Title: The Implementation of the EU Mortgage Credit Directive	Impact Assessment (IA)
IA No:	**Date: 01/12/2014**
Lead department or agency: HM Treasury	**Stage:** Final
	Source of intervention: EU
Other departments or agencies:	**Type of measure:** Secondary legislation
	Contact for enquiries: 020 7270 5000 , mcdconsultation@hmtreasury.gsi.gov.uk

Summary: Intervention and Options

RPC Opinion: GREEN

Cost of Preferred (or more likely) Option				
Total Net Present Value	**Business Net Present Value**	**Net cost to business per year** (EANCB on 2009 prices)	**In scope of One-In, One-Out?**	**Measure qualifies as**
£-17.95m	£-17.95m	£1.5m	No	NA

What is the problem under consideration? Why is government intervention necessary?

The UK is required to implement the EU Mortgage Credit Directive (MCD) requirements by 21 March 2016, in order for the UK to meet its treaty obligations and avoid the risk of facing legal proceedings as a result of infraction. The MCD sets common regulatory standards that Member States are required to meet in order to protect consumers purchasing mortgage loans.

The UK Government needs to make some changes to its existing regime for mortgage regulation in order to meet the requirements set out in the MCD.

What are the policy objectives and the intended effects?

The policy objective in our implementation approach is to achieve compliance with the MCD while minimising the impact on UK industry in terms of their costs and competitiveness. The UK Government has not seen evidence that the MCD offers many benefits to consumers beyond that which is already provided by the high level of protection offered by the existing Financial Conduct Authority (FCA) regime for mortgages.

What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)

The Government has considered two options.

Option 1 - Remove the existing framework for mortgage regulation under the FCA and copy out the MCD's requirements into UK legislation

Option 2 - Seek to maintain the existing regulatory framework, minimising any adjustments required to meet the MCD.

Option 2 is the preferred option. While option 1 would be better aligned with the Government's copy-out principles it would also remove valuable consumer protections, place significant costs on industry and replace a familiar and robust regulatory system, designed to meet the requirements of the UK market, with a completely new framework that is not well adapted to the UK. Option 2 has the benefit of working alongside what is already in place, making minimal changes to achieve compliance only where necessary.

Will the policy be reviewed? It will be reviewed. **If applicable, set review date:** 09/2018

Does implementation go beyond minimum EU requirements?			Yes		
Are any of these organisations in scope? If Micros not exempted set out reason in Evidence Base.	**Micro** Yes	**< 20** Yes	**Small** Yes	**Medium** Yes	**Large** Yes
What is the CO_2 equivalent change in greenhouse gas emissions? (Million tonnes CO_2 equivalent)			**Traded:** n/a	**Non-traded:** n/a	

I have read the Impact Assessment and I am satisfied that (a) it represents a fair and reasonable view of the expected costs, benefits and impact of the policy, and (b) that the benefits justify the costs.

Signed by the responsible Minister: Date: 15 January 2015

Summary: Analysis & Evidence

Policy Option 1

Description:

FULL ECONOMIC ASSESSMENT

Price Base	PV Base	Time Period	Net Benefit (Present Value (PV)) (£m)		
2014	2016	10	**Low:** £-627.26m	**High:** £-627.26m	**Best Estimate:** £-625.44m

COSTS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	£518.5m		£12.2m	**£623.6m**
High	£521.5m		£12.3m	**£627.3m**
Best Estimate	£520m		£12.3m	**£625.4m**

Description and scale of key monetised costs by 'main affected groups'

UK mortgage lenders and intermediaries: these firms would face both significant transition costs and ongoing costs, driven by the compliance, staff and IT changes needed under option 1. More detail is provided in the main text.

Other key non-monetised costs by 'main affected groups'

UK mortgage lenders and intermediaries: these firms may face lower profits due to the disruption caused by the proposed change. We expect this cost to be limited in practice by competitive pressures.

Mortgage consumers: most consumers of mortgages in the UK would suffer detriment from a regime that was not tailored to the UK market, while some consumers would have all protections removed. The scale of this would be expected to be small relative to the market, but the relaxation of advice standards could lead to significant detriment.

Wider society: The move of mortgage regulation from the FCA to the Government may add costs in some places and redistribute it in others. However, this cost is more than likely to be small relative to the other costs considered. Any increase in consumer detriment may also increase the costs faced by civil society groups that provide support or advocacy for consumers.

BENEFITS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	£0		£0	**£0**
High	£0		£0	**£0**
Best Estimate	£0		£0	**£0**

Description and scale of key monetised benefits by 'main affected groups'

No monetised benefits were identified.

Other key non-monetised benefits by 'main affected groups'

No non-monetised benefits were identified.

