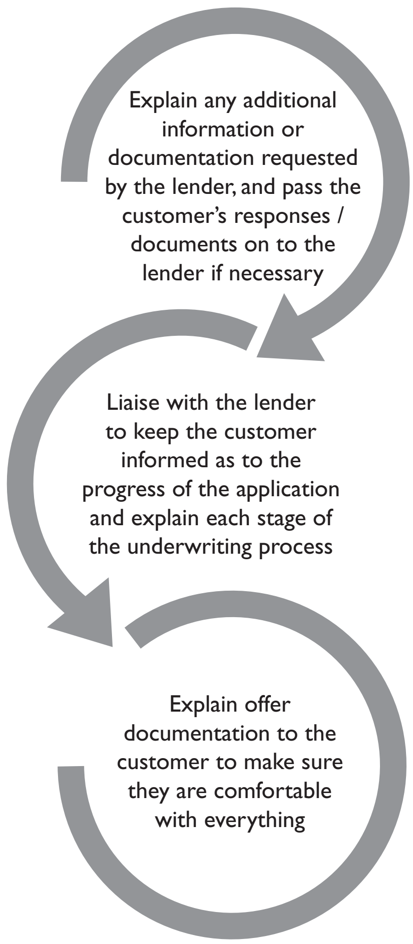
CHECK YOUR UNDERSTANDING 2

In Topic 8, we saw that for an MCD regulated mortgage, the adviser must provide adequate explanations of the recommended product. In addition to providing the ESIS, what does this entail?

9.5 Implementing the recommendation

Once the customer has made the decision, it is the adviser's responsibility to start the application process. Once the application has been completed and submitted to the lender, the lender will take responsibility for underwriting the application. However, the adviser will still have a role in liaising between the customer and the lender, and helping the customer through the process.

FIGURE 9.3 HOW DOES THE ADVISER CONTINUE TO LIAISE WITH THE CUSTOMER?



9.6 Principles of ethical advice

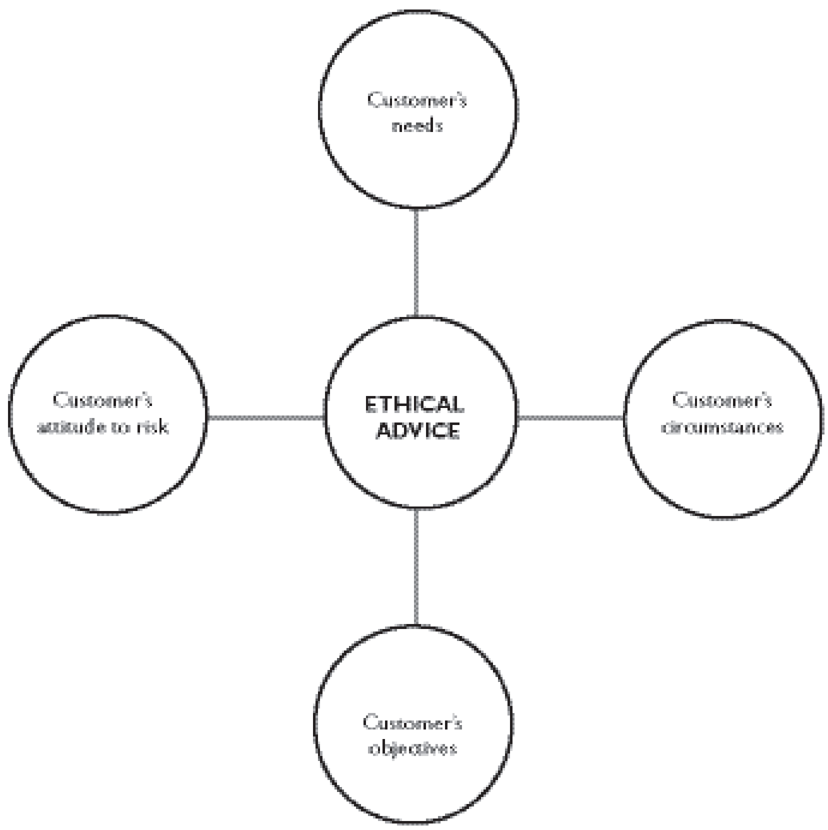
The mortgage adviser has a great deal of responsibility, as their advice will result in the client taking on a long-term commitment. Getting it wrong could cause major problems and distress for the customer, and lead to negative consequences for the adviser. Ethical advice is based on what is best for the customer in view of information known at the time, regardless of the needs of the adviser. For example, the adviser should not be influenced by commission or bonus payments that they might receive for selling certain products.

ETHICS

Conscious decisions taken by individuals and groups based on moral values; distinguishing right from wrong and choosing to do what we believe to be right.

