Chapter 11

Responsible lending, and responsible financing of home purchase plans
11.4 Application

Who?

11.4.1 R
This chapter applies to a firm in a category listed in column (1) of the table in MCOB 11.4.2 R in accordance with column (2) of that table.

11.4.2 R
This table belongs to MCOB 11.4.1 R

<table>
<thead>
<tr>
<th>(1) Category of firm</th>
<th>(2) Applicable section</th>
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<tr>
<td>mortgage lender</td>
<td>Whole chapter</td>
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<tr>
<td>home purchase provider</td>
<td>Whole chapter except MCOB 11.6.1G (2), MCOB 11.6.5R (3) and (4), MCOB 11.6.18 R, MCOB 11.6.19 G, MCOB 11.6.20R (2) and MCOB 11.6.20R (9), MCOB 11.6.40 G to MCOB 11.6.59 G, MCOB 11.6.60R (2)(e), (3) and (4), MCOB 11.7.3R and MCOB 11.9.</td>
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<td>mortgage administrator</td>
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What?

11.4.3 R
This chapter applies:

1. if a firm enters into a regulated mortgage contract or home purchase plan with a customer; or
2. if a firm varies an existing regulated mortgage contract or home purchase plan; and
3. throughout the term of any regulated mortgage contract or home purchase plan which a firm has entered into.
11.5 Purpose

11.5.1 (1) This chapter requires a firm to treat customers fairly by assessing, before deciding to:

(a) enter into a regulated mortgage contract or home purchase plan; or

(b) vary a regulated mortgage contract or home purchase plan;

whether the customer will be able to repay the sums borrowed and interest (in the case of a regulated mortgage contract) or pay the sums due (in the case of a home purchase plan).

(2) This chapter aims to ensure that customers are not exploited by firms that provide finance in circumstances where the customers are self-evidently unable to repay (or pay) through income and have no alternative means of repayment (or payment).

(3) This chapter sets out some limited exceptions to the requirement to assess the customer’s ability to repay (or pay), including transitional arrangements in relation to customers with existing regulated mortgage contracts or home purchase plans which satisfy certain conditions.

(4) This chapter also applies in relation to extending the term of a bridging loan.
11.6 Responsible lending and financing

Contents of this section

11.6.1 G
(1) This section sets out rules and guidance for lenders and providers under regulated mortgage contracts and home purchase plans, in relation to the assessment of affordability for the customer of these contracts. Firms have the option of applying certain of the rules and guidance on a modified basis in relation to regulated mortgage contracts and home purchase plans which are solely for a business purpose or are with high net worth mortgage customers. This section also contains (at MCOB 11.6.41 R to MCOB 11.6.52 G) additional rules, with accompanying guidance, in relation to regulated mortgage contracts which are interest-only mortgages. These rules:

(a) restrict the circumstances in which interest-only mortgages may be entered into, and impose additional requirements on mortgage lenders in those limited cases where they are permitted; and

(b) provide for an exception to the requirement to assess affordability in relation to those interest-only mortgages which are interest roll-up mortgages, and restrict the circumstances in which interest roll-up mortgages may be used (see MCOB 11.6.57 R to MCOB 11.6.59 G).

(2) This section also contains (at MCOB 11.6.53 E to MCOB 11.6.54 G) special provisions for mortgage lenders in relation to bridging loans, including some which apply only where the bridging loan is an interest-only mortgage.

The assessment of affordability

11.6.2 R
(1) Except as provided in MCOB 11.6.3 R, MCOB 11.6.57 R (Interest roll-up mortgages) and MCOB 11.7 (Transitional arrangements):

(a) before entering into, or agreeing to vary, a regulated mortgage contract or home purchase plan, a firm must assess whether the customer (and any guarantor of the customer’s obligations under the regulated mortgage contract or home purchase plan) will be able to pay the sums due; and

[Note: article 18(1) of the MCD]

(b) the firm must not enter into the transaction in (a) unless it can demonstrate that the new or varied regulated mortgage contract or home purchase plan is affordable for the customer (and any guarantor).
(2) In MCOB 11.6, references to payment of sums due means:

(a) in the case of a regulated mortgage contract, the making of the payments to repay the sums advanced and interest reasonably expected to be accrued under the regulated mortgage contract; and

(b) in the case of a home purchase plan, the payment of sums due under the home purchase plan;

in each case as they fall due.

(3) In MCOB 11.6, references to the customer must be read as referring also to any guarantor of the customer’s obligations under the regulated mortgage contract, where the context permits.

11.6.3 R

(1) MCOB 11.6.2 R does not apply to:

(a) entering into a new regulated mortgage contract or home purchase plan as a replacement for an existing regulated mortgage contract or home purchase plan between the customer and the firm (either as the original mortgage lender or home purchase provider or as the transferee of the existing contract), whether or not the new contract relates to the same property; or

(b) a variation of an existing regulated mortgage contract or home purchase plan;

provided the conditions in (2) are satisfied.

(2) The conditions referred to in (1) are that:

(a) the proposed new or varied regulated mortgage contract or home purchase plan would not involve the customer taking on additional borrowing or (for a home purchase plan, increasing the amount of finance provided under the plan) beyond the amount currently outstanding under the existing regulated mortgage contract or home purchase plan, other than to finance any product fee or arrangement fee for the proposed new or varied contract; and

(b) there is no change to the terms of the regulated mortgage contract or home purchase plan which is likely to be material to affordability.

(3) MCOB 11.6.2 R does not apply to a variation to the terms of a regulated mortgage contract or home purchase plan which is made solely for the purposes of forbearance where the customer has a payment shortfall, or in order to avoid a payment shortfall.

11.6.4 E

(1) If a firm treats any of the following changes as not likely to be material to affordability, this may be relied upon as tending to show contravention of MCOB 11.6.2 R:
(a) an extension of the term of the regulated mortgage contract or home purchase plan which it is reasonable to expect will extend into (or further into) the customer’s retirement (including a change from a mortgage with a term to a retirement interest-only mortgage); or

(b) changing from a repayment mortgage to an interest-only mortgage, or vice versa; or

(c) the addition or removal of a customer.

(2) The list in (1) is not exhaustive.

11.6.5 R When assessing for the purposes of MCOB 11.6.2 R whether a customer will be able to pay the sums due, a firm:

(1) must not base its assessment of affordability on the equity in the property which is used as security under the regulated mortgage contract or is subject to the home purchase plan, or take account of an expected increase in property prices;

[Note: article 18(3) of the MCD]

(2) must take full account of:

(a) the income of the customer, net of income tax and national insurance; and, as a minimum

(b) (i) the customer’s committed expenditure; and

(ii) the basic essential expenditure and basic quality-of-living costs of the customer’s household;

[Note: article 20(1) of the MCD]

(3) (if it is a mortgage lender) must assess affordability on the basis of both repayment of capital and payment of interest over the term, except where lending under an interest-only mortgage in accordance with MCOB 11.6.41R (1); and

(4) (if it is a mortgage lender) must take account of the impact of likely future interest rate increases on affordability, as set out in MCOB 11.6.18 R.

[Note: article 18(1) of the MCD]

11.6.6 R For the purposes of MCOB 11.6.2 R, a firm must not rely on a general declaration of affordability by the customer or his representative.

Income multiples

11.6.7 G A firm may wish to impose a limit, expressed as a multiple of the customer’s income, on the amount it is prepared to advance under a regulated mortgage contract or home purchase plan. Such an approach is not, of itself, inconsistent with MCOB 11.6.2 R but, in accordance with the rules in this section, the firm must be able to demonstrate that the loan is affordable, having taken full account of the customer’s income and expenditure, and (for a mortgage lender) the impact of future likely interest rate increases on affordability.
11.6.8 R In taking account of the customer’s income (in accordance with MCOB 11.6.5R (2)(a)) for the purposes of its assessment of whether the customer will be able to pay the sums due:

1. a firm must obtain evidence of the income declared by the customer for the purposes of the customer’s application for the regulated mortgage contract or home purchase plan (or variation). The evidence, whether document-based or derived through the use of automated systems, must be of a type and for a period which is adequate to support each element of income that the firm is taking into account, and subject to appropriate anti-fraud controls; and

2. a firm must not accept self-certification of income by the customer, and the source of the evidence in (1) must be independent of the customer.