Key assumptions/sensitivities/risks | **Discount rate** | 3.5%

Many of the key monetised costs (and lack of benefits) are based on extrapolating the findings of HM Treasury's survey of lenders and intermediaries to the market level. As such, the key assumption is that the findings of this survey are broadly accurate and do not reflect a biased sample.

A number of assumptions are made in the calculation processes which are discussed in full in the detailed description of the evidence base.

BUSINESS ASSESSMENT (Option 1)

Direct impact on business (Equivalent Annual) £m:			In scope of OIOO?	Measure qualifies as
Costs: £53.4m	**Benefits:** £0	**Net:** £-53.4m	No	NA

Summary: Analysis & Evidence

Policy Option 2

Description:

FULL ECONOMIC ASSESSMENT

Price Base	PV Base	Time Period	Net Benefit (Present Value (PV)) (£m)		
2014	2016	10 years	**Low:** £-22.80m	**High:** £-13.10m	**Best Estimate:** £-17.95m

COSTS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	£2.3m		£1.3m	**£13.1m**
High	£7.1m		£1.8m	**£22.8m**
Best Estimate	£4.7m		£1.5m	**£18.0m**

Description and scale of key monetised costs by 'main affected groups'

UK mortgage lenders and intermediaries: There are two main sets of costs for lenders and intermediaries driven by this legislation. These are the cost of the complying with the new regulatory regime for buy-to-let lending to consumers and the costs associated with requiring an FCA mortgages permission to conduct second charge lending. These are both driven by the formal process of requiring FCA permission or registration for different activities, familiarisation costs and the more typical IT and compliance costs.

Other key non-monetised costs by 'main affected groups'

No other non-monetised costs.

BENEFITS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	£0m		£0m	**£0m**
High	£0m		£0m	**£0m**
Best Estimate	£0m		£0m	**£0m**

Description and scale of key monetised benefits by 'main affected groups'

No monetised benefits.

Other key non-monetised benefits by 'main affected groups'

No other non-monetised benefits.

Key assumptions/sensitivities/risks | **Discount rate(%)** | 3.5%

Many of the key monetised costs and benefits are based on extrapolating the findings of HM Treasury's survey of lenders and intermediaries to the market level. As such, the key assumption is that the findings of this survey are broadly accurate and do not reflect a biased sample.

A number of assumptions are made in the calculation processes which are discussed in full in the detailed description of the evidence base.

BUSINESS ASSESSMENT (Option 2)

Direct impact on business (Equivalent Annual) £m:			In scope of OIOO?	Measure qualifies as
Costs:£1.5m	**Benefits:** £0m	**Net:** £-1.5m	No	NA

Evidence Base

Problem under consideration

1. The Directive on Credit Agreements for Consumers Relating to Residential Immovable Property, more commonly referred to as the Mortgage Credit Directive (MCD), was published in February 2014. The UK is required to implement the MCD requirements by 21 March 2016, in order for the UK to meet its treaty obligations and avoid the risk of facing legal proceedings as a result of infraction. The UK Government needs to make changes to its existing regime for mortgage regulation in order to meet the requirements set out in the MCD.

2. The MCD sets out the minimum regulatory requirements that Member States are required to meet in order to protect consumers purchasing mortgage loans. The key areas in which the MCD places requirements on Members States aim to ensure that:

- mortgage firms to act fairly and professionally, and that their staff must have an appropriate level of knowledge and competence;

- advertising of products must be fair and not misleading, with certain standard information included where specific rates are being quoted;

- certain information is provided to the consumer ahead of a contract being concluded;

- lenders conduct an affordability test, looking at customers' income and expenditure, to determine whether they can afford the mortgage loan;

- minimum standards are followed where advice is provided to consumers;

- lenders put in place additional consumer safeguards where loans are in a foreign currency, to protect the customer against exchange rate risk;

- consumers are given a right to be able to exit a mortgage before it reaches the end of the term;

- lenders exercise reasonable forbearance to customers in payment difficulties before initiating repossession proceedings;

- it is easier for mortgage intermediaries to operate across borders; and
- consumers have access to cross-border redress.

3. The Government published a consultation document setting out its proposed approach to implementing the MCD on September 5 2014, as well as a consultation stage impact assessment and draft legislation.[1]

[1] https://www.gov.uk/government/consultations/implementation-of-the-eu-mortgage-credit-directive

Policy objective

4. As explained above, the MCD sets the minimum regulatory requirements that Member States are required to meet in order to protect consumers taking out credit agreements relating to residential property. The UK Government has seen no evidence that the MCD offers many benefits to UK consumers beyond those already provided by the high level of protection offered by the existing Financial Conduct Authority (FCA) regime for mortgages. This a view that is broadly shared by industry, consumer groups and the FCA. However, the MCD does add a number of costs to industry.

