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Mortgage Advisers

MARCH 2008 NEWSLETTER

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This newsletter focusses on the information that came out of the four thematic reviews on mortage advice we carried out during 2007. We published the findings on our website in November of that year.

More detail and resources for firms to use are at:

www.fsa.gov.uk/Pages/Doing/small_firms/mortgage/practice/roadmap/index.shtml

This information adds to the significant amount of information which we have made available to firms as part of our ongoing work looking at quality of advice processes.

You are free to copy the good practices shown here and on our website, but our primary intention is to provide firms with the material they need to see how others work, to make comparisons, and to identify the scope for improvement in their own processes.

Senior management responsibilities

We found that that firms that have failings in their senior management responsibilities had significant failings elsewhere.

Senior management responsibility goes to the heart of how a firm is managed.

We expect the senior managers of all firms to assess the type of business undertaken by their firm and ensure they have appropriate procedures to prevent, identify and address any risks to the firm and its customers. This can be achieved by making full use of the management information available to them.

Management information (MI)

These examples of good and poor practice should help you understand our requirements in this area.

Good practice

Senior management (SM) get regular reports which are accessible and well presented so that it is possible to analyse and check for trends and risks.

For example:

- You have a detailed New Business Register (NBR) and use this to inform your compliance and not just to record sales.

- Firms' management information raises understanding of the business activities undertaken, such as the spread of lenders used and the nature of the sale (self-cert mortgages, lending into retirement, interest only mortgages, etc).
- Information is collated and reviewed for each individual adviser and the firm as a whole.

You use this information to identify potential areas of risk to customers and/or the firm. And you take appropriate follow-up action as necessary, including a review of your mortgage-advice process.

Poor practice

- SM have no understanding of what MI means and have not thought about how MI can help them 'know their business'.
- If they do collect MI they use it purely to analyse sales revenue.
- SM record very limited information on their NBR which means they are unable to draw-off relevant MI.

Monitoring

Good practice

SM have monitoring processes both in relation to their advisers and the business written which they are using to identify risks and trends.

Examples:

- SM extract information from key performance indicators (KPIs).
- Firms look for any trends suggesting a correlation between sales and commissions payable.

SM analyse (for example, by lenders, product types, repayment method, persistency etc) and use information gathered to develop a risk profile that concentrates quality-of-advice reviews on areas where they will be most effective.

Where issues are identified SM make sure that corrective action has been carried out.

The selection of files for checking is risk based rather than random.

Where a compliance consultant produces relevant and appropriate recommendations, SM have implemented all action points and has documentary evidence to support this.

Demonstrating suitability

Good practice

- All firms ensure their communications are clear, fair and not misleading.
- SM ensure that adequate information is held on file to demonstrate the suitability of the recommendation made to the customer.
- SM reviews the quality of any suitability letters to ensure the letter gives a meaningful description of the recommendation made.

Poor practice

- Firms rely on sourcing system printouts to demonstrate suitability when these bear no resemblance to the product recommended.
- Generic paragraphs used in a suitability letters to explain why the product was recommended rather than addressing the individual's needs and circumstances.
- The suitability letter is inconsistent with the information on the file and does not make sense.

Affordability

The problems we found included the following.

- Advisers did not consider affordability after the point the mortgage term ran into retirement;
- Advisers included irregular income (such as bonuses) as a guaranteed annual sum;
- There were cases where outgoings were not plausible; and
- Advisers recommended interest-only mortgages on the grounds of affordability without a plan for repayment.

Good practice

- Advisers verify the accuracy of outgoings such as household and lifestyle expenditure.
- The adviser and customer use a budget planner to determine and record disposable income.
- Advisers calculate a 'buffer zone' to allow for contingencies. This may include an allowance for rate increases.
- Firms keep proof of income on file, especially in fast-track cases.
- Firms make sure Right-to-Buy customers understand they may pay more for their mortgage than they have previously paid in rent.

Poor practice

- Instead of assessing affordability, advisers get the customer to sign a declaration that they could afford the mortgage. This does not remove a firm's responsibilities.
- Advisers decide affordability on "hunches" rather than recorded facts.
- Advisers assess affordability only for new customers not for customers remortgaging or taking out a new loan.
- Firms fail to assess the mortgage's affordability at the end of a fixed term.
- Firms rely on the lender's affordability criteria only.
- Advisers continue broking a with-advice mortgage after the customer refused to disclose their outgoings.
- Advisers do not assess affordability at the SVR on the expectation customers on a lower rate deal will be able to get another deal and never have to go on the SVR.
- Advisers use pre-tax income to make the mortgage appear affordable.
- Advisers took no steps to verify income when the amounts did not appear plausible for the customer's occupation or did not match payments coming into their bank account.
- Firms asssesed affordability on the customer's future expected earnings, without checking the likelihood of getting a particular job or confirmation of a starting date.
- Firms ignored the need for the customer to make payments on unsecured debt when recommending a debt consolidation mortgage for other debt.

Self-certification

Gathering information

As part of the fact finding or Know Your Customer process, firms should collect and record adequate information about a client's circumstances to:

- establish if a client needs to self certify, or could prove income and have access to full status products;
- be satisfied that the information provided about income is plausible;
- as for all advised mortgage sales, assess affordability; and
- ensure that the product being recommended is suitable.