11.6.9 G In relation to taking account of the customer’s income for the purposes of its assessment of whether the customer will be able to pay the sums due:

1. income may be derived from sources other than employment (such as pensions or investments), or from more than one job;

2. the evidence necessary to comply with MCOB 11.6.8 R will vary according to factors such as the employment status and the nature of the employment of the customer (for example, whether he is employed, self-employed, a contractor or retired), his length of employment and, in particular, any elements of income that are not contractually guaranteed. For example: income from overtime working may be evidenced by payslips over a period of time or by checking the level of income regularly paid into a bank account;

3. for a self-employed customer, a firm may wish to consider using projections of future income, where these form part of a credible business plan;

4. a firm may use information it already holds about a customer’s income, for example where the customer holds a current account with the mortgage lender;

5. the source of evidence may be independent of the customer even where it is supplied by the customer; for example, in the form of payslips, bank statements or tax returns;

6. a firm may use information provided to it by a home finance intermediary or other third party, including electronic sources of information, but the firm will retain responsibility for compliance with this chapter; and

7. mortgage lenders and home purchase providers are reminded of their obligations under SYSC 8 in respect of outsourcing where they choose to use a third party to verify income information.
Expenditure

11.6.10 R

For the purposes of a mortgage lender’s or home purchase provider’s assessment of whether the customer will be able to pay the sums due:

(1) the committed expenditure of a customer in MCOB 11.6.5R (2)(b)(i) is his credit and other contractual commitments which will continue after the regulated mortgage contract or home purchase plan (or variation) is entered into;

(2) the basic essential expenditure of a customer’s household in MCOB 11.6.5R (2)(b)(ii) comprises expenditure for: housekeeping (food and washing); gas, electricity and other heating; water; telephone; council tax; buildings insurance; ground rent and service charge for leasehold properties; and essential travel (including to work or school); and

(3) the basic quality-of-living costs of a customer’s household in MCOB 11.6.5R (2)(b)(ii) are its expenditure which is hard to reduce and gives a basic quality of life (beyond the absolute essential expenditure in (2)).

11.6.11 G

(1) Examples of committed expenditure are: credit commitments such as secured and unsecured loans and credit cards; hire purchase agreements; child maintenance; alimony; and the cost of a repayment strategy where the customer has an interest-only mortgage (where affordability has not been assessed on a capital and interest basis: see MCOB 11.6.48 R (Assessing affordability under an interest-only mortgage)).

(2) Examples of basic quality-of-living costs (which can be reduced, but only with difficulty) are: clothing; household goods (such as furniture and appliances) and repairs; personal goods (such as toiletries); basic recreation (television, some allowance for basic recreational activities, some non-essential transport); and childcare.

11.6.12 R

For the purposes of its assessment of whether the customer will be able to pay the sums due:

(1) a firm may generally rely on any evidence of income or information on expenditure provided by the customer unless, taking a common sense view, it has reason to doubt the evidence or information;

(2) in taking account of the customer’s committed expenditure, a firm must take reasonable steps to obtain details of the customer’s actual outstanding commitments; and

(3) in taking account of the basic essential expenditure and basic quality-of-living costs of a customer’s household, a firm may obtain details of the actual expenditure. Alternatively, it may use statistical data or other modelled data appropriate to the composition of the customer’s household, including the customer, dependent children and other dependents living in the household. If it uses statistical or other modelled data a firm must apply realistic assumptions to determine the level of expenditure of the customer’s household.
(1) Examples of evidence of income in MCOB 11.6.12R (1) are payslips and bank statements.

(2) If a firm obtains details of the customer’s credit commitments from the customer, it should corroborate the information, for example by making a credit reference agency search or checking credit card or bank statements.

(3) Where the customer’s credit or contractual commitments are due to end shortly after the regulated mortgage contract or home purchase plan (or variation) has been entered into, a firm should take a common sense approach to deciding whether to include those commitments in its assessment of whether the customer will be able to pay the sums due, according to such factors as the remaining term of the commitment and the magnitude of payments required under it.

**Future changes to income and expenditure**

(1) Examples of future changes to income and expenditure in MCOB 11.6.14R are: reductions in income that may come about following the customer’s retirement; where it is known that the customer is being made redundant; or where the firm is aware of another loan commitment that will become due during the term of the regulated mortgage contract or home purchase plan, such as an equity loan to assist in property purchase.

(2) If the term of a regulated mortgage contract or home purchase plan would extend beyond the date on which the customer expects to retire (or, where that date is not known, the state pension age), a firm should take a prudent and proportionate approach to assessing the customer’s income beyond that date. The degree of scrutiny to be adopted may vary according to the period of time remaining to retirement when the assessment is made. The closer the customer is to retiring, the more robust the evidence of the level of income in retirement should be. For example, where retirement is many years in the future, it may be sufficient merely to confirm the existence of some pension provision for the customer by requesting evidence such as a pension statement; where the customer is close to retirement, the more robust steps may involve considering expected pension income from a pension statement. In accordance with MCOB 11.6.12R (1), a firm should take a common sense view when assessing any information provided by the customer on his expected retirement date.

(3) Where an additional loan commitment is expected to become due during the term of the regulated mortgage contract or home purchase plan, the mortgage lender should assess whether the regulated mortgage contract or home purchase plan will remain
affordable when the loan commitment becomes due, unless there is an appropriate repayment strategy in place to repay that loan, such as through the sale of the property which is the subject of the regulated mortgage contract or home purchase plan.

() When assessing the affordability of a retirement interest-only mortgage with joint borrowers, the firm should consider the ability of a single borrower to continue making the required payments if the other dies, taking into account relevant evidence such as pensions payable to the surviving spouse or civil partner.

Debt consolidation and credit-impaired consumers

11.6.16 R

(1) This rule applies where:

(a) a purpose of a regulated mortgage contract or home purchase plan (or variation) is debt consolidation; and

(b) for a first charge regulated mortgage contract, the customer is a credit-impaired customer.

(2) Subject to (3), where each of the conditions in (1) is satisfied and, if the debts which are to be repaid using the sums raised by the regulated mortgage contract or home purchase plan (or variation) were not repaid, the transaction would not be affordable for the customer, the firm must take reasonable steps to ensure that, on completion of the transaction, those debts are actually repaid.

(3) The requirement in (2) does not apply if the firm has assumed that the customer’s existing debts which are to be repaid using the sums raised by the regulated mortgage contract or home purchase plan (or variation) will not in fact be repaid and, accordingly, include them as committed expenditure in the affordability assessment for the customer.

11.6.17 G

The requirement in MCOB 11.6.16R (2) for reasonable steps may be satisfied by the mortgage lender’s, or home purchase provider’s, repaying the committed expenditure directly to the creditors concerned as a condition of granting the regulated mortgage contract or home purchase plan.

Considering the effect of future interest rate rises

11.6.18 R

(1) Under MCOB 11.6.5R (4), in taking account of likely future interest rate increases for the purposes of its assessment of whether the customer will be able to pay the sums due, a mortgage lender must consider the likely future interest rates over a minimum period of five years from the expected start of the term of the regulated mortgage contract (or variation), unless the interest rate under the regulated mortgage contract is fixed for a period of five years or more from that time, or for the duration of the regulated mortgage contract (or variation), if less than five years.

(2) In coming to a view as to likely future interest rates, a mortgage lender must have regard to:

(a) market expectations; and

(b) any prevailing Financial Policy Committee recommendation on appropriate interest-rate stress tests;

and must be able to justify the basis it uses by reference to (a) and (b).
(3) For the purposes of this rule, even if the basis used by the mortgage lender in (2) indicates that interest rates are likely to fall, or to rise by less than 1%, during the first five years of the regulated mortgage contract (or variation), a mortgage lender must assume that interest rates will rise by a minimum of 1% over that period.

(1) Under MCOB 11.6.5R (4), in taking account of likely future interest rate increases for the purposes of its assessment of whether the customer will be able to pay the sums due, a second charge lender must also consider the likely future interest rates of any regulated mortgage contract in existence at the time of the assessment and remaining in existence after the relevant second charge regulated mortgage contract has been entered into.

