FINANCIAL CONDUCT AUTHORITY

Finalised Guidance

Guidance for firms supporting their existing mortgage borrowers impacted by the rising cost of living

FG23/2

10 March 2023

Note: additional options are now available, outlined in PS 23/8

1 Summary

1.1 Many mortgage borrowers face higher mortgage payments alongside the rising cost of living. Borrowers may approach lenders needing or wanting to reduce, or smooth increases in, their monthly payments.

1.2 In December 2022 we consulted on draft general guidance which explains how firms can support their customers including through automated processes and digital channels. The guidance set out the flexibility firms have when providing forbearance to those who need it, and the scope firms have to vary contract terms for other borrowers who want to reduce their monthly payments.

1.3 We consulted on the content of the guidance for two weeks as we wanted to act quickly so firms were clear about the effect of our Rules, Guidance and Principles to protect consumers in these difficult times. We did not produce a cost benefit analysis as the guidance does not impose new expectations or requirements on firms. We considered that to consult for longer was unnecessary and could have caused a delay that may have been prejudicial to the interests of consumers.

1.4 The purpose of this guidance is to ensure firms are clear about the effect of our rules and the range of options they have to support their customers including those who are facing higher interest rates alongside the rising cost of living.

1.5 The finalised guidance can be found in Chapter 2 below and the feedback we received, along with our responses, can be found in the Feedback Statement in Annex 1.

1.6 The finalised guidance set out below explains how firms can comply with our existing Rules, Guidance and Principles. The guidance is not temporary but is subject to change if we make changes to our underlying Rules and Principles. Any other changes would be subject to consultation.

2 Guidance for firms supporting their existing mortgage borrowers impacted by the rising cost of living

2.1 This guidance explains how firms can support their customers including through automated processes and digital channels. It sets out the flexibility firms have when providing forbearance to those who need it, and the scope firms have to vary contract terms for other borrowers who want to reduce their monthly payments.

2.2 It should be read alongside the Mortgage Conduct of Business Sourcebook (MCOB) the Tailored Support Guidance (TSG), Guidance for firms on the fair treatment of vulnerable customers (VCG) and the June 2022 Dear CEO letter which confirm our expectations of firms.

Providing forbearance

2.3 In the Dear CEO letter, we said that the TSG is also relevant to borrowers in financial difficulties due to the rising cost of living. So, if a customer indicates that they are experiencing or reasonably expect to experience payment difficulties due to the rising cost of living, firms should offer prospective forbearance to enable them to avoid, reduce, or manage any payment shortfall that would otherwise arise. This includes customers who have not yet missed a payment (TSG paras 3.3, 5.9).

2.4 There are many different types of forbearance which are not limited to the options set out in our rules (at MCOB 13.3.4AR). Firms may offer payment concessions where they agree to accept less than the contractual monthly instalment (resulting in a payment shortfall), but they may also offer contract variations such as term extensions and temporary switches to interest-only. Not all firms will be able to offer contract variations.

2.5 Firms must act honestly, fairly and professionally in accordance with the best interests of their customers (MCOB 2.5A). Given this, Principle 6, and MCOB 13.3.4AR, any forbearance option(s) should be appropriate to a customer's individual circumstances.

2.6 Firms should be able to justify a decision to offer a particular forbearance option (MCOB 13.3.4CG, Principle 6).

Providing forbearance at scale

2.7 The TSG (para 2.8) confirms that firms have flexibility and scope to tailor their approach to meet the operational challenge of many customers needing help at the same time. Our rules and guidance do not impose prescriptive requirements about how a firm collects information on a customer's individual financial circumstances or how it ensures any forbearance option proposed is appropriate for that customer given their individual circumstances (TSG para 2.9). Firms can use automation or digital tools to:

- automate processes, such as asking borrowers to provide information on their circumstances, including their income and expenditure
- offer a customer a forbearance option the firm has identified as appropriate to the customer’s individual circumstances, and seek the customer’s agreement to it
- offer a customer a range of options that the firm has identified as appropriate to the customer’s individual circumstances for the customer to choose from

2.8 In the context of the rising cost of living, a firm may be able to offer a group of customers with similar needs and circumstances a range of options that are appropriate to their circumstances.

2.9 Firms should have policies, procedures and controls in place to avoid agreeing inappropriate forbearance arrangements with customers who may have more complex needs, including those who may be in more vulnerable circumstances due to physical or mental illness, unemployment or other characteristics of vulnerability.

2.10 Information can be provided to customers digitally, although some may not have access to online channels or may find digital interactions difficult. Firms should therefore offer to engage with customers in different ways, including through a range of channels and, where possible, give customers the ability to switch between them (TSG paras 5.33-5.34).

Contract variations for the purposes of forbearance

2.11 Firms may vary a contract without assessing affordability (as set out in MCOB 11.6.2R) when doing so solely for the purposes of forbearance where the customer has a payment shortfall, or in order to prevent one occurring (MCOB 11.6.3R(3)). This could include a contract variation which switches a repayment mortgage onto an interest-only basis for all or part of its term, or extends the mortgage term into (or further into) retirement.

2.12 When dealing with a customer who is in or at risk of payment shortfall, firms may, where appropriate, vary a contract to accept payment on an interest-only basis for a temporary period without evidence of a clearly understood and credible repayment strategy (MCOB 11.6.43R). A variation is unlikely to be considered appropriate and temporary if, after the temporary period is over, the customer is not obliged to make payments of interest and capital which are designed to repay the mortgage in full over the remaining term.

2.13 If permanently varying a contract to an interest-only mortgage, a firm would need to have evidence of a clearly understood and credible repayment strategy (MCOB 11.6.41R).

2.14 A firm would need to demonstrate that in offering a variation under forbearance it is acting fairly and in accordance with a customer’s best interests (Principle 6, MCOB 2.5A), and that the change is appropriate to the customer’s individual circumstances.

Implications of forbearance arrangements

2.15 Firms must give customers adequate information to understand the implications of any proposed arrangement (MCOB 13.3.4AR(2), TSG paras 4.7 and 5.29-5.30). Firms should ensure they give customers timely information to enable them to

understand their financial position and their options (TSG para 5.29). This could include information on the impact of deferring payments of interest or capital on the total amount payable.

