

**MORTGAGE...MORTGAGE...MORTGAGE...MORTGAGE...MORTGAGE...MORT****Welcome to Mortgage Target...**

Welcome to the inaugural edition of Mortgage Target; the newsletter tailored for Paradigm Mortgage Firms that will cover the important issues arising in the regulatory world. Each quarter we will aim to provide you with the most relevant articles, written in an easy manner and more importantly highlighting the potential impact on your day-to-day business.

We begin this Autumn edition of Mortgage Target with a look at the FSA's approach to strengthen the industry's defences against mortgage fraud and how this may affect Paradigm Mortgage Firms.

Also inside this issue, we provide an overview of the findings from the FSA's review of quality of advice processes, including useful examples of good and poor practices. We also have a round up of the governments rescue initiatives aimed at kick starting the housing market.

We provide further useful information on the replacement of the RMAR by GABRIEL, including a recommendation to print off your previous RMAR returns which otherwise will be lost when the systems switch over.

If you have any comments or constructive feedback regarding Mortgage Target, please e-mail suecaughtry@paradigmmortgages.com

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FSA Focus on Mortgage Fraud

On Tuesday 22 July 2008 the FSA wrote to the key trade bodies outlining their approach to strengthen the industry's defences against mortgage fraud and to make it harder for organised mortgage fraudsters to get away with their crimes.

As part of their approach, the FSA plans to visit 200 intermediaries to assess their financial crime systems and controls and to gather more information from lenders who may have spotted unusual applications. It will also work towards improving intelligence sharing across the industry and will review the Approved Persons regime specifically related to mortgage intermediaries and brokers.

As part of this a voluntary initiative was launched in 2006 by the FSA in collaboration with the Council of Mortgage Lenders (CML) and is called Information from Lenders (IFL). The aim of this is to identify how the industry could work together to reduce the risk of financial crime. IFL encourages lenders to declare cases where they have detected proven or suspected fraudulent mortgage applications which they consider serious enough to have the intermediary removed from their panel. Since the scheme began there have been over 300 reports of fraudulent activity and this has resulted in enhanced supervisory oversight for these firms, many of which have left the industry.

The CML Director General Michael Coogan commented on the FSA's announcement:

"We welcome the FSA's focus and practical approach in this area, and we expect that even more lenders will now participate in the voluntary initiative designed to identify and investigate broker fraud."

More information on the FSA/CML voluntary initiative can be found at:

http://www.fsa.gov.uk/pages/Doing/Regulated/supervise/mortgage_fraud.shtml

Within the last year the FSA have banned 17 individuals, whilst more have faced fines for committing fraud against banks and building societies. Cases have involved brokers making applications in their own names in order to defraud lenders, and consenting to customers inflating their incomes on application forms.

FSA Director of Enforcement Margaret Cole emphasised that "Perpetrators of fraud will increasingly find themselves facing bans and significant fines, as well as action by the police or other agencies aimed at confiscation of assets."

Paradigm Mortgage firms should continue to be vigilant and ensure you have effective and robust financial crime systems and controls in place. This includes providing relevant and effective financial crime training for staff and implementing and maintaining robust processes and procedures.



FSA Enforcement Action - Fraud

Year to date has seen the FSA take serious enforcement action against mortgage brokers and Paradigm cannot stress enough the importance and resource that the FSA apply to this area. The following are a small example of recent action taken by the regulator.

Gordon Benville, an IFA who traded as Kingsfield in Deal, Kent was sent to prison for three and a half years after pleading guilty to relate to obtaining money transfer by deception and other fraud offences.

Sadia Nasir, approved person and director of London Mortgage and Financial Services Ltd based in Ilford, London, was banned and fined £129,000 for being involved in numerous fraudulent mortgage applications.

The FSA banned a mortgage broker and fined him £100,000 for submitting false mortgage applications. Omotayo Fawole was an FSA approved person and sole controller of Oasis Mortgage and Financial Services Ltd (Oasis) based in Woolwich, South East London.

Calling all Mortgage Brokers...

The FSA has recently requested that mortgage brokers assist in the battle to combat mortgage fraud, by being sufficiently vigilant. If brokers have 'clear suspicions' of fraudulent activity by another broker (preferably backed up with evidence) they should report it directly to the FSA.

Philip Robinson, FSA's Director of Financial Crime and Intelligence division provided guidance for brokers in the role they play in assisting with the reduction of mortgage fraud:

- Brokers should ensure suitable advice is being given;
- Firms should ensure that their businesses cannot be used as a means to carry out fraud;
- A firms systems and controls must be robust enough to ensure a reduction in fraud; and
- Firms should continue to relay vital information to the FSA in order to ensure industry wide success in the reduction of mortgage fraud.