5. A further aim of the MCD is to facilitate a better internal market in mortgage lending across Europe. However, the Government does not believe that it offers much benefit in this area in practice because it does not address the primary obstacles for such a market. From a lender's perspective, these include the relative difficulty in understanding credit risk in unfamiliar markets and the complexity in enforcing loans under foreign legal systems. For consumers, the scale and nature of a mortgage commitment drives a preference for dealing with well established, or local, brands.

6. The UK has therefore been sceptical about the value of the MCD. Throughout the negotiation of the MCD, the UK focused on aligning the Directive requirements as far as possible with the existing UK regulation, with a view to minimising the impact on UK industry and consumers. This is also the objective for the Government's proposed approach to implementing the MCD.

7. In considering the implementation of the MCD the Government has considered 2 options:

- Option 1 – Remove the existing framework for mortgage regulation under the FCA and copy out the MCD's requirements into UK legislation

- Option 2 – Seek to maintain the existing regulatory framework, minimising any adjustments required to meet the MCD.

8. The Government believes option 2 best meets these policy objectives. While Option 1 would ensure that the UK avoids any 'gold-plating', evidence suggests that it would be extremely costly and disruptive in the near term and would dismantle the robust consumer protections which have been developed specifically for the UK market over the last decade.

9. The preferred option 2 achieves the Government's objectives more effectively, as it builds on the existing regulatory framework, recently strengthened by the Mortgage Market Review, and does not seek to remove existing protections. Additionally this approach seeks to minimise the impact of the changes on UK mortgage firms, as far as is possible.

The ‘do nothing’ scenario

10. In our assessment of options 1 and 2 we have taken the hypothetical ‘do nothing’ scenario to be the counterfactual. In practice it will not be possible to ‘do nothing’ as the MCD places legal obligations on the UK, and so it has not been included as an option. However, it is useful to set out the key characteristics of the ‘do nothing’ scenario, so that the impacts of options 1 and 2 can be better understood.

- First charge mortgage lending is regulated by the FCA under the Mortgages and Home Finance: Conduct of Business sourcebook (MCOB).
- Second charge lending is regulated by the FCA under the Consumer Credit sourcebook (CONC)
- Buy-to-let lending to consumers is not conduct regulated by the FCA

Sources of evidence

11. HM Treasury published a consultation stage impact assessment on 5 September 2014 that set out, at a high level, the costs and benefits that had been identified through analysis of the implications of these options as well as informal discussions with industry and the FCA. At the time this document was published HM Treasury did not have the evidence needed to provide accurate monetary estimates of a number of costs and benefits, but committed to gathering more information over the course of the consultation.

12. Over the consultation period we conducted a number of surveys of mortgage lenders and intermediaries. These surveys were designed in collaboration with industry groups including the Council of Mortgage Lenders (CML), Building Societies Association (BSA), Funding and Leasing Association (FLA), and the Association of Mortgage Intermediaries (AMI). Responses were received from lenders of all sizes (ranging from ~0.02% market share to ~29%), representing over 50% (by market share) of the first charge, second charge and buy-to-let mortgage markets. For this reason, we assume that the results of this survey can be taken as broadly representative of these markets.[2]

13. The results of the survey form the basis of the majority of evidence presented in this impact assessment. However, where possible this has been complemented by evidence provided by the CML, FCA, HM Treasury and the European Commission.

One-in, two-out

14. As this measure involves the implementation of an EU Directive, and does not add to the costs on business other than in areas where this is required by the Directive, it is out of scope for the purposes of one-in, two-out (OITO). The Government has taken advantage of all the relevant exemptions to limit any additional regulatory burdens on UK business.

[2] However, adjustments have been made where significant outliers are present, or the answers provided made it clear that the respondent had misunderstood the question. Additionally, we varied the level of the costs and benefits provided by this survey to account for the possibility of variation in the population.

Option 1

16. Option 1 would involve the UK Government copying out the MCD into legislation. The MCD would then form the legal basis of the regulatory framework for mortgage lending in the UK, which would then be supervised and enforced, most likely by the FCA. This would constitute a fundamental and abrupt change to UK to both the content of UK mortgage regulation and the regulatory framework that underpins it. It would run counter to the established approach that the Government has taken to financial regulation more generally and as such would be likely to create much uncertainty.

17. The key changes that would be required in practical terms are summarised in below in table 1.

Table 1 – Key changes required under option 1

	Currently	Under option 1
Source of mortgage regulation	FCA Mortgage Conduct of Business (MCOB) rules	HM Treasury legislation copying out the MCD.
Responsibility for the content of mortgage regulation	FCA	HM Treasury
Responsibility for the scope of mortgage regulation	HM Treasury	HM Treasury
Responsibility for the supervision and enforcement of mortgage regulation	FCA	FCA

18. The overwhelming response from respondents to the consultation agreed that this was not a desirable approach. The Government has therefore decided not to pursue this option further.