2.16 Firms should ensure they are clear in their communications about the credit file implications of any forms of support they offer customers, including rescheduling or refinancing of accounts (TSG para 4.7).

Customers not requiring forbearance – but wanting to reduce their monthly payments (contract variations)

2.17 Firms may offer a range of contract variations to support borrowers who would like to reduce their monthly payments, and our rules allow this regardless of whether customers are facing payment difficulties. Not all firms will be able to offer contract variations. A firm can vary or replace an existing contract without undertaking an affordability assessment provided there is no additional borrowing or change to its terms which is likely to be material to affordability (MCOB 11.6.3R).

Interest rate switches

2.18 Firms may offer borrowers the ability to switch their interest rate. Where there are no other changes to the terms of their contract, and the interest rate change is not material to affordability, the requirement to undertake an affordability assessment will not apply (MCOB 11.6.3R).

2.19 A borrower may be switching from an expiring fixed (or otherwise incentivised) rate to a higher incentivised or fixed rate. To determine whether this change would be material to affordability (and therefore whether the requirement to undertake an affordability assessment will apply) firms can compare the proposed new rate to the rate the customer would pay if not for the change – such as any standard variable rate (SVR) that would apply once the current deal expires.

Term extensions

2.20 Some customers seeking to reduce their monthly payments may want to extend the term of their mortgage. An affordability assessment will not generally be required for term extensions up to the customer's expected retirement age if there are no other changes to the terms of the mortgage (MCOB 11.6.3R).

2.21 Where the term is extending into (or further into) retirement, it is more likely that the change would be material to affordability (see MCOB 11.6.4E), in which case an affordability assessment would be required.

Variation to interest-only

2.22 Some borrowers seeking to reduce their monthly payments may want to switch their repayment mortgage onto an interest-only basis for all or part of its remaining term.

2.23 A firm may agree to vary a contract from a repayment mortgage to an interest-only mortgage (permanently or temporarily) if it has evidence that the customer will have in place a clearly understood and credible repayment strategy (MCOB 11.6.41R).

2.24 A firm will need to undertake an affordability assessment (under MCOB 11.6.2R) and the cost to the customer of their repayment strategy must form part of this (MCOB 11.6.5R(2) and 11.6.48R). This would include situations in which the repayment strategy is for the mortgage to revert to a capital and interest repayment basis after an interest-only period.

Implications of contract variations

2.25 MCOB 7 sets out relevant disclosure requirements when making certain types of contract variations (see for example MCOB 7.6.28R when the variation would change the amount of each payment due). More generally, firms should give customers relevant and timely information to enable them to understand the implications of any variation of terms (Principles 6 and 7).

Exceptions to the requirement to provide advice

2.26 MCOB 4.1.4R(2) explains that MCOB 4 applies in relation to any form of variation of a regulated mortgage contract. These rules often require a firm to provide advice as part of an interactive sale (MCOB 4.8A), but there is greater flexibility when varying a contract. This flexibility includes:

- variations to the mortgage contract made solely for the purposes of forbearance (MCOB 4.8A.19R) and;
- variations not made for forbearance purposes, provided they do not involve additional borrowing and, where the change includes a rate switch, the customer is presented (via a non-interactive channel) with all products offered by the firm for which the customer is eligible (MCOB 4.8A.10R).

2.27 This means that, where appropriate, firms could provide forbearance or offer borrowers options, such as term extensions up to retirement and rate switches, at scale on an execution-only basis via digital channels, for example to meet requests for support in volume.

Annex 1 Feedback Statement

1. In December 2022 we consulted on draft general guidance which sets out the flexibility firms have when providing forbearance to those who need it, and the scope firms have to vary contract terms for other borrowers who want to reduce their monthly payments.

2. We received 27 responses from a range of stakeholders including 1 consultancy, 14 consumer representatives and 12 firm representatives (including 7 industry trade bodies). We are grateful for the detailed and helpful responses we received and would like to thank those who responded to this consultation. This Feedback Statement summarises the feedback we received and our response.

3. Respondents welcomed the guidance. Industry representatives supported the focus on being able to consider a range of options to help borrowers depending on their circumstances. They sought clarification on some technical aspects of the guidance. Consumer representatives also generally agreed with an approach which encouraged firms to consider a range of options, but some asked for the guidance to go further and require firms to offer certain options.

4. The updated guidance, published today, is largely unchanged. It includes 3 small amendments which are summarised at the end of this statement.

5. The guidance advances our consumer protection objective and is designed to protect existing mortgage borrowers who are struggling to make payments due to increases in the cost of their mortgage as well as the wider impact of the rising cost of living. It ensures firms are clear about what tools they can use to support customers in different circumstances. It is effective immediately. We also consider the additional clarity provided by the guidance ensures it is consistent with our duty to promote (so far as is compatible with advancing, in this case, our consumer protection objective) effective competition in the interests of consumers. We have considered the different impacts of the proposals on firms and consumers. We do not consider our guidance will adversely affect consumers with protected characteristics under the Equality Act 2010. Alongside our guidance, we published consumer communications to help potential first-time buyers and existing borrowers affected by rising prices.

Next steps

6. The guidance explains how firms can comply with our existing Rules, Guidance and Principles for Businesses. It is not temporary but is subject to change, for example if we make changes to our underlying rules. Any other changes would be subject to consultation.

7. We have published final rules and guidance for a new Consumer Duty which comes into force on a phased basis from 31 July 2023. Firms will need to consider what impact the Duty might have on the range and nature of customer support measures offered.

8. We will continue to review how firms are delivering against our expectations and check they are treating customers fairly. We will take robust action where we identify firms who are delivering poor customer outcomes.

Summary of feedback and our response

9. This section summarises the feedback received on our draft guidance and our response to this.

Alignment with our expectations of firms

10. Many of the 14 responses from consumer representatives wanted the guidance to be more prescriptive and set out expectations that firms act in a particular way. Recognising that not all firms offer contract variations, some respondents wanted us to direct all firms to provide all options. Four respondents suggested that firms be required to explicitly set out the help the lender can consider, for example on their websites. Other respondents sought assurance that we would check that firms treat customers fairly.