(2) The second charge lender must, at a minimum, base its assessment under (1) on the balance outstanding of any regulated mortgage contract relevant under (1).

In relation to MCOB 11.6.18R (2):

(1) an example of market expectations is the forward sterling rate published on the Bank of England website. A mortgage lender should not use its own forecast; and

(2) a mortgage lender should not link its determination to market expectations without considering the likely effect of rate changes in accordance with the market expectations on the specific regulated mortgage contract in question.

Responsible lending or financing policy

A firm must put in place, and operate in accordance with, a written policy (which may be contained in more than one document), approved by its governing body, setting out the factors it will take into account in assessing a customer’s ability to pay the sums due. The policy must address the following matters:

(1) how income and expenditure is to be assessed, including (except as provided in MCOB 11.6.32R (1) and MCOB 11.6.39R (1)):
   (a) details of the types of income which are acceptable;
   (b) the proportion of different income streams which is acceptable;
   (c) how variations in income over time, of which the firm is aware, are to be considered;
   (d) what is acceptable evidence of income (including the time period to be covered by the evidence); and
   (e) how committed expenditure, basic essential expenditure and basic quality-of-living costs are taken into account when assessing affordability;

(2) how future interest rates are taken into account when assessing affordability;
(3) the calculations used to determine whether the regulated mortgage contract or home purchase plan is affordable;

(4) how the mortgage lender's or home purchase provider's anti-fraud controls are incorporated into affordability assessments;

(5) how the mortgage lender's or home purchase provider's method of calculating the size of the advance for each customer, based on a consideration of the customer's income and expenditure, is to be monitored, including the timing of reviews and key performance indicators to be used (see § MCOB 11.6.22 R (Monitoring));

(6) the actions to be taken if the mortgage lender's or home purchase provider's calculation method, referred to in (5), does not perform as expected;

(7) how regular audits of compliance with the mortgage lender's or home purchase provider's responsible lending or financing policy established in accordance with this rule are to be undertaken (as required by § MCOB 11.6.24 R);

(8) how the record keeping requirements in § MCOB 11.6.60 R are to be met;

(9) (if applicable) the matters required by § MCOB 11.6.50 R (Interest-only policy); and

(10) (if applicable) how the firm will apply the rules in § MCOB 11.7 (Transitional arrangements) so as to permit exceptions to its procedures for affordability assessments, to include arrangements for use of management information to monitor its application of those exceptions.

[Note: article 18(2) of the MCD]

11.6.21 Examples of different income streams in § MCOB 11.6.20R (1)(b) are: income derived from sources other than employment; income from more than one job; and elements of income that are not contractually guaranteed.

11.6.21A An MCD mortgage lender must keep a record of the valuation and types of immovable property accepted as a security, as well as the related mortgage underwriting policies used.

[Note: article 19(2) and second sentence of article 26(1) of the MCD]

11.6.21B When considering the period for which the records kept under § MCOB 11.6.21A R are to be retained, MCD mortgage lenders are reminded of the high-level record-keeping provisions in SYSC.

Monitoring

11.6.22 A firm must put in place, and be able to demonstrate that it has, robust systems and controls (including the use of management information and key performance indicators) to monitor the effectiveness of its affordability assessments, including in preventing payment difficulties.
**11.6.23** Except as provided in [MCOB 11.6.32R (2)] and [MCOB 11.6.39R (2)], the monitoring in [MCOB 11.6.22R] should:

1. Include use of management information, key performance indicators and root cause analysis to review and (where appropriate) adjust and improve the **mortgage lender’s or home purchase provider’s** method of calculating the size of the advance for each **customer**, based on a consideration of the customer’s income and expenditure; and

2. Take place on a regular basis. However, a **firm** should put in place key performance indicators that trigger more frequent reviews; for example, if the incidence of **customers** being in **arrears**, or of early **arrears**, is higher than expected.

**11.6.24** A **firm** must ensure that its compliance with the responsible lending or financing policy required by [MCOB 11.6.20R] is reviewed at least once per calendar year:

1. In any case where the **firm** has an internal audit function or outsourced equivalent, by that function; and

2. In any other case, by the **firm’s** internal compliance function or an outsourced equivalent.

**Alternative provisions for loans which are solely for a business purpose**

**11.6.25** Where a **regulated mortgage contract** is solely for a business purpose, a **firm** may opt to apply [MCOB 11.6.26R] to [MCOB 11.6.31R] in place of [MCOB 11.6.5R] to [MCOB 11.6.19G].

**11.6.26** When assessing for the purposes of [MCOB 11.6.2R] whether a **customer** will be able to pay the sums due, a **firm**:

1. Must not base its assessment of affordability on the equity in the property which is used as security under the **regulated mortgage contract**, or take account of an expected increase in property prices;

2. Must:
   (a) where the repayments will be made from the resources of the **customer**;
      (i) take full account of the income, net of income tax and national insurance, or net assets (or both) of the **customer**; and the customer’s committed expenditure; and
      (ii) take account, in general terms as a minimum, of the basic essential expenditure and basic quality-of-living costs of the customer’s household; and
   (b) where the repayments will be made from the financial resources of the business, take full account of the strength of those resources;

3. In a case falling within (2)(b), if the **customer is relying on the business for his personal income**, must as a minimum consider in
general terms whether the business can support the customer’s basic essential expenditure and basic quality-of-living costs;

(4) must assess affordability on the basis of both repayment of capital and payment of interest over the term, except where lending under an interest-only mortgage in accordance with MCOB 11.6.41 R (1); and

(5) must take account of the impact of likely future interest rate increases on affordability.

11.6.27 R For the purposes of MCOB 11.6.2 R, a firm must not rely on a general declaration of affordability by the customer or his representative.

11.6.28 R In taking account (in accordance with MCOB 11.6.26 R (2)) of the customer’s income or net assets (or both) and the resources of the business for the purposes of its assessment of whether the customer will be able to pay the sums due:

(1) a firm must obtain evidence of the income or net assets (or both) of the customer and the resources of the business, as declared by the customer for the purpose of the customer’s application for the regulated mortgage contract (or variation); and

(2) a firm must not accept self-certification of income by the customer, and the source of the evidence in (1) must be independent of the customer.

11.6.29 R In MCOB 11.6.26 R, for the purposes of taking full account of committed expenditure and taking account in general terms of basic essential expenditure and basic quality-of-living costs, the meaning of those phrases is as set out in MCOB 11.6.10 R.

11.6.30 G The information which a firm should consider when taking account, for the purposes of MCOB 11.6.26 R (2)(b), of the strength of the financial resources of the business will vary according to the characteristics of the business, but may include factors such as the cash flow, assets and liabilities of the business.

11.6.31 R If a firm is, or should reasonably be aware from information obtained during the application process, that there will, or are likely to, be future changes to the income and expenditure of the customer, or the resources of the business, during the term of the regulated mortgage contract, the firm must take them into account when assessing whether the customer will be able to pay the sums due for the purposes of MCOB 11.6.2 R.

11.6.32 R Where a firm chooses, in accordance with MCOB 11.6.25 R, to apply the provisions of MCOB 11.6.26 R to MCOB 11.6.31 R in place of MCOB 11.6.5 R to MCOB 11.6.19 G:

(1) its policy in MCOB 11.6.20 R (1) need not address each of the matters prescribed in sub-paragraphs (a) to (e) of that rule;
(2) MCOB 11.6.23 G does not apply; and

(3) in each case the record-keeping requirements in MCOB 11.6.60R (2)(a) to (d) apply only to the extent relevant, but the record in MCOB 11.6.60R (1) must also include, to the extent relevant:

(a) the customer's assets and the evidence relied on to assess them; and

(b) the details considered in relation to the resources of the business.

Alternative provisions for loans with high net worth mortgage customers

Where a regulated mortgage contract is for a high net worth mortgage customer, a firm may opt to apply MCOB 11.6.34 R to MCOB 11.6.38 R in place of MCOB 11.6.5 R to MCOB 11.6.19 G.