The information the adviser needs to establish is summarised in Figure 9.4. Attitude to risk is an important consideration, as some mortgage products involve a greater element of risk than others. For instance, the uncertainty of how future interest rate movements will affect the monthly payments on a capped or discounted mortgage must be weighed against the certainty provided by a fixed-rate product.

FIGURE 9.4 WHAT DOES THE ADVISER NEED TO ESTABLISH?



It is almost impossible to impose ethical values through legislation and detailed rules; instead, the regulator provides guidelines as to what constitutes ethical behaviour and promotes examples of good practice. The principles of responsible lending are one example. The fair treatment of customers initiative that you studied in UK Financial Regulation is another, and we will revisit it here because it is central to the ethical provision of advice.

9.6.1 Fair treatment of customers

The FCA's fair treatment of customers initiative, originally referred to as treating customers fairly, is a key element of one of its objectives: to secure an appropriate level of protection for consumers. This has been enhanced by the FCA's introduction of the Consumer Duty, which provides firms with a number of specific obligations.

There are no specific rules relating to fair treatment of customers, although it is implicit in several conduct of business rules and the FCA's regulatory guidance includes The Responsibilities of Providers and Distributors for the Fair Treatment of Customers (RPPD). Additionally, the FCA publishes its six outcomes for the fair treatment of customers, forming part of the regulator's core supervisory work with firms. The FCA assesses firms' ability to deliver the six outcomes and the FCA Consumer Duty goes further.

FCA Principles 6 and 7 have particular relevance to the fair treatment of customers. With the establishment of the new Principle 12, and in view of the degree of overlap between the principles, the FCA has clarified that where Principle 12 applies to a client, Principles 6 and 7 are disapplied. In other words, Principle 12 overrides Principles 6 and 7. Principle 12 applies to retail clients, so Principles 6 and 7 still apply to non-retail clients.

IN BRIEF

FCA PRINCIPLES FOR BUSINESSES

In UK Financial Regulation you looked at the FCA's Principles for Businesses. Eight of the principles are especially relevant to the fair treatment of customers:

Principle 1: A firm must conduct its business with integrity.

Principle 2: A firm must conduct its business with due skill, care and diligence.

Principle 3: A firm must take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management.

Principle 6: A firm must pay due regard to the interest of its customers, and treat them fairly.

Principle 7: A firm must pay due regard to the information needs of its clients, and communicate information to them in a way that is clear, fair and not misleading.

Principle 8: A firm must manage conflicts of interest fairly, both between itself and its customers and between a customer and another client.

Principle 9: 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 judgement.

Since 31 July 2023, Principle 12 applies under the Consumer Duty:

Principle 12: A firm must act to deliver good outcomes for retail customers.

FACTFIND

If you would like more information on the regulatory guidance available, the Responsibilities of Providers and Distributors for the Fair Treatment of Customers is provided as part of the FCA Handbook at: www.handbook.fca.org.uk/handbook/RPPD/link/?view=chapter.

Further information on the FCA's expectations in relation to fair treatment of customers is available at: www.fca.org.uk/firms/fair-treatment-customers.

9.6.2 What does fair treatment of customers mean practically?

In the process of gathering information and building a picture of the client's personal and financial circumstances, an adviser must bear in mind at all times that they must do what is best for the client.

This could mean that an adviser recommends a product that is entirely different from the one in which the client initially expressed an interest, or that the client thought would be suitable for their circumstances. It may occasionally mean that the adviser advises against a certain product, such as a flexible or offset mortgage, because they do not feel that the client is sufficiently knowledgeable or sophisticated in financial matters to handle the account in a way that would best serve their needs.

With regard to certain specialist home finance products, such as Islamic home finance, the adviser needs to take into account the motives behind selecting such a product, for example the borrower's beliefs with regard to interest payments and their preferences concerning associated products such as insurance. This consideration must continue with any documentation or communications between the lender or adviser and their clients, taking care that they are consistent with the discussions that have taken place.

If the recommended mortgage is not the firm's cheapest appropriate contract, the firm must explain why the more expensive mortgage has been recommended.

9.6.3 A new Consumer Duty

In May 2021, the FCA published a consultation paper (CP21/13) *A new Consumer Duty*, which aimed to "set clearer and higher expectations for firms' standards of care towards consumers". The final rules and guidance were published in July 2022, with the Duty coming into force from 31 July 2023 for new and existing products and services available for sale or servicing, and 31 July 2024 for closed-book products. The Duty represents a further move towards outcome-based regulation and away from a process-focused 'tick box' mentality. Senior management are required to take a proactive approach, with a focus on ensuring products and services really meet the needs of customers who buy them. It aims to "ensure a higher and more consistent standard of consumer protection for users of financial services and help to stop harm before it happens" (FCA, 2021).

As firms will be expected to assess how customer needs are met, the FCA will be able to identify and take action against practices that fail to deliver the right consumer outcomes before they become normal market practice.