11. Responses from firms and trade bodies were concerned that some media reports had misinterpreted the guidance by suggesting that all borrowers would be able to vary their contracts, without affordability or appropriateness checks, when this is not the case. They asked that we make it clearer that while all firms are committed to support borrowers in payment difficulty, including by considering temporary payment concessions, not all firms would be willing or able to agree to contract variations.

12. Firms and trade bodies wanted us to emphasise that although reductions in monthly mortgage payments may bring short-term relief to those worried about increased costs, ultimately this will increase the cost of their mortgage over time and result in more interest paid overall. They were concerned that we emphasise that it is important that consumers pay their mortgage where they can afford to do so.

13. The Money and Pensions Service also suggested the Guidance could include a reference to MoneyHelper.

Our response

14. As consumers are affected by the rising cost of living it is critical that firms and mortgage administrators meet the standards we expect to support their borrowers, including those in financial difficulty.

15. This guidance clarifies the effect of our existing rules and principles and is not intended to set new expectations or requirements of firms or to repeat the position set out in other documents such as the expectations around repossessions or the treatment of vulnerable customers. It explains how firms can support borrowers in, or at risk of, payment difficulty and confirms the flexibility firms have under our rules and guidance to support borrowers in different ways.

16. We agree that borrowers should only seek help to reduce their mortgage payments where they need to. The guidance does not oblige firms to agree to contract variations. Where contract variations are agreed, firms are required (unless they are acting for the purposes of forbearance) to demonstrate the borrower can afford their mortgage payments under the revised terms unless the change is not material to affordability. When providing forbearance firms need to demonstrate they are acting

fairly, in accordance with a customer's best interests, and that any arrangement is appropriate given a customer's individual circumstances.

17. Our expectations of firms include:

- Considering what more they can do to encourage mortgage borrowers to think about switching to a less costly option *where that is available*.
- Giving *all* borrowers in payment difficulty appropriate forbearance that is in their interests and that takes account of their circumstances.
- Providing *all* customers with an appropriate level of care and support. The level of care needed for customers who have characteristics of vulnerability may be different from that for others and firms should take particular care to ensure they are treated fairly. Our Vulnerable Customer Guidance (VCG) sets out our view of what firms should do to comply with their obligations under our Principles and ensure they treat customers in vulnerable circumstances fairly.
- Supporting borrowers in payment difficulty or struggling with debt, by making them aware of, and helping them access, money guidance or free debt advice.
- Ensuring that any fees and charges levied on any borrower because they are in payment shortfall are fair and do no more than cover a firm's costs.
- Being transparent about the range of options they can consider when a customer is facing financial difficulties to enable customers and those advising them to understand and evaluate the options. Where possible firms should set these out on their websites.

18. This list is not exhaustive. We already expect borrowers in arrears to be provided with a specific MoneyHelper guide (MCOB 13.4.1R), but we agree that firms may find it helpful to refer to Moneyhelper in their communications with customers.

19. We want firms to focus on improving the quality of services offered so we will continue to test the way firms support borrowers in financial difficulty. We will continue to review how firms are delivering against our expectations and check they are treating customers fairly. We will do this by collecting and reviewing data from firms on the outcomes for consumers. We will identify firms who have a higher concentration of customers who may be at risk of financial difficulty over the coming months, as well as firms whose outcomes, when compared to their peers, suggest that they may not be delivering the support we expect. We will take robust action where we identify firms who are delivering poor customer outcomes.

When forbearance applies

20. Some respondents, including trade bodies and firms, asked if we could provide more guidance on when a borrower, at risk of a payment shortfall, would be eligible for forbearance.

21. Firms and their trade bodies asked us to set out a clear statement on the principles and objectives of forbearance recognising the risks of over-forbearance and the role of repossession in the event that a borrower cannot recover their position and home ownership is unsustainable. One trade body suggested a customer should have to

demonstrate the need for forbearance rather than simply indicate that they are experiencing or reasonably expect to experience payment difficulties.

22. We were also asked to clarify how the guidance will interact with the incoming Consumer Duty, to define terms such as 'borrowers impacted by the rising cost of living', 'temporary', 'financial difficulty' and 'payment difficulty', and to explain the information firms should collect to demonstrate when temporary support is appropriate.

Our response

23. The guidance is clear that a firm should offer prospective forbearance if a mortgage borrower indicates that they are experiencing or reasonably expect to experience payment difficulties due to the rising cost of living. This includes customers who have not yet missed a payment. We do not expect firms to ask a borrower for evidence that they will otherwise miss payments before offering forbearance.

24. The objective of forbearance is to give customers time to adjust so that they can pay their mortgage in the long term. We do not think it is necessary, appropriate, or practical to define 'forbearance' or borrowers who may, or may not, be in financial difficulty (or who face payment difficulty) due to the rising cost of living or where support will be temporary or appropriate. Doing so could have unintended consequences where similar terms are used for other regulatory purposes. Firms should focus on providing appropriate support to customers in need and, for the purpose of applying this guidance, approach such terms in light of their ordinary meaning and the purpose of the forbearance provisions.

25. Firms are not obliged or required to provide advice when varying a contract (or providing forbearance). A borrower may choose to seek advice including from a third-party. Any lender fees for varying a contract or fees for advice should be disclosed before proceeding and any fees and charges levied on any borrower because they are in payment shortfall must be fair and do no more than cover a firm's costs (MCOB 12.4).

26. Firms have flexibility to consider what information they may need to demonstrate that forbearance agreed is appropriate and in accordance with a customer's best interests. Firms will need to determine, given their business model and customer base, what further actions they may need to take to demonstrate good customer outcomes under the Consumer Duty.

Proactively contacting, and responding to, borrowers at risk of missing payments

27. Several consumer respondents suggested our guidance should direct firms to proactively reach out to borrowers in payment difficulty or at risk of missing payments rather than relying on customers to contact them when they may not realise they are eligible for help or not know how to go about getting it. Two respondents raised concerns that some firms are turning away borrowers who have not yet missed payments, and that some firms do not contact borrowers even after they have missed payments. Two suggested all firms should offer support to all

customers facing increased payments including those who face higher payments because their fixed rates are expiring.

