Safe as houses

What does the Mortgage Market Review mean for today’s aspiring home-owners?

An extract from Perspective: The Responsible Lending Issue
Essential insights into the issues facing your industry today
Perspective invited Roy Armitage, Head of Risk at Kensington Mortgages, to reflect on mortgage lending in the post-MMR environment.

In the beginning
The Mortgage Market Review, or MMR as we have come to know it, began as a Consultation Paper by the then FSA in 2009, setting out proposals for a new mortgage regulatory framework. Should we forget, it was the mortgage industry as a whole that was said to have largely created the financial crisis in 2008 by lending to those who could not afford the loan they had applied for: the MMR was the regulators’ response to bring improved standards of lending practice into the industry.

Nearly three years of consultation with the industry followed to ensure the proposals were both proportionate and workable, and in the interests of a fair and sustainable mortgage market as well as consumers. In October 2012, the FSA issued a final Policy Statement encompassing the new rules and it is these rules that were introduced by the Financial Conduct Authority (as it is now known) on 26th April 2014.

All change
These new Mortgage Conduct of Business rules represent the biggest shake-up of the mortgage industry since Mortgage Day (M Day) in 2004, when the FSA first started regulating the market. Two of the most prominent changes as part of the MMR have already received a great deal of media and industry coverage:

The removal of the non-advised sales process
Most interactive sales, such as face-to-face or on the telephone, now need to be advised and go through a full advice process, with every seller required to hold a relevant mortgage qualification. An ‘execution only’ process will only be allowed for certain non-interactive sales, including those carried out on the internet or through the post and, where applicable, applications from industry professionals and high net worth individuals.

A comprehensive affordability assessment
Lenders will be fully responsible for assessing whether the customer can afford the loan, including a much more detailed consideration of personal outgoings at the application stage.

Significant debate has taken place within the industry regarding how valid this new affordability assessment is and whether it’s necessary, but on reading consumer reaction to the MMR announcements, the general view seems to be summed up as ‘Why would a lender not try and ensure I can pay my mortgage? It’s in my interests and is surely common sense.’

Growing interest
The other key area around affordability is for lenders to demonstrate the ability of the customer to withstand interest rate increases, based on an independent view of forward rate curves. Whilst this provision is new, most lenders have been stress-testing their affordability calculations for some years; Kensington certainly has. One thing that has not changed with MMR is the type of information a lender uses to validate income and verify affordability. This remains the lenders’ choice, so long as they are able to justify the approach they take.

Lenders like Kensington will, therefore, continue to be able to make lending decisions based on their judgement of the customer’s circumstances and some of the more extreme predictions regarding ‘excluded customers’ following the implementation of the MMR are most likely to be proved incorrect.

This means, for example, that Kensington’s underlying lending policy for the self-employed remains unchanged, as long as we believe that the lending decision remains demonstrably transparent, compliant and responsible.

Entrepreneur central
This, of course, is good news for the nation’s growing army of self-employed workers and other potential borrowers whose circumstances are not straightforward and who need a carefully considered and individual approach.

One of the most striking features of the economic recovery is, according to the Bank of England, the record 4.5 million Britons who are now self-employed. The Bank says that self-employment rose by more than 200,000 in the three months to January and accounted for almost half of the rise in employment since 2010.

Work and Pensions Secretary, Iain Duncan Smith was quick to jump on these figures, proclaiming: “This country has a great history of entrepreneurship and small businesses are in many ways the backbone of the UK economy.”

He went on to say that the entrepreneurial spirit is alive and well in the UK – and no part of society, it seems, is immune from the entrepreneurial bug.
According to the Office for National Statistics, those aged 50 and over have accounted for more than 70% of the increase in the number of self-employed since 2008, while the New Enterprise Allowance claims to have helped more than 40,000 former benefits claimants to start new businesses since 2011. Additionally, nearly two-thirds of mothers with children under 10 are looking to become ‘entrepreneurs’ by starting a business from home in the next three years, according to research by an insurer.

**Responding to demand**

This demographic shift towards self-employment does not look like it will be slowing down any time soon and, as long as these customers can properly demonstrate affordability through a clear document trail, lenders who have the appetite can grow their self-employed business accordingly.

One new dilemma for lenders is that they will increasingly be unable to validate self-employed income using SA302s alone. This is because HMRC has made it clear this is not a reliable source of income data as it is effectively self-declared, even though SA302s have been used successfully by lenders for many years prior to the MMR.

MMR has changed the way we do many things, but it has not hampered, and will not hamper, our ability to provide self-employed customers and other customers with unusual circumstances with mortgages that are appropriate to their circumstances. This is a good outcome from the new regulations and excellent news for all our customers.

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