When assessing for the purposes of MCOB 11.6.2 R whether a customer will be able to pay the sums due, a firm:

(1) must not base its assessment of affordability on the equity in the property which is used as security under the regulated mortgage contract, or take account of an expected increase in property prices;

[Note: article 18(3) of the MCD]

(2) must:

(a) take full account of the income, net of income tax and national insurance, or net assets (or both) of the customer; and the customer's committed expenditure; and

(b) take account, in general terms as a minimum, of the basic essential expenditure and basic quality-of-living costs of the customer's household;

[Note: article 20(1) of the MCD]

(3) must assess affordability on the basis of both repayment of capital and payment of interest over the term, except where lending under an interest-only mortgage in accordance with MCOB 11.6.41R (1); and

(4) must take account of the impact of likely future interest rate increases on affordability.

For the purposes of MCOB 11.6.2 R, a firm must not rely on a general declaration of affordability by the customer or his representative.

In taking account of the customer's income or net assets (or both) (in accordance with MCOB 11.6.34R (2)(a)) for the purposes of its assessment of whether the customer will be able to pay the sums due:

(1) a firm must obtain evidence of the income or net assets (or both) declared by the customer for the purpose of the customer's application for the regulated mortgage contract (or variation); and
(2) a firm must not accept self-certification of income by the customer, and the source of the evidence in (1) must be independent of the customer.

11.6.37 R In MCOB 11.6.34 R, for the purposes of taking full account of committed expenditure and taking account in general terms of basic essential expenditure and basic quality-of-living costs, the meaning of those phrases is as set out in MCOB 11.6.10 R.

11.6.38 R If a firm is, or should reasonably be, aware from information obtained during the application process, that there will, or are likely to, be future changes to the income and expenditure of the customer during the term of the regulated mortgage contract, the firm must take them into account when assessing whether the customer will be able to pay the sums due for the purposes of MCOB 11.6.2 R.

11.6.39 R Where a firm chooses, in accordance with MCOB 11.6.33 R, to apply the provisions of MCOB 11.6.34 R to MCOB 11.6.38 R in place of MCOB 11.6.5 R to MCOB 11.6.19 G:

(1) its policy in MCOB 11.6.20 R (1) need not address each of the matters prescribed in sub-paragraphs (a) to (e) of that rule;

(2) MCOB 11.6.23 G does not apply; and

(3) in each case the record-keeping requirements in MCOB 11.6.60 R (2)(a) to MCOB 11.6.60 R (2)(d) apply only to the extent relevant, but the record in MCOB 11.6.60 R (1) must also include, to the extent relevant, the customer’s assets and the evidence relied on to assess them.

Interest-only mortgages

11.6.40 G The rules in this part (MCOB 11.6.41 R to MCOB 11.6.49 R) provide that interest-only mortgages may be entered into by mortgage lenders in limited circumstances.

11.6.40A G A shared equity credit agreement may be an interest-only mortgage.

Entering into interest-only mortgages

11.6.41 R (1) A mortgage lender may only enter into an interest-only mortgage, or switch a repayment mortgage onto an interest-only basis for all or part of its term, if:

(a) it has evidence that the customer will have in place a clearly understood and credible repayment strategy; and

(b) as far as it is reasonably able to assess at that time, the repayment strategy has the potential to repay the capital borrowed and any interest reasonably expected to be accrued under the interest-only mortgage.

(2) In MCOB 11.6, a reference to an interest-only mortgage is to be read as including any regulated mortgage contract which includes an
interest-only period or where part of the sum is advanced on an interest-only basis.

(3) A mortgage lender must not accept speculative repayment strategies for the purposes of (1).

11.6.42 Firms are reminded that:

(1) interest-only mortgages include those where some, but not all, interest is payable at the end of the term. Accordingly, the requirement in MCOB 11.6.41R (1)(b) applies equally to such interest-only mortgages as it does to those where all of the interest is accrued until the end of the term; and

(2) a lifetime mortgage is a type of interest-only mortgage, as full repayment of capital and interest is not required over the term. Accordingly, the requirements in the Handbook (including in MCOB 11.6 and MCOB 11.7) which apply to interest-only mortgages apply to lifetime mortgages, unless specifically disapplied. Depending always on its terms, a lifetime mortgage may also be an interest roll-up mortgage, as noted in MCOB 11.6.59 G.

11.6.43 MCOB 11.6.41R (1) does not prevent a mortgage lender, when appropriate, from making a temporary concession, by which he accepts payment of interest only, with a customer who is in arrears or has a payment shortfall, or is at risk of arrears or a payment shortfall, on a regulated mortgage contract.

11.6.44 Firms are reminded that whether it is appropriate to take the action contemplated by MCOB 11.6.43 R will depend on all the circumstances of the particular case and must be considered having regard to, among other things, Principle 6 and the rules in MCOB 13.

11.6.45 The following are examples of repayment strategies that may, subject to the circumstances of the customer, be acceptable for the purposes of MCOB 11.6.41R (1):

(1) regular deposits into a savings or investment product;

(2) the periodic repayment of capital from irregular sources of income (such as bonuses or some sources of income from self-employment);

(3) the sale of assets such as another property or other land owned by the customer; and

(4) for a shared equity credit agreement or a retirement interest-only mortgage, the sale of the property which is the subject of the agreement.

11.6.46 Acceptance by a mortgage lender of any of the following repayment strategies for the purposes of MCOB 11.6.41R (1) may be relied upon as tending to show contravention of that rule:
(1) an expectation that the value of the property which is the subject of the regulated mortgage contract will increase over its term sufficiently to enable the customer to sell the property to repay the capital borrowed and, where applicable, pay the interest accrued under the interest-only mortgage;

(2) an intention on the part of the customer to utilise an expected, but uncertain, inheritance to repay the capital borrowed and, where applicable, pay the interest accrued under the interest-only mortgage; and

(3) the sale of the property which is the subject of the regulated mortgage contract, where that is the customer's main residence and the mortgage lender does not consider whether the property will have the potential to:
   (a) provide sufficient funds for the customer to repay the capital borrowed and, where applicable, the interest accrued under the interest-only mortgage; and
   (b) allow the customer to purchase a cheaper property to reside in or execute any other associated strategy.

The above list is not exhaustive.

11.6.46A R MCOB 11.6.46E(3)(b) does not apply in relation to a retirement interest-only mortgage.

11.6.47 G In complying with MCOB 11.6.41R (1), where a customer's repayment strategy is the sale of the property which is the subject of the regulated mortgage contract, a mortgage lender may wish to consider, as part of its assessment of that repayment strategy, factors such as the equity in the property when considered in relation to the level of property prices in the relevant area at the time of the consideration or, for a lifetime mortgage, the borrower's life expectancy.

Assessing affordability under an interest-only mortgage

11.6.48 R For the purposes of MCOB 11.6.2 R, where a mortgage lender is lending under an interest-only mortgage in accordance with MCOB 11.6.41R (1), it may assess affordability on the basis of payment of interest only over the term (plus repayment of such capital as may be due to be repaid over the term). If it does so, it must consider as part of the customer's committed expenditure under MCOB 11.6.5R (2)(b)(i) (or the equivalent alternative provision for transactions with high net worth mortgage customers or solely for business purposes) the cost to the customer of the repayment strategy (unless the mortgage is a retirement interest-only mortgage).

Review during the term of interest-only mortgages

11.6.49 R (1) This rule applies in relation to all interest-only mortgages which a mortgage lender enters into on or after 26 April 2014 except:
   (a) lifetime mortgages;
   (aa) retirement interest-only mortgages;
   (b) bridging loans; and
(c) any other case where the repayment of capital borrowed and, if applicable, interest accrued, is certain.

(2) Except as set out in (3), a mortgage lender must carry out a review (as a minimum, once) during the term of the mortgage, in which contact is made with the customer, to check that the customer's repayment strategy is still in place, and that it is still reasonable to expect that the repayment strategy has the potential to repay the capital borrowed and, where applicable, pay the interest reasonably expected to be accrued under the interest-only mortgage. The review must be carried out at a stage of the term when, if the repayment strategy is not in place, or not adequate, there is likely to be sufficient time prior to the end of the term for the customer to take appropriate steps to remedy the situation.