Firms should be on the look out for:

- Suspected fraudulent documentation
- False – or doubts about – income and employment details
- Links or trends between clients

This is not meant to be an additional burden to firms but part of their regulatory responsibilities. Firms should ensure that they have robust systems and controls in place to prevent their own firms being used for committing fraud.

Over the coming weeks the FSA will be visiting firms to assess whether they are being used for mortgage fraud.

The FSA have provided guidance for brokers on how to report suspected fraudulent activities. The following guidance should be considered in addition to statutory duties to report suspicious activities:

If in discussions with clients you learn that other brokers have been:

- Encouraging applicants to inflate their income or provide false employment details;
- Offering clients access to false documentation to support mortgage applications.

The FSA also provide information on what to provide in reports including a template reporting document which brokers may want to use.

Further information about how to use this form and how to report fraudulent activities by other brokers can be found at:

http://www.fsa.gov.uk/pages/Doing/small_firms/mortgage/library/report_fraud.shtml

The general consensus from the industry is that both intermediaries and the FSA have a part to play in helping reduce fraud. In a recent article in Mortgage Solutions Emma Tyler from OFM Group provided her opinion “it is down to intermediaries to help reduce fraud-help being the operative word alongside the FSA” and Melanie Brian from Savills Private Finance comments were “the FSA may need to make more of an intervention and provide more supervision, as well as support.”

FSA call for Firms to continue to Treat Customers Fairly despite current market conditions

Last month the FSA called once again for firms to ensure they continue to treat customers fairly in current market conditions. In a recent review the FSA found that the way in which some clients are being treated, particularly those with impaired credit histories, was unfair and inflexible. Whilst the number of customers facing repossessions and arrears is at an all time low they are actually on the increase and the FSA are warning firms that they should be flexible and repossession should be a last resort.

Whilst we appreciate that Paradigm Mortgage firms are not money lenders we recommend that you continue to ensure that all customers are treated as individuals and that all their current needs and circumstances are considered when making a recommendation that involves borrowing money.



FSA Review of Quality of Advice Processes

The FSA explained in its last Annual Report that for many people borrowing money to buy a home is one of the biggest financial commitments they will make and it is vital that they are treated fairly by mortgage lenders and intermediaries. This is not a new concept. The FSA focused on this area early last year when they carried out a review of the quality advice provided by financial advisers and firms in relation to mortgages. They found many areas of weakness and so provided firms with tools to assist them in improving the quality of advice provided to their clients. This included publishing examples of good and poor practice in June 2007.

Earlier this year the FSA conducted a second review of the quality of advice in mortgage intermediaries to establish if firms had made improvements to their advice processes. Additionally the FSA want to ascertain how successful the communication process from the first review had been in educating and raising standards to ensure firms have robust advice processes in place.

Approximately 250 firms, of which 220 were smaller firms, were reviewed through a range of telephone assessments, visits or mystery shops

The review focussed on 6 key areas:

- Management controls
- Assessment of customer needs and affordability
- Recommendations including product research
- Communications with customers
- Quality of advisers (training and competence)
- Post sale

The overall findings from the FSA are that quality of firms' mortgage advice processes is still not up to the required standard and that not enough progress has been made since the first review as many of the areas identified as having weaknesses continue to be a concern.

These are some of the key findings:

- Approximately half of the small firms visited were not gathering appropriate or making proper use of it.
- Many of the small firms visited and mystery shopped were not adequately assessing income and expenditure.
- Lack of affordability assessments where the mortgage term continued beyond the customers' stated retirement age. On a number of occasions firms did not consider the plausibility of the customer's stated retirement age in relation to their occupation.
- Many files relating to higher risk products did not adequately demonstrate suitability.
- Many firms failed to appropriately monitor the quality of advice in the files mentioned above.
- In over half of interest only cases there was no planned repayment vehicle in place to cover the remaining capital.
- In approximately one third of sub prime cases there was no justification as to why this type of product was appropriate.
- In over half the self-certification cases there was a distinct lack of justification as to why this product was more suitable than a full status product.
- In most of the firms visited suitability letters, for example, were not well tailored to individual circumstances.

Once again the FSA have published examples of good and poor practice. Some of which we have outlined for your convenience on the following pages. Other examples and case studies can be found at:

http://www.fsa.gov.uk/Pages/Doing/small_firms/mortgage/practice/advice/index.shtml

FSA Review of Quality of Advice Processes

Examples of Good & Poor Practices

Assessment of Customer Needs

Nearly half the files reviewed in this project did not contain sufficiently documented 'know your customer' information. Fact find documents were inadequate or not sufficiently completed.