28. One consumer representative suggested the guidance could place greater emphasis on a firm having to act in the best interests of borrowers - and that firms be required to justify why options not used were not in a customer's best interests. One trade body asked for clarity that an income and expenditure assessment is still required when considering forbearance for a customer, including for those who had not yet missed payments.

Our response

29. The focus of this guidance is to ensure firms are clear about how they can support customers who may be struggling with their mortgage payments. We complemented our consultation with consumer communications designed to encourage borrowers who are struggling to contact their lender or seek out other sources of support and help.

30. In November 2022, we published our key findings from our Borrowers in Financial Difficulty work including the need for some firms to more effectively engage with borrowers in financial difficulty. For customers who had missed a payment, we found some firms did not do enough to engage with them. We said that firms should be clear that they want to help customers and set the right tone. Firms should also offer to engage with customers in different ways, including through a range of channels, taking into account expectations set out in the VCG for the fair treatment of customers in vulnerable circumstances (FG21/1, Chapter 1).

31. As the impact of the rising cost of living continues, we expect that more customers will need support from their lenders. Although our rules do not require mortgage firms to proactively identify and contact borrowers at risk of payment shortfall, we have already encouraged firms to think about what they can do to meet our expectations to support customers who need help. Some firms, such as lenders who are also current account and credit card providers, may have more data than others and may have more scope to identify borrowers more vulnerable to payment difficulty. Others may want to consider the appropriateness of more generic outreach communications. Firms should make it clear to borrowers how they can seek support if they are in payment difficulty. Where firms are aware that a borrower needs support, including where a borrower contacts them asking for forbearance, a firm should not wait until the borrower misses payments before considering what support it is appropriate to offer.

32. When providing support, a firm needs to demonstrate it is acting fairly and in accordance with a customer's best interests (Principle 6, MCOB 2.5A) taking account of their individual circumstances. A borrower's current and future income and expenditure may be a relevant consideration when considering what is appropriate but there is no specific MCOB requirement that a firm carry out an income and expenditure assessment in a particular case (whether or not the customer has yet missed payments). Although it may be good practice, there is no expectation in MCOB that firms explain why alternative options are not in a customer's best interests. However, we do expect firms to be able to justify a decision to offer a particular option (MCOB 13.3.4CG).

33. We want firms to focus on improving the quality of services offered so we will continue to test the way firms support borrowers in financial difficulty. We will take robust action where we identify firms who are delivering poor customer outcomes.

Providing forbearance using automation at scale

34. Trade bodies generally welcomed the guidance on the existing flexibility available should demand for support increase, but three saw challenges in designing an approach that could meet the FCA's expectations that firms do not take a 'one size fits all' approach and be compatible with the incoming Consumer Duty. Two trade bodies and one firm asked for clarification of firms' ability to offer more than one appropriate option. They suggested this was inconsistent with expectations in the TSG and the FCA's findings that firms relying on customers to determine what they could pay or select their payment arrangement was poor practice. Respondents also raised concerns about the need to manage expectations, presented by the media, that incorrectly suggested that all borrowers would be able to self-serve from a wide menu of available options.

35. Six consumer representatives raised concerns that allowing firms to provide forbearance on-line without a discussion was unlikely to meet the needs of more vulnerable consumers such as those who struggle to engage through digital means and those with more complex needs such as a serious illness. One raised concerns about the ability of firms to act in a customer's best interests. Another said their own work suggested that firms were not doing enough to ensure they supported such borrowers, for example by properly taking account of the specific individual needs of borrowers including the impact of any prognosis for those with serious illnesses, which is exacerbated by the rising cost of living.

36. Consumer representatives wanted stronger interventions to ensure forbearance, and access to firm staff, is inclusive and available. They also wanted confirmation of stronger sanctions where there is evidence that borrowers face barriers to accessing support. Two respondents wanted firms to have to consider any requests from borrowers for alternative options, including where the borrower presented additional information about their circumstances.

Our response

37. One of the aims of the guidance is to confirm that firms who may be facing large volumes of requests for support may be able to take a differentiated approach depending on the needs and circumstances of different customers. For example, some customers may need a little help to smooth the sharp increases in their monthly payment. Others need more bespoke support. By automating support for customers for whom it is appropriate, it may be possible for firms to preserve the more limited availability of their expert case handlers for those customers who need most support. The guidance is permissive so where firms do not want to, or cannot, automate or digitise the process to provide appropriate forbearance, they do not need to do so.

38. Our recent Borrowers in financial difficulty findings highlighted that ineffective engagement with customers in more vulnerable circumstances can lead to poor outcomes, with inappropriate and unsustainable arrangements that are overly

focused on arrangements to repay shortfalls. We agree that those with serious medical conditions, as well as those with other characteristics of vulnerability such as unemployment, are more likely to need more tailored support that clearly takes account of their specific short-term and longer-term needs and circumstances.

39. While firms do have scope to automate support for a group of customers with similar needs and circumstances and offer them a range of options, they will first need to be able to determine that any option offered is appropriate to the customer's circumstances. The guidance confirms that they should have controls in place to avoid agreeing inappropriate forbearance arrangements with customers, including those customers who have more complex needs.

40. The guidance also notes that although information can be provided to customers digitally, firms should, wherever possible, offer to engage with customers in different ways. The support offered should recognise that some customers may not have access to online channels or may find digital interactions difficult.

41. We have clear expectations about how borrowers should be treated, and we will continue to supervise and enforce our existing rules. We will take robust action where we identify firms who are delivering poor customer outcomes. However, where a borrower feels they have been treated unfairly or is unhappy with the support offered they can complain to the firm. If the borrower is unhappy with the firm's response, they can refer their complaint to the Financial Ombudsman Service who will consider what is fair and reasonable.

Taking account of wider indebtedness

42. Some respondents asked whether the scope of the guidance extended to all products held by the customer and suggested the guidance should require firms to have regard to other debts and priority commitments such as energy bills. One trade body asked whether TSG paragraph 5.24, which addresses borrowers having difficulties with other priority debts, applied.