(3) The review in (2) is not required in any case where, despite reasonable efforts to contact the customer, the mortgage lender has been unable to do so.

(4) Following the review in (1), where appropriate the mortgage lender must take reasonable steps to discuss with the customer what may be done to address the situation.

Interest-only policy

A mortgage lender which enters into interest-only mortgages (unless they are only lifetime mortgages) must include in the policy which is required by MCOB 11.6.20 R (Responsible lending and financing policy) a policy on interest-only mortgages, setting out its processes and procedures for ensuring compliance with MCOB 11.6.41R (1) and for safeguarding the interests of customers during the term of interest-only mortgages. This policy must include:

(1) details of the mortgage lender's plans for lending by way of interest-only mortgages, including its planned volumes of lending on that basis over a specified period, and provision for reviewing the actual volumes of lending on that basis, including the timing and method of review;

(2) specification of the types of repayment strategy which will be considered acceptable, and the evidential requirements and other controls which will be applied to ensure that only such types will be accepted, including the controls to be applied where the repayment strategy is the sale of the property which is the subject of the regulated mortgage contract;

(3) the procedures for checking the existence and adequacy of the repayment strategy in line with the policy, including questions to be asked of the customer;

(4) the arrangements for monitoring and auditing compliance with the policy, processes and procedures (see MCOB 11.6.22 R and MCOB 11.6.24 R (Monitoring)); and

(5) the process for the review required by MCOB 11.6.49 R which, as a minimum:

(a) prescribes the timing of the review;
(b) prescribes the content of the review, including the questions to be asked of the customer and the actions to be taken if the customer proves difficult to contact or otherwise does not co-operate with the review;

(c) sets out how it is to be decided whether the customer’s repayment strategy meets the criteria in MCOB 11.6.49R (2); and

(d) sets out the actions which will be appropriate to be considered during the discussions in MCOB 11.6.49R (2), depending on the circumstances of the customer.

11.6.51 (1) The controls in MCOB 11.6.50R (2) may include, where appropriate: maximum loan to value limits; minimum equity requirements; regional factors such as property prices; or other eligibility requirements.

(2) The policy and procedures for safeguarding the interests of a customer under an interest-only mortgage should not permit the mortgage lender to change the interest-only mortgage to a repayment mortgage, extend the term or otherwise change the features of the interest-only mortgage unless to do so is compatible with the duties of the mortgage lender under Principle 6 and any other applicable rules and regulations, including those relating to arrears or payment shortfall. A mortgage lender should also have regard to the CRA when drafting the provisions of regulated mortgage contracts in relation to changes to their features.

11.6.52 MCOB 11.6.50 R sets out requirements for mortgage lenders to have appropriate procedures for managing interest-only mortgages in order to safeguard the interests of customers. Firms are reminded of the rules and guidance in SYSC (notably SYSC 7.1) relating to systems and controls for the management of risks to which firms themselves are exposed. Firms will need to consider whether their systems and controls are adequate in relation to the management of risks arising from interest-only mortgages.

Assessing the customer’s repayment strategy for bridging loans

11.6.53 For a bridging loan which is an interest-only mortgage, acceptance by a mortgage lender as a repayment strategy for the purposes of MCOB 11.6.41R (1) of an expectation that, by entering into the bridging loan, the customer’s credit status will be sufficiently improved to enable him to refinance to a longer-term regulated mortgage contract (except where the mortgage lender has evidence of a guaranteed offer for such a longer-term contract) may be relied upon as tending to show contravention of that rule.

11.6.54 For a bridging loan which is an interest-only mortgage, in complying with MCOB 11.6.41R (1):

(1) where the customer’s repayment strategy is the sale of his existing home, the mortgage lender may wish to consider asking for it to be supported by an independent valuation of that property, as a condition of accepting that repayment strategy; and
(2) where the customer's repayment strategy is the replacement of the bridging loan with a mainstream regulated mortgage contract, the mortgage lender should not accept that repayment strategy unless it is reasonably satisfied that a mainstream mortgage lender will be willing to enter into a regulated mortgage contract with the customer. A firm may wish to consider requesting evidence of a guaranteed offer or agreement in principle that will be in place once the existing term of the bridging loan has expired, or obtain the necessary income and expenditure information, in order to be so satisfied.

Extending the term of a bridging loan

11.655 R Except in relation to a secured overdraft which is solely for a business purpose or is with a high net worth mortgage customer:

(1) when considering extending the term of a bridging loan, a mortgage lender must comply with MCOB 11.6.2 R as if the bridging loan were a new loan;

(2) where MCOB 11.6.2 R does not apply in relation to extending the term of a bridging loan (because the bridging loan is an interest roll-up mortgage, and therefore MCOB 11.6.57 R applies), the mortgage lender must consider with the customer, before he commits himself to extend the term, the impact of the extension on the customer’s remaining equity in the property which is the subject of the bridging loan; and

(3) a firm must not agree to extend the term of a bridging loan unless the customer has made a positive choice to do so.

11.656 G Firms are reminded that, when extending the term of a bridging loan to which MCOB 11.6.55 R does not apply, in accordance with MCOB 2.5A.1 R, they must act honestly, fairly and professionally in accordance with the best interests of their customer.

Interest roll-up mortgages

11.657 R The requirements in MCOB 11.6.2 R (and any Handbook provisions applicable only to that rule) do not apply in relation to an interest roll-up mortgage, or to the type of lifetime mortgage described in MCOB 9.4.132AR.

11.657A G The type of lifetime mortgage described in MCOB 9.4.132AR is one under which the customer makes payments to start with, but which can be converted to an interest roll-up mortgage at any time of the customer’s choosing.

11.658 R A mortgage lender may not enter into an interest roll-up mortgage, or vary an existing regulated mortgage contract so that it becomes an interest roll-up mortgage, unless it is:

(1) a lifetime mortgage; or

(2) a bridging loan; or
(3) a loan to a high net worth mortgage customer; or

(4) a loan solely for business purposes; or

(5) a shared equity credit agreement.

11.6.59  Firms are reminded that an interest roll-up mortgage is a type of interest-only mortgage, where no payments of interest or capital are required or anticipated until the mortgage comes to an end. Depending always on their terms, it is possible to structure the types of product set out in MCOB 11.6.58R (1) to (4) as an interest roll-up mortgage. Where that is the case, MCOB 11.6.2R will not apply in relation to them, but MCOB 11.6.40 G to MCOB 11.6.52 G will apply to all interest roll-up mortgages, to the extent they are permitted by MCOB 11.6.58 R.

11.6.59A  A shared equity credit agreement may be an interest roll-up mortgage.

Record-keeping

11.6.60  (1) A firm must make, in paper or electronic form, an adequate record of the steps it takes to comply with the rules in this chapter in relation to each customer.

(2) The record in (1) must include the information taken into account in each affordability assessment, so that it is possible to understand from the record the basis of the mortgage lender’s or home purchase provider’s lending or financing decision, including (except as provided in MCOB 11.6.32R (3) and MCOB 11.6.39R (3)):

(a) the customer’s income, including, where relevant, a breakdown of the different income types;

(b) the customer’s committed expenditure;

(c) the basic essential expenditure and basic quality-of-living costs of the customer’s household (whether actual expenditure for that household or assumed expenditure from statistical or other modelled data, including information to show why the assumed data is appropriate to that customer’s household);

(d) the evidence relied on to assess income and expenditure;

(e) the rate or assumptions used to test affordability against likely future interest rate rises;

(f) the repayment type and term of the regulated mortgage contract, or the term of the home purchase plan; and

(g) the calculation used to determine whether the regulated mortgage contract, home purchase plan is (or, where applicable, following the variation, remains) affordable for the customer.

(3) In relation to interest-only mortgages, the record in (1) must include:

(a) the reasons for each decision to offer an interest-only mortgage to a customer;

(b) the evidence of the customer’s repayment strategy and, where applicable, its cost;
(c) details of the firm’s attempts to contact the customer where required by MCOB 11.6.49 R; and

(d) the outcome of each review required by MCOB 11.6.49 R (whether conducted once during the term of the interest-only mortgage or more frequently).