Affordability

Assessment of affordability was not inadequate in over a third of the cases reviewed. The FSA found particular weaknesses where the loans extended into retirement and around the self-certification of income. Record keeping was also weak.

Examples of good practices

- Firm uses a detailed budget planner in the fact find to identify a net disposable income figure and affordability; this is then discussed with the customer to agree how much the customer is willing to commit towards the mortgage.
- Firm looks to help customers repair their credit. The client is referred to a credit counselling service or Citizens Advice, where debt consolidation through remortgaging might not be appropriate.

Examples of poor practices

- Affordability assessed on the customer's income and costs of servicing debt only. No account taken of household and other regular expenses incurred by the customer.
- Affordability assessed on gross income figure in budget planner, with no account taken of deductions for tax or national insurance.
- No income and expenditure assessment carried out before the recommendation. Reliance is placed solely on the customer stating they can afford the payments.

Mortgages into retirement

Examples of good practice

- The firm identified the customer's planned retirement date and, where relevant, the details of their post-retirement income and changes in outgoings to assess affordability throughout the product term.

Examples of poor practice

- Failing to consider affordability into retirement where mortgage terms run past the customer's planned retirement date. The firm did not collect information on the customer's income in retirement and therefore could not demonstrate suitability of their recommendation.

Self certification

Examples of good practices

- Clarifying why customers need to self-certify and recommending full status where this is more appropriate.
- Where a customer has income from various sources including PAYE and wishes to self-certify their income, the firm verifies the customer's main income.
- Firm implements a policy not to recommend self certification to full-time employed customers with no other sources of income.

Examples of poor practices

- No clarification of why the customer needs to self-certify and whether a full status application would be possible. This may result in the customer paying a higher mortgage rate than necessary.
- Failure to undertake plausibility checks on income information supplied by customers. In cases where the customer over-estimates or exaggerates their income, there is a risk the customer may not be able to afford the mortgage payments, particularly where there are arrears or other credit problems. The firm may also be complicit in the submission of potentially fraudulent information to mortgage lenders.
- Failure to cross-reference details held on file, for example where the employment information supplied by the applicant does not agree with the employer's reference.

Training and competence

It is essential that senior management have appropriate training and competence schemes tailored to the firm's needs which are regularly reviewed and updated. This ensures a firm treats its customers fairly and provides suitable advice.

Examples of good practices

- Detailed pre-employment checks for new advisers.
- Well documented training and competence procedures, which were put into practice.
- Comprehensive training and personal development records kept up-to-date, noting reviews and observed interviews.

Examples of poor practices

- No formal process for assessing advisers as competent, relying on the previous employer's assessment or 'instinct'.
- Advisers lack product knowledge and lenders' underwriting requirements for the sub prime sector.

Communicating with customers

In cases where firms used suitability letters to inform the client of the reasons for their product recommendation, two thirds were considered to be inadequate.

Examples of good practice

- A brief questionnaire for completion by clients to establish their understanding of the recommendation.

Examples of poor practice

- Where suitability letters were issued, the firm used standard paragraphs and sentences without ensuring they were relevant to the customer. This resulted in unclear letters which potentially misled the customers and failed to explain why the recommendation had been made.

Post-sale

Examples of good practice

- The firm actively seeks to offer a credit repair facility to their customers and contacts them before the end of any mortgage scheme to discuss their future requirements. If the customer wishes to arrange a remortgage, they conduct a further fact find and obtain the customer's authority to carry out a new credit search. This assesses whether the customer's credit status has improved enough to consider remortgaging at a prime or near-prime rate.

Examples of poor practice

- A firm contacted customers twelve months after arranging a two-year fixed rate mortgage, as a courtesy call to see if everything was running smoothly. These calls often resulted in the customer remortgaging during the early repayment charge period of the initial mortgage. In many cases, the firm was unable to demonstrate that there was any financial (or other) benefit to the customer from re-mortgaging.

Non-advised sales

The scripted questions used by firms as part of their non-advised sales process were inadequate in a quarter of cases reviewed. The questions did not provide the firm with sufficient information to enable them to offer their customers a reasonable range of unbiased products.

Examples of good practices

- Telephone sales were recorded to monitor the sales team. Recordings were discussed in one-to-one meetings to discuss good and poor practice and improve performance.

Examples of poor practices

- Failure to use scripted questions for non-advised sales.
- Scripted questions do not provide the firm with sufficient information to justify the range of products offered to the customer.