At any point during this process information could come to light to enable the client to have access to full status products.

Could the client be full status?

A client may indicate they want to self-certify, but a broker still needs to establish if this is the most suitable route to take. This involves discussing with a client whether proof of income is available and explaining that producing this may mean they will have access to full-status mortgages that might be more suitable and have more favourable terms.

Various documents could be used to help prove income such as:

- P60s;
- available payslips;
- accountant's or employer's letter confirming income;
- management accounts;
- self-assessment tax forms; and
- benefit documents.

If a client is unable to prove income, a self-certification product may be suitable.

Is the income plausible?

During the discussion, the broker should obtain and record information about a client's employment, and income and expenditure patterns to establish if there are reasons to doubt plausibility and to assess affordability.

A firm can rely on information a client gives it unless, taking a common sense view, it has a reason to doubt it. However it is the firm's responsibility to ask clients the right questions in order to source a suitable product and to assess affordability. To achieve this, you should discuss:

- employment type;
- income, including a breakdown of income figures for various sources (such as basic salary, overtime/bonuses/relocation payments/benefits);
- frequency and reliability of income;
- net profit for self employed clients;
- proportion of profit if client is part of a partnership;
- drawings from limited companies, for example by speaking to the client's accountant; and
- representative income if a company director's profits vary from year to year.

Firms should also consider what other information the client may have provided. For example where a bank statement is provided for identification purposes, the information could be reviewed to gauge income or expenditure. Firms need to determine the plausibility of information not only to avoid the possibility of fraudulent applications being submitted with inflated incomes and to manage money-laundering risks, but also to recognise that if this happens, the affordability assessment will be fundamentally flawed.

Can the client afford the mortgage?

Even if the client is self certifying their income this does not alter the fact that the broker is responsible for ensuring that the mortgage recommended is affordable; if it is not affordable, it is not suitable.

Training and Competence

Our review showed that:

- recruitment and induction of advisers is generally handled well; and
- supervision and training are not.

Recruitment

Good practice

- A recruitment policy is in place to ensure that the individual is suitable for the role.
- Roles and responsibilities are clearly established and documented.
- An appropriate initial training plan is in place.
- Previous employer references are sought and kept for an appropriate length of time.

  These include:

  - quality of business completed;
  - competence status; and
  - complaints and disciplinary history.
- Credit checks or other fit and proper checks are completed on appointment and then at least once a year.

Poor practice

- Firms appoint new recruits without carrying out appropriate checks (eg they are family members, friends or acquaintances).
- Personal references are accepted where workplace references should be available.
- Firms leave the recruitment process entirely to consultants. Then they do not see the references received or the checks carried out on their behalf.
- No evidence of suitability for role exists.
- Training needs of new recruits are not identified or recorded.

Supervision

Good practice

- Firms have procedures to ensure that supervisors are properly trained and competent.
- There are clear criteria and procedures for assessing competence of advisers.
- There are measurable benchmarks for development of non-competent staff to competence and clear timescales for this to happen.
- Knowledge is tested and weaknesses are followed up.
- As well as knowledge, questioning, advising and presentation skills are assessed.
- Firms keep records of observations or development points and follow these up where appropriate.
- Key Performance Indicators (KPIs) include quality measures such as take-up rates, business mix, results of file checks, tests, observations and complaints.
- New advisers' competence is assessed under supervision before they work independently.
- Competence is re-assessed regularly and the results are used to influence the level of supervision.

Poor practice

- Simply passing an exam is seen as achieving competence.
- Key Performance Indicators are based only on sales figures.
- Once staff have been assessed as competent no further asessments are carried out.
- Advisers who are also senior managers receive no supervision or competence assessments.

- Demonstrating a specific number of hours of Continuous Professional Development (CPD) is accepted as a proof of competence.
- The quality of advice provided to clients by competent staff is not assessed
- No failure policy exists so there is no defined strategy for dealing with advisers who fall below the standard required by the firm.
- Supervision is not risk based. It takes no account of the skills, experience and knowledge of advisers or the complexity and risk involved with products being recommended.
- Supervision and assessments are too infrequent or too poor in quality to identify risks or training needs.

Qualifications and training

Good practice

- A training plan exists for the forthcoming year with time scheduled in advance for team meetings and training events.
- Advisers are encouraged to obtain higher qualifications and to improve their knowledge and skills.
- Complex cases are discussed in recorded training events.
- A variety of training and assessment methods are used for developing competence such as:
  - sitting a relevant mock exam;
  - product and market training; and
  - practical training such as mock sales interviews.
- The firm ensures appropriate examinations are taken and passed within a reasonable timescale.
- Effectiveness of training is regularly evaluated.

Poor Practice

- Training needs identified during quality of advice checks or sales observations are not addressed by action plans.
- Staff are not encouraged to read the trade press or to attend FSA or industry events. They are not encouraged to regularly review www.fsa.gov.uk and other relevant websites.
- The firm does not provide training opportunities or make use of training provided by training providers.