Our response

43. We confirm that we consider the expectations in paragraph 5.24 of the TSG, that firms take account of wider borrower indebtedness and other priority debts, to be relevant to borrowers struggling due to the rising cost of living.

Contract variations for the purposes of forbearance

44. One firm asked for clarification as to whether they would need to assess affordability before agreeing to extend a borrower's mortgage term into their retirement for the purposes of forbearance. A trade body asked for further guidance on how a firm should go about mitigating the risks of agreeing a temporary switch to interest-only if it did not assess affordability or seek evidence of a credible repayment strategy. Further questions about temporary variations to interest-only are considered at paragraphs 83-92.

Our response

45. When acting for forbearance, firms have more flexibility under our rules. The assessment of affordability otherwise required by MCOB 11.6.2R where a variation of contract is material to affordability, does not apply. However, a firm will still need to demonstrate that it is acting fairly and in accordance with a customer's best interests and taking account of their individual circumstances. This may include considering the impact on current and future affordability.

46. Where a firm is extending a customer's mortgage term into retirement or temporarily accepting payment of interest-only for forbearance purposes, firms should take a proportionate approach depending on the customer's circumstances and the nature and extent of the change being contemplated. For example, a term extension that takes a mortgage one or two years into a customer's expected retirement is likely to have a minimal impact on the overall sustainability of the mortgage if the customer's expected retirement is still many years in the future. Similarly, it will be relevant to take account of the relative length of the remaining mortgage term (and the effect on monthly payments when the mortgage reverts back to repayments on a capital and interest basis) when considering whether it is appropriate to agree a temporary variation to interest-only.

Implications of forbearance arrangements

47. Two trade bodies asked if firms explaining the implications of forbearance on the total amount payable could do this verbally and provide illustrative examples or whether the implications needed to be personalised and provided in writing.

Our response

48. Neither our MCOB 13 rules nor the TSG require firms to provide personalised information in writing to explain the implications of forbearance, but firms should consider what is appropriate in individual cases. Setting out this information in writing will of course help firms to demonstrate that they have treated customers fairly and given them adequate information to help them understand the implications of any proposed arrangement, as required by MCOB 13. Firms may also want to consider what may be needed to inform customer understanding and support good consumer outcomes aligned with the incoming Consumer Duty.

Credit file reporting

49. Many respondents commented on credit file reporting. Two consumer representatives suggested we should issue more prescriptive, clearer and stronger requirements on how lenders should report forbearance arrangements to Credit Reference Agencies (CRAs). One trade body suggested the guidance should confirm that forbearance will be reported as normal on a borrower's credit file, and another suggested the guidance should remind firms that arrangements for borrowers not in payment shortfall may not need to be reported to CRAs. One consumer representative

suggested that firms should be clear when support would not have an impact on a customer's credit file.

50. Three respondents suggested improving consumer communications to ensure any potential impact on credit files did not deter borrowers from seeking the help and support they need.

51. Two consumer representatives suggested we take steps to explore whether lenders can amend the way in which they report a mutually agreed forbearance option to reduce the impact on the credit file of a borrower receiving short-term support. In contrast 5 industry representatives, including one CRA, said it was critical to maintain the integrity of credit information and supported an approach that did not seek to interfere with existing well established credit file reporting arrangements.

Our response

52. Borrowers are understandably concerned about the impact of any support on their credit file. Unlike the pandemic, the impact of the rising cost of living is likely to be longer-lasting and impact different customers at different times. It is therefore important that credit files accurately reflect the degree of financial difficulty that a borrower faces. Such information is essential to ensuring lenders have an accurate picture of a borrower's financial circumstances and supports responsible lending. Not recording evidence of credit impairment risks borrowers being able to take out further credit that they cannot afford and falling into, or deeper into, financial difficulty.

53. We agree that consumers should understand the credit file implications of any support received, including the circumstances when support would not be reported to credit files. Our guidance sets out that firms should ensure they are clear in their communications about the credit file implications of any forms of support they offer customers.

54. In view of the above we do not think that it would be appropriate to change our approach where borrowers receive support from their lender in the current circumstances. We therefore expect firms to continue to report support provided to credit files in the usual way, in line with the position previously set out in the TSG.

55. However, we are aware of the importance of this issue, both in terms of market integrity and how it impacts consumer outcomes. We are therefore continuing our wider work in this area following publication of our Credit Information Market Study Interim Report and Discussion Paper. This sets out our recent findings on the credit information sector, including those relating to the reporting of forbearance arrangements, and considers potential wider remedy proposals to improve the consistency and quality of data.

Alignment with prudential expectations that firms monitor for heightened risk of loss

56. Trade bodies and firms wanted clarity that the guidance is aligned to expectations set out in the Finalised Guidance 11/15: Forbearance and Impairment Provisions (FG 11/15) issued in 2011. One trade body wanted clarity that the guidance was not

implying that firms should consider whether future requests for contract variations (outside of forbearance) indicated a heightened risk of loss, which should be accounted for. They wanted clear guidance that firms were not expected to ask all such customers to confirm they were not in payment difficulty.

57. They said the examples provided in FG11/15 of potential impairment indicators might contradict the expectations set out in this Guidance in the section on customers not requiring forbearance. They noted that firms would find it challenging to apply the requisite good practice on recognition of impairment without performing some level of affordability assessment to establish if customers are in financial difficulty.

58. Further, one trade body sought clarity that customers seeking a contract variation without disclosing any payment difficulty would also not trigger the application of Section 8 of the TSG 'Debt help and money guidance'.

Our response

59. FG11/15 addresses good risk management principles and practices, including the prudential and conduct considerations, when providing forbearance and making provisions for impairment. Our guidance does not change the considerations flagged in FG11/15 and does not require firms to ask all customers seeking a variation of terms if they are in payment difficulty.

60. One of the aims of FG11/15 is to ensure that effective processes are in place in the identification, reporting, monitoring and loss risk assessment of forbearance. This remains relevant, particularly given the potential impact of the macro-economic environment on borrowers' ability to maintain their mortgage payments. Our new guidance does not have any impact on a firm's prudential approach and does not set any additional or new expectations that firms treat all requests for contract variations outside of forbearance arrangements as indicating a heightened risk of loss.