FSA Enforcement Action - Suitability

Leybridge Ltd

On 21st August 2008 Mortgage Advisers Leybridge Ltd became the first casualty of this thematic review of advice. The firm exposed 425 customers to the risk of being mis-sold a mortgage by failing to provide suitable advice.

The regulator found that Leybridge failed to meet the FSA's requirements as follows

- The firm breached the FSA's Principle that "A firm must take reasonable care to ensure the suitability of its advice and discretionary decisions for any customer who is entitled to rely upon its judgment" by failing to record and maintain adequate information about customers' circumstances which led to the firm being unable to demonstrate the suitability of advice.
- The FSA also confirmed that Leybridge adopted inadequate file checking systems whereby mortgage processors would check each file for the existence of information rather than the standard of completion. Files were then only checked on a sample basis by Directors this was not a regular occurrence nor were the checks adequate. The system in place for recording these file reviews was also inadequate.

The FSA proposed a fine of £24,000 which Leybridge was unable to pay so it waived this to enable Leybridge to compensate its customers who may have been disadvantaged.

FSA director of enforcement Margaret Cole says: "Leybridge's record keeping was so poor that they could not demonstrate that the sales of mortgages were suitable and had no way of proving to us that the firm was treating its customers fairly."

We would have imposed a fine of £24,000 but had we done this the firm would not have been able to afford properly to carry out a customer redress exercise. The FSA decided that the priority was to ensure customers received a fair deal and so we waived the fine on this occasion."

Approved Financial Solutions Ltd

Earlier this month the FSA fined Derbyshire mortgage broker Approved Financial Solutions (AFS) £63,000 for failing to

- give suitable advice and
- communicate accurate information about mortgage charges to its customers.

Jonathan Phelan, Head of Retail Enforcement at the FSA, said:

"AFS's failings were serious because its sales process enabled vulnerable customers to apply for mortgage contracts that they could not necessarily afford. In giving the mortgage advice, AFS also failed to provide customers with accurate information about the mortgage contracts. The firm's customer base is largely sub-prime and many of them were seeking to re-mortgage to consolidate existing debts...Behind this poor compliance regime, we found that in all the sales files that we reviewed the customers had provided AFS with false income and employment information."

The FSA found that AFS failed in a number of areas which could have a detrimental effect on its customers:

- Lack of systems and controls in relation to monitoring the quality of advice provided by advisers
- Inadequate documented reasons for recommending suitable mortgage contracts
- Failure to disclose correct fees to customers
- The recommendation of self-cert mortgages when high street mortgages were more suitable

The FSA says that AFS co-operated fully and has been proactive in finding solutions to identified shortcomings and to improve the resourcing and quality of its compliance function.

Whilst AFS have made unsuitable recommendations to customers, a past business review was not deemed appropriate in this particular case as a lot of customers had provided false information about themselves.

AFS agreed to settle at an early stage of the FSA's investigation and therefore qualified for a 30% discount under the FSA's executive settlement procedure. Otherwise, the FSA would have imposed a financial penalty of £90,000.

GABRIEL - Important Information

With the FSA's new regulatory reporting system, GABRIEL, replacing the RMAR, you should have or will soon be receiving an email from the FSA, which provides details of where firms can find further information on GABRIEL. This includes an electronic leaflet containing an overview of the changes together with a link to a free online training package. Links to these two items are included below for your convenience:

[Integrated Regulatory Reporting – What's coming up for RMAR reporters](#)

[Online training package](#)

In addition, there are a couple of other areas where we feel it would be useful to provide some additional information for firms.

Print outs of previous RMAR returns

Once GABRIEL comes into effect any information regarding RMARs previously completed will be removed from the system and firms will no longer be able to access this data. In view of this **we recommend firms print off and save copies of previously completed returns for their records ASAP in order that they have a useful point of reference going forward.**

Input of Professional Indemnity Insurance details

Under GABRIEL, firms will need to input details of both their Professional Indemnity Insurance requirements and the particulars of the actual cover that they have in place. In our opinion, the required information for GABRIEL is likely to be the following and therefore firms may wish to note this information in preparation for GABRIEL's introduction:

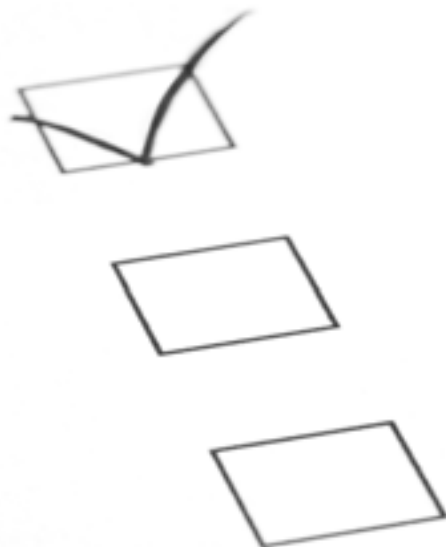
€1,000,000 for a single claim against the firm (sterling equivalent); and

€1,500,000 in the aggregate (sterling equivalent);

No more than £5,000 policy excess

Please note that GABRIEL will permit a choice of currency which you can input into your return (the default is £ sterling).