(4) In relation to the extension of the term of a bridging loan which falls within MCOB 11.6.55 R, the record in (1) must include:

(a) the customer’s positive choice to extend the term;

(b) the reasons for the decision to extend the term; and

(c) the evidence of the customer’s repayment strategy and its cost.

(5) A firm must retain the records required by (1) to (4) for the term of the regulated mortgage contract or home purchase plan.

(6) Where a firm enters into or varies a regulated mortgage contract or home purchase plan under MCOB 11.7 (Transitional arrangements), it must keep, for the term of the contract or plan, a record of:

(a) the outstanding balance on the existing contract or plan;

(b) the cost of the repairs or maintenance work to the property, where relevant;

(c) any product fee or arrangement fee financed by any additional borrowing taken on under the contract or increase in the amount of finance provided under the plan; and

(d) the rationale for each decision made to enter into or vary a regulated mortgage contract or home purchase plan under MCOB 11.7 (Transitional arrangements), including why the firm considered it to be in the customer’s best interests.

(7) A firm must make, and keep up to date, an adequate record of the policy required by MCOB 11.6.20 R. When the policy is changed, a record of the previous policy must be retained for so long as any regulated mortgage contract or home purchase plan to which it was applicable remains outstanding.

[Note: article 18(2) of the MCD]

11.6.61 For the purposes of MCOB 11.6.60R (2)(c) and (g), if it is not practicable for the firm to record on the customer’s file full details of the calculation method applied, it should record clearly which version of that method was applied in order that the file can be reviewed in conjunction with the applicable version of the method, so that it is possible to reconstruct the lending decision.
11.7 Transitional arrangements

11.7.1 When considering entering into a first charge regulated mortgage contract or varying a first charge regulated mortgage contract or home purchase plan, a firm need not apply the rules in MCOB 11.6.2 R to MCOB 11.6.18 R inclusive (as modified by MCOB 11.6.25 R to MCOB 11.6.31 R and MCOB 11.6.33 R to MCOB 11.6.38 R, where applicable) if it has established, acting reasonably, that the following conditions are satisfied:

(1) the customer has:
   (a) an existing first charge regulated mortgage contract (whether or not entered into on or after 31 October 2004) with the firm or home purchase plan (whether or not entered into on or after 6 April 2007) which was in existence prior to 26 April 2014; or
   (b) an existing first charge regulated mortgage contract with the firm or home purchase plan which was entered into in reliance on, and in compliance with, MCOB 11.7;

(2) subject to MCOB 11.7.2 R, the proposed regulated mortgage contract or home purchase plan, or variation, would not involve the customer taking on additional borrowing (or, for a home purchase plan, increasing the amount of finance provided under the plan) beyond the amount currently outstanding under the existing regulated mortgage contract or home purchase plan, other than to finance any product fee or arrangement fee for the proposed new or varied contract;

(3) the proposed transaction would be in the customer’s best interests; and

(4) the customer has not, after 26 April 2014 increased the size of the advance under the existing regulated mortgage contract or home purchase plan other than to finance any relevant product fee or arrangement fee in relation to, or the cost of essential repairs or maintenance to the property which is the subject of, that regulated mortgage contract or home purchase plan.

11.7.2 The condition in MCOB 11.7.1R (2) does not apply if each of the following conditions is satisfied:

(1) the firm is the mortgage lender or home purchase provider under the existing regulated mortgage contract or home purchase plan in MCOB 11.7.1R (1);
(2) the value of the property which is the subject of the regulated mortgage contract or home purchase plan is at risk if repairs or maintenance work to the property are not carried out;

(3) the funds generated by the additional borrowing or increase in finance provided are to be used to carry out the repairs or maintenance work; and

(4) the firm has obtained credible evidence which demonstrates that the additional borrowing or increase in finance are no more than the cost of the repairs or maintenance work.

(5) the proposed transaction is:

(a) the variation of an existing non-MCD first charge regulated mortgage contract,

(b) the entry into a non-MCD first charge regulated mortgage contract, or

(c) a home purchase plan or variation of a home purchase plan.

11.7.3 R (1) When considering entering into a first charge regulated mortgage contract which is an interest-only mortgage or varying a first charge regulated mortgage contract which is an interest-only mortgage, a mortgage lender need not apply the rules in ■ MCOB 11.6.41R (1), ■ MCOB 11.6.49 R, ■ MCOB 11.6.50 R and ■ MCOB 11.6.60R (3) if the conditions in ■ MCOB 11.7.1 R) are satisfied, and if it has established, acting reasonably, that the existing regulated mortgage contract in ■ MCOB 11.7.1R (1) is an interest-only mortgage.

(2) Where only part of the sum advanced under the existing regulated mortgage contract is on an interest-only basis, (1) applies, but only to that part.

11.7.4 G In accordance with its obligation under Principle 6 to treat its customers fairly, a firm should not treat a customer with whom it enters into or varies a regulated mortgage contract or home purchase plan pursuant to this section 11.7 less favourably than it would treat other customers with similar characteristics, for example by offering less favourable interest rates or other terms.

11.7.5 G Firms should note the record-keeping requirements at ■ MCOB 11.6.60R (6) which apply when regulated mortgage contracts and home purchase plans are entered into or varied under this section.

11.7.6 R Where a firm has elected to apply any of MCOB TPs 22, 24, 26, 28, 30, 32, 34, 36, 38 or 40 in ■ MCOB TP 1.1, any first charge regulated mortgage contract they propose to enter into between 21 September 2015 and 21 March 2016 is not to be regarded as an MCD regulated mortgage contract for the purposes of this chapter.
11.8 Customers unable to change regulated mortgage contract, home purchase plan or provider

11.8.1 Where a customer is unable to:

(1) enter into a new regulated mortgage contract or home purchase plan or vary the terms of an existing regulated mortgage contract or home purchase plan with the existing mortgage lender or home purchase provider; or

(2) enter into a new regulated mortgage contract or home purchase plan with a new mortgage lender or home purchase provider;

the existing mortgage lender or home purchase provider should not (for example, by offering less favourable interest rates or other terms) take advantage of the customer’s situation or treat the customer any less favourably than it would treat other customers with similar characteristics. To do so may be relied on as tending to show contravention of Principle 6 (Customers’ interests).
11.9 Remortgaging with the same or a different lender with no additional borrowing

Application and purpose

11.9.1 (1) Subject to (2), this section applies to a firm in relation to a customer who:
   (a) is a borrower under a regulated mortgage contract ("the existing regulated mortgage contract"), whether with that firm or a different firm; and
   (b) wishes to enter into a new regulated mortgage contract ("the proposed regulated mortgage contract") with that firm to replace the existing regulated mortgage contract.

(2) But this section only applies if:
   (a) the proposed regulated mortgage contract would not involve the customer borrowing:
      (i) a capital amount greater than that outstanding under the existing regulated mortgage contract at the date of the customer's application for the proposed regulated mortgage contract; or
      (ii) where a purpose of the proposed regulated mortgage contract is to replace two or more existing regulated mortgage contracts, a capital amount greater than the cumulative capital amount outstanding under those contracts at that date;
   disregarding any increase that is exclusively for the purpose of financing a product fee or arrangement fee for the proposed regulated mortgage contract or a fee charged by a mortgage intermediary for arranging or advising on regulated mortgage contracts in relation to the proposed regulated mortgage contract;
   (b) the proposed regulated mortgage contract is to be secured on the same property as the existing regulated mortgage contract;
   (c) on the date on which the customer applies for the proposed regulated mortgage contract:
      (i) there is no sum that has become due under the terms of the existing regulated mortgage contract that constitutes a payment shortfall; and
      (ii) at no point in the period of 12 months ending on that date has there been a sum that has become due under the terms
of the existing regulated mortgage contract that constituted a payment shortfall;

(d) the written policy required by MCOB 11.6.20R (responsible lending policy) addresses how the firm will apply the rules in this section; and

(e) the firm has and operates an internal switching policy (see MCOB 11.9.12R).