61. Our guidance confirms that firms can offer forbearance, in accordance with the existing requirements in MCOB 13 (and the TSG), without completing a full affordability assessment required by MCOB 11.6.2R (including as further set out in MCOB 11.6.5R). This is not intended to conflict with guidance in FG 11/15 that indicates that there are sound prudential and conduct reasons to consider what is affordable for a borrower in payment difficulty now and over the remaining term of the mortgage, taking account of the customer's individual circumstances.

62. We agree that Section 8 of the TSG is unlikely to be relevant unless a firm knows that a customer is experiencing payment difficulties, or a customer indicates that they are experiencing or reasonably expect to experience payment difficulties. However, firms should consider the wider expectations set out in our Dear CEO letter that firms support borrowers showing signs of financial difficulty or struggling with debt, by making them aware of and helping them access money guidance or free debt advice.

Capitalisation

63. One trade body, one firm and one consumer representative asked whether we would make it easier for firms to capitalise any payment shortfall resulting from borrowers needing forbearance without having to exhaust other options where the customer can demonstrate affordability and is in recovery.

Our response

64. Firms must not automatically capitalise a payment shortfall where the impact would be material and should not agree to capitalisation except where no other option is realistically available to assist the customer (MCOB 13.3.4AR(1)(d) and MCOB 13.3.4DG).

65. Our rules are intended to ensure firms accurately reflect the financial difficulties faced by their borrowers, to encourage them (where possible) to arrange to repay payment shortfalls over a shorter term to reduce the total interest payable – and to reduce the risk of a borrower capitalising arrears when another reasonable alternative is available.

66. However, we recognise that capitalisation can be appropriate where the root cause of payment difficulty is temporary and short-term (it played a larger role during the exceptional circumstances of the pandemic, for example). We will consider consulting on whether we should amend the existing guidance in MCOB 13 as part of our plan to consult on the future of the TSG which may include proposing changes to our Handbook. This will enable us to consider the factors relevant to determining whether it might be appropriate for a firm to agree to capitalise a shortfall in individual cases.

Interest rate switches

67. A number of respondents asked for clarity on the potential need for an affordability test where a lender offers a rate switch to its existing borrowers. They argued that a like for like rate switch, where there is no additional borrowing or other change to the mortgage terms, should not require a further affordability test. Industry respondents understood potential affordability checks for rate switches to be inconsistent with the policy intention communicated when the rules were introduced (see PS12/16). They were concerned that the possible need for an affordability assessment could prevent borrowers from switching from a low reversion rate to a higher fixed rate.

68. Some consumer representatives suggested that firms should be obliged to offer their existing borrowers new deals. Two suggested firms should offer new deals to borrowers in arrears. While not suggesting that borrowers should be offered new deals one lender thought the guidance should be clear that firms can consider rate switches as forbearance for borrowers in payment shortfall.

Our response

69. Firms are not obliged to offer new deals to existing borrowers, but most active lenders will do so providing a borrower is up-to-date with payments. The decision under the voluntary industry agreement to restrict access only to borrowers who are up to date with payments is not derived from our rules. To clarify this position, we have amended paragraph 2.18 of the guidance to make it clear that rate switches for borrowers in payment shortfall are not prohibited by our rules. Access to rate switches for borrowers in payment shortfall depends on firm practice. We welcome and support firms offering rates to borrowers in payment shortfall that enable them to reduce and/or fix their contractual payments.

70. The guidance explains the effect of our existing conduct rules and principles. An assessment of affordability, required by MCOB 11.6.2R, applies to all contract variations, including rate switches, unless one of the circumstances set out in MCOB 11.6.3R applies. One such circumstance is a customer switching their rate with their existing lender.

71. An affordability assessment may apply if the borrower is switching to a higher rate, for example if they want to switch from a low reversion rate to a higher fixed rate. This is consistent with our policy statement in PS 12/16 at paragraphs 3.9 to 3.11. In such cases we think it is appropriate that a firm considers the borrower's ability to pay **if** the effect of the rate switch is **material** to affordability, for example if the resulting mortgage payment will be **materially** more expensive.

72. A borrower will often be switching to take advantage of a lower rate. Therefore, as set out in the guidance, a firm can compare the proposed new rate to the rate the customer would pay if not for the change – such as any standard variable rate (SVR) that would apply once the current deal expires.

Term extensions

73. One trade body commented on the importance of allowing borrowers who are not otherwise in payment difficulty being able to access term extensions (up to retirement) without advice and without having to demonstrate affordability.

74. One consumer representative wanted us to compel all firms to offer borrowers a term extension (or interest-only variation). Another sought clarification as to why a borrower can as part of forbearance extend their mortgage into retirement without an affordability assessment but the same change outside of forbearance would be subject to an affordability assessment. Given the customer circumstances are the same they felt the application of the rules should be the same. Another wanted us to relax the requirements to enable borrowers to more easily extend their term, particularly for those who have interest-only mortgages, to help borrowers particularly in situations where the mortgage matures when only one party to the mortgage would be in retirement.

Our response

75. Our rules enable firms to agree to extend the term of the mortgage where the change is not material to affordability.

76. Our rules exist to protect customers and seek to prevent customers encountering future payment difficulties by entering into mortgages they cannot afford. Before a customer varies their mortgage in a way that is material to affordability, the lender must be able to demonstrate that the mortgage as varied is affordable, whether the variation takes the form of a term extension into retirement or something else. It is therefore important to consider whether a customer who will have to make repayments when they are retired will be able to afford those repayments in retirement. MCOB 11 makes clear that firms should take a prudent and proportionate approach to the question of affordability in retirement, in part according to the amount of time remaining on the mortgage term before the customer expects to retire. If a borrower seeking to extend their term into retirement fails their lender's affordability tests and subsequently tells the firm that in absence of the term extension they will not be able to maintain their current payments, then the firm should consider what forbearance it can offer in the same way as it might do for a borrower who has not previously sought to extend their mortgage term.