Firms may wish to note that as the limits in the FSA handbook are stated in Euros, firms must select a Stirling equivalent or greater at the time of taking out a new policy or on renewal. If the exchange rates drop or increase during the term of the policy that is fine but the indemnity limit should be reviewed at each renewal to ensure it is above the Euro minimum.



Housing Market — Government Rescue Package

Within the last month or so the government has announced a £1bn rescue package in the hope of kick starting the housing market. We thought it would be beneficial for Paradigm Mortgage Firms if we provided a summary of the rescue package for future reference.

The package includes:

- Equity loans for first time buyers
- Increase in Stamp Duty land tax relief
- Faster payment of income support for mortgage interest payments
- New powers to councils to bail out home owners on the threat of repossession

Loans for first time buyers

This offers free loans to first time buyers buying a new build house who have a household income of less than £60k. Potential home owners will be offered the chance to take out an equity loan of up to 30% of the property value which will be funded by the government and the developer. The government scheme is designed to assist approximately 10,000 first time buyers take the first step onto the property ladder.

Stamp Duty

Stamp duty land tax will not apply to purchases of residential property of £175,000 or less. This will provide an exemption from stamp duty land tax for land transactions consisting entirely of residential property where the chargeable consideration is not more than £175,000. This relief will apply to transactions with an effective date on or after 3rd September 2008 and before 3rd September 2009.

Mortgage Interest payments for people on state benefits

Mortgage interest payments will be paid for people on certain state benefits such as income support, pension credit and jobseekers allowance will be increased from £100,000 to £175,000 and application times will be cuts from 39 to 13 weeks.

Repossessions

Local authorities will be given extra funding to assist people in danger of having their homes repossessed. This will be assistance for more struggling homeowners through existing schemes such as sale and leaseback, shared ownership or more equity loans.

Industry Reaction

The various initiatives, some old, some new, have been met by a mixed response from the industry. With the average house price in July 2008 just over £175,000 at £178, 364* some believe that this increase is just not enough and there is scepticism as to how many first time buyers will actually benefit from this. On the other hand there has been more of a positive reaction in relation to the assistance which will be available for homeowners who face the nightmare of repossession. It should be noted that some rescue initiatives will not begin until April 2009.

*source: land registry



OFT launches consultation on irresponsible lending

On 1st August 2008, the OFT announced the launch of a public consultation looking at irresponsible lending in UK consumer credit markets. Paradigm Mortgage firms should be aware that as part of this consultation the OFT will consider all forms of consumer credit lending which the OFT licences and all participants in the market including lenders, brokers and other intermediaries.

This follows major changes to the Consumer Credit Act, in which the OFT must have due regard when it is considering firms' fitness to hold a licence. The main outcome is expected to be clear guidance on lending behaviours and practices which the OFT considers to be irresponsible.

The OFT has previously provided some guidance on what constitutes irresponsible lending in its general fitness guidance [General Guidance for licensees and applicants on fitness and requirements](#)

The OFT can refuse or revoke a licence if it decides that a trader is not fit to hold such a licence.

PARADIGM — BUSINESS CONSULTANTS FOR PROFESSIONAL ADVISERS

The regulatory environment is evolving quickly with a seemingly constant flow of new regulation and guidance being produced for firms to understand and implement within their businesses.

At Paradigm we understand the difficulties facing firms in not only finding the time to understand these changes and how they may affect their business, but also in successfully ensuring that these changes are implemented with the minimum effort and impact.

Our experienced team has a wide and varied knowledge that enables us to provide comprehensive guidance and also helps us to understand how this impacts on your business.

Through Paradigm Group we can provide regulatory consultancy support which includes:

- Financial Promotions
- Technical queries
- Remote File Reviews
- RMAR completion
- FSA Applications + Change of Entity/Variation of Permissions/Approved Persons
- Complaints Guidance
- Risk assessment and mitigation plans
- Monitoring plan design and audit,
- Treating Customers Fairly (TCF) and much more...

To find out how you can take advantage of our regulatory consultancy service please contact Sue Caughtry on 0845 688 1344 suecaughtry@paradiqmmortgages.com

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