(3) For the purposes of this section, linked borrowing which is linked to an existing regulated mortgage contract is to be treated as if it were an existing regulated mortgage contract.

11.9.2 R MCOB 11.9.14R (notice to customers) also applies to a firm that has permission for administering a regulated mortgage contract.

11.9.3 G (1) The purpose of this section is to facilitate borrowers switching mortgages, provided that they are not taking out additional borrowing. But the mortgage does not have to be exactly like-for-like and the borrower can, for example:

(a) extend the term of the mortgage, for example to replace a mortgage with 10 years remaining with a new mortgage with a 25-year term;

(b) consolidate a first charge regulated mortgage contract and one or more second charge regulated mortgage contracts into the proposed regulated mortgage contract (but unsecured loans and other debts cannot be consolidated, unless the unsecured loan or debt is linked borrowing which is linked to an existing regulated mortgage contract);

(c) move from an interest-only mortgage to a repayment mortgage (provided it is more affordable); or

(d) take a mortgage with a different type of interest rate, for example to move from a variable rate to a fixed rate.

(2) This section permits firms to choose to modify certain provisions when assessing a customer’s ability to afford a mortgage. The provisions capable of modification are grouped (such as the provisions linked to the assessment of income and expenditure). Firms can choose whether to adopt all, some, or none of the modifications in this section, on a case-by-case basis (though they cannot modify some provisions in a group and not others). However, we would expect firms to have regard to Principle 6 (“A firm must pay due regard to the interests of its customers and treat them fairly”) and not unfairly apply rules in one case but not another where the customers’ circumstances are otherwise the same.

(3) But the firm must have an internal switching policy in place and operate in accordance with it, if it wishes to rely on the rules in this section. This means that, if the firm has allowed a customer to
remortgage to it, it will allow the customer the benefit of the rules in this section again, or rely on MCOB 11.6.3R or MCOB 11.7 (if relevant), if the customer wants to switch again to a more affordable product with the firm (see MCOB 11.9.12R). In addition, the firm’s responsible lending policy (see MCOB 11.6.20R) must set out how the firm will apply the rules in this section.

(4) Where a customer has a payment shortfall and has entered into a repayment arrangement with their current mortgage lender, the customer should be treated as having a payment shortfall until such time as the shortfall is repaid. This would be the case even though the customer may have started to have a payment shortfall more than 12 months before the date on which they apply for the proposed regulated mortgage contract but they are (and have been) up to date with payments under the repayment arrangement. Where a payment shortfall has been capitalised in accordance with MCOB 13, the firm may treat the customer as eligible provided that the capitalisation occurred more than 12 months before the date on which the customer applies for the proposed regulated mortgage contract and the customer has made all the payments due under the mortgage contract during those 12 months on time.

The assessment of affordability

11.9.4  
(1) A firm may elect that the modifications to the rules in MCOB specified in (2) are to apply in relation to the proposed regulated mortgage contract. The firm may not elect that only some of those modifications apply in relation to the proposed regulated mortgage contract but not others.

(2) (a) MCOB 11.6.2R does not apply, but 11.9.5R applies in its place.

(b) MCOB 11.6.3R and 11.6.4E do not apply.

(c) MCOB 11.6.5R and 11.6.6R do not apply.

11.9.5  
(1) The firm must not enter into the proposed regulated mortgage contract unless that contract is more affordable for the customer (and any guarantor) than the existing regulated mortgage contract.

(2) The proposed regulated mortgage contract is more affordable than the existing regulated mortgage contract if:

(a) the aggregate amount of:

(i) the monthly payments due from the customer under that contract in respect of any discounted or introductory period, or (where there is no discounted or introductory period) in respect of the term of the proposed regulated mortgage contract; and

(ii) any product fee or arrangement fee due from the customer in relation to that contract, and any fee charged by a mortgage intermediary for arranging or advising on regulated mortgage contracts in relation to that contract, which the customer intends to pay without including it in the amount being lent under the proposed regulated mortgage contract;
is less than the aggregate amount due from the customer under the existing regulated mortgage contract (or all the existing regulated mortgage contracts, if more than one) in respect of the proposed regulated mortgage contract’s discounted or introductory period or (where there is no discounted or introductory period) in respect of the term of each existing regulated mortgage contract;

(2) the monthly payment that was due from the customer under the existing regulated mortgage contract (or the aggregate of the monthly payments due under all the existing regulated mortgage contracts, if more than one) in each of the 12 months before the date on which the customer applies for the proposed regulated mortgage contract, ignoring any atypical payments, was greater than:

(b) the typical monthly payment which would be due from the customer under the proposed regulated mortgage contract in any discounted or introductory period; or

(b) (where there is no discounted or introductory period) the typical monthly payment which is expected to be due for the term of the proposed regulated mortgage contract; and

(2) the interest rate applicable under the proposed regulated mortgage contract:

(c) in respect of any discounted or introductory period; or

(c) (where there is no discounted or introductory period) that which is expected to apply during the term of the contract;

is lower than the interest rate currently applicable under the existing regulated mortgage contract (or each existing regulated mortgage contract, if more than one).

11.9.6 (1) MCOB 11.6.7G does not apply in relation to a regulated mortgage contract entered into under rules disapplied by virtue of MCOB 11.9.4R.

(2) MCOB 11.9.5R(2) determines whether one regulated mortgage contract is more affordable than another. The references in that rule:

(a) to a discounted or introductory period include, for example, any fixed rate period after which a different interest rate applies, and any period in respect of which interest is deferred. Where interest is due in respect of a discounted or introductory period but is deferred, it is the gross rate payable that should be considered for the purposes of the conditions in MCOB 11.9.5R(2), as if interest were not deferred;

(b) to a typical monthly payment should be taken to ignore any payment in respect of a period greater or less than a month (for example, where a first payment is larger, or smaller, than that which would normally be due because it relates to a period greater or less than a month);

(c) to aggregate amounts due under the existing regulated mortgage contract should be taken to be on the assumption that that contract would not be redeemed early and would not incur an early repayment charge; and
(d) to future payments or interest rates should be taken to be on the assumption that there is no variation to the reference rate in question, unless the regulated mortgage contract expressly provides for a variation (for example, when considering a lifetime Bank of England base rate tracker, it should be assumed that the Bank of England base rate will remain unchanged).

### Assessment of income and expenditure

11.9.7 **R**

1. **A firm** may elect that the modifications to the rules in MCOB specified in (2) are to apply in relation to the proposed regulated mortgage contract. The firm may not elect that only some of those modifications apply in relation to the proposed regulated mortgage contract but not others.

2. (a) ■ MCOB 11.6.8R, ■ 11.610R and ■ 11.6.12R (income and expenditure) do not apply.

   (b) ■ MCOB 11.6.14R (future changes to income and expenditure) does not apply, but if the term of the proposed regulated mortgage contract extends beyond the date on which the customer (or, where there are joint borrowers, one of them) expects to retire or, where that date is not known, the date on which the customer will reach the state pension age, the firm must consider whether the customer’s income beyond that date would be sufficient to enable them to meet their commitments under the contract.

   (c) ■ MCOB 11.6.18R (considering the effect of future interest rate rises) does not apply.

11.9.8 **G**

1. ■ MCOB 11.9.7R modifies the affordability assessment required by ■ MCOB 11.6, in line with the modification to ■ MCOB 11.6.2R made by ■ MCOB 11.9.4R. This is on the basis that a customer who has evidenced an ability to afford a mortgage at a higher monthly payment than that which would be charged under the proposed regulated mortgage contract may be treated as likely to be able to afford the proposed regulated mortgage contract.

2. ■ MCOB 11.6.9G, ■ 11.6.11G, ■ 11.6.13G and ■ 11.6.15G do not apply in relation to a regulated mortgage contract entered into under rules which are disapplied by virtue of ■ MCOB 11.9.7R.