77. A firm has more flexibility when considering what forbearance might be appropriate because the customer is already in payment difficulty. It can consider a range of options that may be appropriate, having regard to what is in the customer's interests. This could include a term extension into retirement. The firm should explain the implications of any forbearance agreed. If agreeing to extend a term into retirement this should include explaining the risk that the customer cannot afford their mortgage in retirement.

Reversing a term extension without checking affordability

78. One consumer representative suggested that a borrower who has extended their loan term to make their mortgage payment affordable should be able to reverse this easily at a later date without having to demonstrate affordability. Another consumer representative suggested that term extensions into retirement agreed under forbearance should be subject to review to establish if the borrower can subsequently reduce the term so that it no longer extends into the borrower's retirement.

Our response

79. Unlike temporary payment concessions and temporary contract variations, which revert to the original terms at the end of the temporary period, the extension of a mortgage term is a more permanent action. A further variation to reduce a mortgage term that has previously been extended will be subject to our affordability rules if the effect of the variation is material to affordability. In other words, where reducing the term materially increases the contractual monthly payment, a firm must check that this will be affordable to the borrower, including in future if rates rise (unless the mortgage is fixed for a period of 5 years or more).

80. Term extensions may be appropriate for borrowers who are finding their payments unaffordable in the near term. This may include the extension of the term into retirement. A firm will need to give the borrower adequate information to understand the implications of the variation.

81. Given this need for a term extension in the first place there is a risk these borrowers will find that reversing to the original term in future may not be affordable as the resulting payment, for any given interest rate, will be higher than the amount they could not afford before they extended the term. Given this, we believe it is appropriate that a borrower seeking to reduce their mortgage term demonstrates the ability to make these higher payments to reduce the risk of them having payment difficulties in future.

82. Most mortgage contracts allow borrowers to make significant overpayments without incurring an early repayment charge. This provides borrowers with an alternative option that effectively reduces the mortgage term, while maintaining the flexibility of a lower contractual payment.

Temporary variations to interest-only

83. Trade bodies and firms said that customer expectations had been raised by media suggestions that customers can temporarily switch to interest-only without having to evidence a credible strategy to repay the capital. They raised concerns that the longer-term consequences may outweigh the short-term benefits with customers facing even higher payments in future. They also noted that while firms were likely to offer the option to defer payments of capital under forbearance, they were less likely to offer temporary interest-only contract variations.

84. One response challenged our interpretation of the application of a particular rule. MCOB 11.6.43R indicates that firms may, when dealing with a customer who is in or at risk of payment shortfall, where appropriate, vary a contract to accept payment on an interest-only basis for a temporary period without evidence of a clearly understood and credible repayment strategy (as well as agree an interest-only concession from existing contract terms). Another suggested the guidance recognise the difficulty in determining with confidence that a customer will be able to resume full capital and interest repayments in a difficult economic environment.

85. One firm saw difficulty in being able to differentiate between a customer in payment difficulty from a customer that is eligible for interest-only switches outside of forbearance supported by a credible repayment strategy. Another asked that the guidance more clearly state whether our rules allowed firms to offer temporary variations to interest-only for customers wanting to reduce their mortgage payments but not requiring forbearance (as well as permanent variations to interest-only where the borrower has a credible and well understood repayment strategy). And one asked whether, where a temporary interest-only variation was agreed, a firm needs to assess affordability of the capital and interest payments over the remaining term.

86. Two consumer representatives said that the FCA should respond to the recent sharp rise in interest rates and the rising cost of living as if this were an emergency. They suggested we allow firms to agree temporary switches to interest-only of up to two years with no affordability assessment. They argued this would prevent arrears building in this period and prevent repossessions. A third consumer organisation was

concerned about the risks of temporary interest-only variations and term extensions into retirement (including where they are carried out under forbearance). They noted that consumers are typically much more confident of their ability to make additional payments in future, or may plan to sell their house, but experience shows that they may be being over optimistic about their scope to do this in practice.

Our response

87. We do not agree that the current situation is similar to that faced at the beginning of the coronavirus pandemic where customers who were affected were impacted suddenly and at the same time. The effect of the rising cost of living and increased mortgage costs is more likely to impact different customers at different times and in different ways such that a tailored approach that takes account of individual circumstances is appropriate.

88. Mandating that firms should allow all borrowers to defer capital payments for 2 years without considering their likely ability to meet future payments brings significant risks. It would mean that customers who can afford to pay more than interest-only would pay more interest than they need to – and those who do not have scope to increase their mortgage repayment term will likely face significantly higher and potentially unaffordable payments in 2 years' time. Interest-only concessions risk only delaying and increasing any payment shock, and should only be used when it is appropriate to a customer's particular circumstances.

89. While some borrowers may have scope to extend their mortgage term and demonstrate increased affordability in future, customers have different needs and circumstances and would benefit from support that is tailored to their circumstances to help them manage the transition to making higher payments.

90. Therefore, our expectations focus on firms considering forbearance that takes account of individual circumstances. All firms need to do this. This guidance does not oblige firms to agree to contract variations but explains how firms can support borrowers in, or at risk of, payment difficulty and confirms the flexibility firms have under our rules to support borrowers in different ways.

91. We consider that our rules permit firms to offer temporary interest-only concessions for customers requiring forbearance, whether or not this involves a contractual variation. The guidance also confirms our rules permit firms to offer borrowers temporary variations to interest-only outside of forbearance where they choose to do so, provided they have evidence that the customer will have in place a clearly understood and credible repayment strategy. This strategy can include payments reverting to a capital and interest repayment basis. Consideration of the credibility of the customer's strategy to make future, typically higher, payments will form part of the wider affordability assessment required by MCOB 11.6.2R undertaken before agreeing the temporary variation.

92. Where this option is not available, we expect a firm to consider forbearance options if they are aware that a borrower is in payment difficulty either because the borrower has told them this or the firm has identified this.

Combining temporary interest-only with a term extension

93. Two respondents sought clarification that a firm could consider a combination of a temporary switch to interest-only and an extension of term which, if the period of temporary switch and extension of term were aligned (and all other things were equal), would mean the borrower would face payments after the temporary interest-only period, that were no higher than the payments faced before the variation was agreed. So, for instance, a borrower who requested a 2-year temporary switch to interest-only combined with a 2-year extension of term would have 2-years 'respite' in the form of reduced payments before needing to make payments at the required level.