The Duty applies to products and services offered to 'retail customers', such as MCD regulated mortgages, and applies to firms forming part of the distribution chain whether or not there is a direct relationship with the buyer. It does not apply to institutional investors, professional clients or eligible counterparties.

There are three key elements to the Consumer Duty:

- **A consumer principle (Principle 12)**: "A firm must act to deliver good outcomes for retail customers".
- **Three cross-cutting obligations**, which develop the overarching expectations from Principle 12. Firms must:
  - act in good faith towards retail customers;
  - avoid causing foreseeable harm to customers;
  - enable and support retail customers to pursue their financial objectives.
- **Four outcomes**, which provide a set of rules and guidance to detail the expectations for the key elements of the firm–consumer relationship:
  - **Products and services** – products and services are specifically designed to meet the needs of consumers and sold to those whose needs they meet. This includes processes for the testing and approval of new products, a requirement for products to meet the needs of target markets, reviews of products and their risk to the target market, and distribution channel arrangements.
  - **Price and value** – firms must ensure products provide fair value for customers.
  - **Consumer understanding** – applies at all stages of the product cycle. Communications equip consumers to make effective, timely and properly informed decisions about financial products and services. The outcome covers key requirements to consider for customer communications, including customer characteristics and information needs, customer understanding, product complexity, accuracy, relevance and timeliness.
  - **Consumer support** – firms must ensure an appropriate standard of customer service support to meet the needs of retail customers, so they can realise the benefits of products and services and act in their

interests without undue hindrance. Firms must ensure that customers can use the product as reasonably anticipated and ensure they do not face unreasonable barriers when they want to make changes, transfer to a new provider, make a claim, cancel or complain.

There is a degree of overlap between the requirements of the new Principle 12 and the existing Principles 6 (Consumer interests) and 7 (Communication with clients), although Principle 12 is wider ranging and is supported by detailed rules and guidance in the Handbook.

As well as new contracts, Principle 12 and the Consumer Duty apply to all retail contracts in existence on 31 July 2023. Firms will not be required to relinquish or change any contractual rights in order to meet the obligations, although they can choose to do so. In this case, where appropriate, firms will need to find other ways to ensure they prevent harm to the customer.

The requirements of Principle 12 also include firms in the distribution chain that do not have a direct relationship with the client but could affect the consumer outcomes. Where Principle 12 applies, it effectively replaces Principles 6 and 7. Principles 6 and 7 will continue to apply in areas not covered by Principle 12, such as services to professional clients.

FACTFIND

You can read the FCA’s feedback to CP21/13 and the final rules and guidance at the following links:

www.fca.org.uk/publication/finalised-guidance/fg22-5.pdf

www.fca.org.uk/publication/policy/ps22-9.pdf

THINK AGAIN ...

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

For instance, can you:

- summarise the stages in the advice process?
- outline the areas that need to be discussed as part of the factfind?

- state the fundamental principle that underpins the provision of ethical advice?
- state the six outcomes for the fair treatment of customers?
- explain how fair treatment of customers applies in practice to the advice process?

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 (2021) *FCA to introduce new Consumer Duty to drive a fundamental shift in industry mindset* [online]. Available at: www.fca.org.uk/news/press-releases/fca-introduce-new-consumer-duty-drive-fundamental-shift-industry-mindset

Test your knowledge

?

Use these questions to assess your learning for Topic 9. Review the text if necessary.

Answers can be found at the end of this book.

1) The primary requirement of the advice process is that:

   a) the product recommended should be the best fit to the customer's needs from the range available.

   b) the amount of time the adviser invests in the customer should be reflected in the commission earned.

   c) the customer should be sold the product they ask for.

   d) the recommendation should be suitable for the customer's needs.

2) If a mortgage adviser asks a customer about the age at which they expect to retire, this is most likely to be so that the adviser can:

   a) ascertain whether the type of property the customer is interested in buying is suitable for them.

   b) recommend an appropriate term for the mortgage.

   c) ensure that the customer can afford the repayments from their pension income.

   d) establish whether the customer is good at long-term planning.

3) Why might an adviser want to know about a customer's future career plans or expectations of promotion, as well as their current situation?

   a) It might influence the price of a product.

   b) It might influence a mortgage lender's decision.

   c) It might influence the type of product the adviser would recommend.

4) What are the four key pieces of information that an adviser needs from their customer in order to provide a recommendation that meets the customer's needs?1)

   a) Wants, circumstances, objectives and attitude to risk.

b) Needs, circumstances, objectives and attitude to risk.

c) Needs, wants, circumstances and attitude to risk.

5) The Consumer Duty includes three 'cross-cutting' obligations, which develop the overarching expectations from Principle 12. Which of the following is **not** one of them? Firms must:

a) act in good faith towards retail customers.

b) avoid causing foreseeable harm to customers.

c) enable and support retail customers to pursue their financial objectives.

d) ensure products provide fair value for customers.