3. If the term of the proposed regulated mortgage contract extends beyond the date on which the customer (or, where there are joint borrowers, one of them) expects to retire or, where that date is not known, will reach the state pension age, the firm should take a prudent and proportionate approach to considering whether the customer’s income beyond that date would be sufficient to enable them to meet their commitments under the contract. The degree of scrutiny to be adopted may vary according to the period of time remaining to retirement when the assessment is made. The closer the customer is to retiring, the more robust the evidence of the level of income in retirement should be. For example, where retirement is many years in the future, it may be sufficient merely to confirm the existence of some pension provision for the customer by requesting evidence such as a pension statement; where the customer is close to...
retirement, the more robust steps may involve considering expected pension income from a pension statement.

(4) This section does not prevent a firm from undertaking an investigation of the customer’s financial circumstances before offering to enter into a regulated mortgage contract with the customer. Where a firm does so, it may take into account that the customer is not in payment shortfall and that the proposed regulated mortgage contract is more affordable than the existing regulated mortgage contract when determining the nature and degree of that investigation. In particular, the firm may also wish to consider whether it is necessary to require the same information from the customer as it would from a customer who does not currently have a regulated mortgage contract.

(5) If the firm is considering the effect of future interest rate rises on the prospect of the customer meeting their obligations under the proposed regulated mortgage contract, the firm may wish to have regard to the extent to which the interest rate applicable to the existing regulated mortgage contract is higher than that applicable to the proposed regulated mortgage contract. The firm may also wish to have regard to the fact that the customer is not in payment shortfall in relation to the existing regulated mortgage contract.

Interest-only mortgages

11.9.9 R

(1) A firm may elect that all of §11.6.41R, §11.6.43R, §11.6.46E, §11.6.46AR, §11.6.48R and §11.6.50R do not apply in relation to the proposed regulated mortgage contract.

(2) But a firm may not make an election under (1) if:

(a) the existing regulated mortgage contract is a repayment mortgage and the proposed regulated mortgage contract is an interest-only mortgage; or

(b) under the terms of the proposed regulated mortgage contract, the capital amount that will be outstanding at the end of that contract may be higher than that which would be outstanding at the end of the existing regulated mortgage contract (or the aggregate of that which would be outstanding at the end of each existing regulated mortgage contract, if more than one).

11.9.10 G


(2) §MCOB 11.6.49R (review during the term of interest-only mortgages) applies to an interest-only mortgage entered into by a firm which has made an election under §MCOB 11.9.9R(1).

Explanation of affordability assessment, and accompanying warning

11.9.11 R

(1) This rule applies if a firm makes an election under any of the following rules:
MCOB 11 : Responsible lending, and responsible financing of home purchase plans

Section 11.9 : Remortgaging with the same or a different lender with no additional borrowing

(1) MCOB 11.9.4R (assessment of affordability);
(2) MCOB 11.9.7R (assessment of income and expenditure);
(3) MCOB 11.9.9R (interest-only mortgages).

(2) The firm must provide the customer with an explanation which indicates:
(a) what steps the firm has taken to ascertain that the proposed regulated mortgage contract is more affordable than the existing regulated mortgage contract; and
(b) how the steps it has taken differ from the steps it would have taken under MCOB 11 if the firm had not applied rules in this section.

(3) The firm must accompany the explanation with a warning (as relevant to the individual case) that:
(a) interest rates may increase and the customer could end up paying a higher interest rate than they are currently paying under the existing regulated mortgage contract, even though the firm has assessed that the proposed regulated mortgage contract is currently more affordable;
(b) the firm’s assessment that the proposed regulated mortgage contract is currently more affordable has not taken into account any early repayment charges that the customer may incur in relation to repaying their existing regulated mortgage contract; and
(c) where the term of the proposed regulated mortgage contract is to end later than the term of the existing regulated mortgage contract, the customer may end up paying more in interest overall as a result of entering into the proposed regulated mortgage contract.

(4) The firm must provide the explanation and the warning:
(a) in a durable medium; and
(b) no later than the firm provides the customer with an offer document.

(5) The firm need not provide an explanation or a warning under this rule if a mortgage intermediary has already provided the explanation and the warning to the customer in relation to the proposed regulated mortgage contract.

Internal switching policy

11.9.12

(1) An internal switching policy is a policy which:
(a) is made or approved by the governing body of the firm; and
(b) commits or obliges the firm:
   (i) to permit an eligible customer to enter into a more affordable regulated mortgage contract (see MCOB 11.9.5R(2)); and
   (ii) to apply such of the rules in this section as may be necessary to enable that customer to enter into that contract (though
the firm may apply other rules in addition if it wishes), or to rely on § MCOB 11.6.3R or § MCOB 11.7 (if relevant) to enable that customer to enter into that contract.

(2) For the purposes of an internal switching policy, a customer must be eligible if:

(a) the firm has entered into the existing regulated mortgage contract as the lender;

(b) the firm chose to apply one or more of the rules in this section in relation to the existing regulated mortgage contract;

(c) the customer wishes to enter into a more affordable regulated mortgage contract with the firm (see § MCOB 11.9.5R(2)); and

(d) the customer meets the conditions in § MCOB 11.9.1R(2)(c)(i) and (ii).

If a firm has an internal switching policy but does not, without good reason:

(1) permit an eligible customer to enter into a more affordable regulated mortgage contract; or

(2) apply § MCOB 11.6.3R or § MCOB 11.7 (if relevant) or such of the rules in this section as may be necessary to enable that customer to enter into the more affordable regulated mortgage contract;

this may be relied on as tending to show contravention of Principle 6.

Notice to customers

(1) For the purpose of this rule, a customer is a notifiable customer if, when the firm makes the determination required by this rule:

(a) the customer meets the conditions in § MCOB 11.9.1R(2)(c)(i) and (ii), and there is no fee or charge which has become payable under the regulated mortgage contract and remains unpaid beyond the date on which it was due to be paid;

(b) the customer’s regulated mortgage contract is:

(i) not a lifetime mortgage; and

(ii) for residential purposes, and the customer does not have the lender’s consent to let the property; and

(c) the regulated mortgage contract had a discounted or introductory period which has expired (such that the interest rate payable by the customer under that contract is a reversion or standard variable rate).

(2) A firm with permission for administering a regulated mortgage contract must have, and operate in accordance with, a strategy for:

(a) determining whether each of the customers in relation to whom the firm is carrying on that activity for an unregulated owner is a notifiable customer; and

(b) giving the notice required by this rule at least once to each such notifiable customer.
(3) For the purposes of (2), an unregulated owner is a person who does not have permission for entering into a regulated mortgage contract and:

(a) who entered into the regulated mortgage contract as lender; or

(b) to whom the rights of the lender under regulated mortgage contract have passed by legal or equitable assignment, or by operation of law.

(4) A firm which has permission for entering into a regulated mortgage contract but is no longer carrying on that activity in relation to a particular portfolio or book of regulated mortgage contracts must have, and operate in accordance with, a strategy for:

(a) determining whether each of the customers in that portfolio or book is a notifiable customer; and

(b) giving the notice required by this rule at least once to each such notifiable customer.

(5) The notice must:

(a) include a statement to the effect that it has recently become simpler for a customer to enter into a more affordable mortgage with another lender if the customer is not looking to borrow any more than they currently owe under their mortgage and has kept up to date with their mortgage payments over the last 12 months; and

(b) refer the customer to sources of information about how to switch their mortgage to a lender who applies the rules in this section.

(6) A notice under this rule must be in a durable medium.

(7) A firm is not required to give a notice under this rule to a customer in relation to a regulated mortgage contract if another person has given such a notice to the customer in relation to that contract.

11.9.15 R

(1) The governing body of the firm must adopt or approve the strategy required by MCOB 11.9.14R no later than 1 May 2020.

(2) The firm must make the determination and give the notice required by MCOB 11.9.14R no later than 1 September 2020.

11.9.16 G

In developing and implementing their strategy for notifying relevant borrowers of the possibility of switching lender under this section, firms should have regard both to the purpose of this section and to the likely timescales for lenders to be ready to offer mortgages to borrowers in reliance on the rules in this section. For example, they should neither notify borrowers before there are lenders ready to make use of the rules in this section, nor delay sending notices until shortly before 1 September 2020 (as to do so might leave borrowers paying for a less affordable mortgage for longer than is necessary).
Section 11.9: Remortgaging with the same or a different lender with no additional borrowing