Our response

94. Our rules permit firms who want to do this to combine variations of contract. In this case they will need to consider the rules and guidance relating both to temporary switches to interest-only and to term extensions, as well as the impact of any combination. For example, they will need to consider if the variation is likely to be material to affordability when offered outside forbearance (for example if the term extends into the borrower's retirement).

95. In the example provided the impact is likely to be a significant increase in total interest paid over the life of the mortgage. Firms should give customers relevant and timely information to enable them to understand the implications of any variation of terms.

96. A borrower may want to consider what other options the firm offers, for example a simple term extension on its own that might be affordable and have less impact on the total amount paid over the life of the mortgage.

The role of advice

97. One firm thought there was an expectation that any borrower seeking to extend their mortgage term into retirement would need to obtain advice. They were concerned that the absence of an advice requirement for a borrower extending their term up to retirement could lead to poor outcomes incompatible with our expectations under the Consumer Duty.

Our response

98. Our rules do not require that a borrower seeking to extend their mortgage term receives advice, whether or not the new term extends into retirement. In both cases a firm should consider whether the variation of the contract is material to affordability and if so to assess whether the borrower can afford the mortgage now and in future (for example, in their retirement).

99. Firms need to ensure they are acting fairly and in accordance with a customer's best interests (Principle 6, MCOB 2.5A). Enabling a customer to enter into or vary a mortgage without advice is not incompatible with this or the Consumer Duty.

However, firms will still need to ensure borrowers have the necessary information to make an informed decision about their options and their implications, including by explaining the implications of forbearance agreed in accordance with paragraphs 2.15-2.16 of the Guidance as well as disclosing the implications of a contract variation in accordance with the requirements in MCOB 7 (see paragraph 2.25).

Structure and status of the Guidance

100. Many respondents, both from industry and consumer representatives felt it was confusing for firms, consumers, and their advisers, to have to refer to multiple sources of guidance including this proposed guidance, the Handbook, the Dear CEO letter and the TSG. Suggestions included adding this to the FCA's cost of living hub, updating the TSG to more clearly set out its relevance to the rising cost of living - and consolidating the different sources of Rules and guidance in the Handbook.

Our response

101. This guidance clarifies the effect of our existing rules and principles and is not intended to set new expectations or requirements of firms. Our expectations of firms are necessarily set out in our Handbook, in other non-Handbook guidance, and in communications to firms such as our June 2022 Dear CEO letter. We plan to consult on the future of the TSG shortly, and that may include proposing changes to our Handbook.

Application of the guidance to Buy-to-let

102. One trade body and one firm asked if the guidance applied to unregulated buy-to-let mortgages.

Our response

103. Our rules in MCOB only apply to regulated mortgages. Where an authorised person carries on activity in relation to an unregulated agreement to provide credit which is secured on land, its conduct in relation to compliance with our Principles, including the fair treatment of customers, could be relevant to our assessment of whether it is satisfying the Threshold Conditions.

Out of scope of this guidance

104. Three respondents suggested further support was needed for borrowers in closed books and asked us to compel firms with closed books to offer particular products or contract variations to their borrowers.

105. Several respondents commented on wider cost of living or mortgage market issues. This included suggestions relating to consumer communication strategies, the boundaries in our Perimeter Guidance (PERG) which are relevant to the provision of and signposting to money guidance and debt advice, and suggestions that lenders do

more to reach out to later life interest-only customers near maturity. Some firms and trade bodies also asked about the prudential treatment of some options.

Our response

106. We welcome these additional views and insights but they are beyond the intended scope of this guidance – which is a clarification of existing rules and expectations which apply to all regulated firms, including mortgage administrators.

107. We published data in our Mortgage Prisoner Review so Government and industry can determine if there are any further practical and proportionate solutions that can be found for borrowers in closed books who are unable to switch.

     We will consider the views provided where relevant to our further work, for example, in our review of the future of the Tailored Support Guidance.

Summary of changes made to the final guidance

108. This section summarises 3 minor changes made to the draft guidance. We have:

a. included the sentence "*Not all firms will be able to offer contract variations*" in both the section "Customers not requiring forbearance – but wanting to reduce their monthly payments (contract variations)" as well as the sub-section "Providing forbearance". This is to clarify that it is the case whether or not the variation is for forbearance purposes.

b. amended the sentence in the sub-section "Contract variations for the purposes of forbearance" from:

   A variation is only likely to be considered appropriate and temporary if, after the temporary period is over, the customer is obliged to make payments of interest and capital which are designed to repay the mortgage in full over the remaining term.

   to:

   A variation is unlikely to be considered appropriate and temporary if, after the temporary period is over, the customer is not obliged to make payments of interest and capital which are designed to repay the mortgage in full over the remaining term.

   This change is to more clearly set out our view of when a switch to interest-only can be considered temporary and to avoid suggesting that the repayment basis is the only relevant question when considering whether a switch to interest-only would be appropriate.

c. amended the reference to rate switches to make it clearer that any decision by a firm to restrict access to rate switches only to borrowers who are up to date with payments is not derived from our rules. Rather it reflects the industry voluntary switching agreement:

   ~~Many f~~Firms may offer borrowers ~~who are up to date with payments~~ the ability to switch their interest rate.

List of non-confidential respondents

- All Party Parliamentary Group on Mortgage Prisoners
- Association of Mortgage Intermediaries
- Association of Short Term Lenders Ltd
- Barclays Bank Plc
- Building Societies Association
- Christians Against Poverty
- Citizens Advice Bureau
- Citizens Advice Scotland
- Consumer Council Northern Ireland
- Debt Camel
- Finance & Leasing Association
- Financial Services Consumer Panel
- Institute of Money Advisers
- Jackson Cohen Associates
- Lloyds Banking Group
- Macmillan Cancer Support
- Money & Pensions Service
- Money Advice Trust
- Money Saving Expert
- Mortgage Prisoner Group
- Perenna
- The Money Charity
- The Mortgage & Insurance Shop
- UK Finance
- Which?