Approach to analysis of costs and benefits

19. In the Regulatory Policy Committee's (RPC) opinion on the consultation stage impact assessement published by HM Treasury in September 2014, they stated that the Department should provide further evidence regarding proportionality at the final stage to justify its assessment that a full analysis of option 1 would not be proportionate, even following the collection of further information. The RPC also requested that there should be a sufficient discussion of the likely scale of costs and benefits, even where monetising them is not considered possible. In response to this the Department has fully monetised all costs where it was possible to do so, and where it was not, every effort has been made to give indicative assessments of the potential scale of the costs and benefits. This was done on a case by case basis depending on the availability of information on different costs and benefits. However, common to all the evidence gathered were two factors that drove the level of detail in our analysis. First, the absence of either any comparable regulatory

changes in terms of scale and type in the mortgage market made it difficult for both the Department and mortgage market stakeholders to provide an accurate assessment of the costs and benefits. Second, given that industry feedback strongly echoed the view of the Government that this was not an attractive approach, we judged that we should not ask stakeholders to expend significant resources analysing the potential cost of this complex change.

20. In this option, all the changes that would impose a cost or benefit would be driven by Government legislation and as such there is no accompanying analysis of the impact of option 1 from the FCA.

Compliance with the Government's guiding principles for EU legislation

21. Option 1 would meet many of the Government's guiding principles for EU legislation by using copy-out. You could argue that the large costs associated with this option could put UK mortgage lenders at a competitive disadvantage over other EU firms. But this disadvantage would in practice be limited given our assessment that significant barriers to cross-border lending will remain following the implementation of the MCD. It is likely therefore that this option would maximise the Department's ability to demonstrate compliance with the Government's guiding principles for EU legislation.

Costs of option 1

Transitional costs:

- **UK mortgage lenders and intermediaries**

  Familiarisation, Compliance, IT and Staff costs

22. There would be significant transitional costs associated with option 1. HM Treasury's survey of lenders and intermediaries suggested that the key drivers of one-off costs would be changes to IT systems. Option 1 effectively involves undoing all the regulatory changes made since 2004 and would mean fundamental redesigning complex systems and processes, driving costs similar to or greater than those seen for other major regulatory changes.

23. We estimated the transitional costs to lenders under option 1 using data from our survey, which asked a selection of lenders and intermediaries to estimate the one-off costs to their firm under option 1[3]. As described above, it was clear from the responses that lenders had some difficulty estimating this with precision. Nevertheless, all lenders provided estimates, which came to a total of £247m.[4] This cost represented the cost to the 47.8%[5] of the market the lenders surveyed represented. As such, we then scaled this up to the level of the market giving a total cost to lenders (across all mortgage business) of £517m.

24. We then used a similar process to calculate the cost of option 1 to intermediaries using the survey responses we received. As before, we calculated the sum of the cost estimates received by the intermediaries, coming to a total of £1.1m. However, scaling this to the market level was complicated by the fact that the survey to intermediaries did not include details of individual respondents' market shares. The survey for intermediaries asked those completing it to select from a series of options what range their market share fell within (for example 2%-10%). Using these answers we have been able to construct estimates of the maximum and minimum market shares our sample represented. These were 26% and 74% (giving a best estimate of 50%). These estimates were then used to create a high, low and best (mean) estimate of the cost of option 1 to intermediaries, giving figures of £4.5m, £1.6m and £3m respectively. This is summarised in annex a – table 6.

25. The significant difference in the magnitude of these costs between lenders and intermediaries can be explained by the less extensive requirements for intermediaries set out in the MCD, largely explained by the fact that intermediaries are a far more significant feature of the UK market (where typically around 50% of mortgages completed are on an intermediated basis) than other European markets. In addition this discrepancy is consistent with other regulatory changes, where the costs for intermediaries tends to be smaller, perhaps driven by the greater complexity of lender IT and compliance systems.

Disruption to the market from an abrupt overhaul of the regulatory framework

26. A further driver of transitional costs raised by some of those surveyed was as a result of the disruption to the market that may arise from firms having to implement such a significant change over such a short time period. A common theme from firms responding to the consultation document was around the challenges of implementing the required changes to the necessary timetable, even for the Government's preferred option 2. The changes implied by option 1 are far more extensive and it is possible that lenders would at least need to reduce the amount of new business they took on following March 2016, with some lenders indicating that they would expect they would have to pull out of the market altogether. This could result in a loss of profit for lenders and intermediaries over the short term, as well as potential rises in the cost of mortgages resulting from the reduction in their supply.

27. We have not been able to quantify this cost because of a lack of data on which to base any assumption of how large this contraction would be and over what period it would be sustained.[6] Furthermore, as noted above there would be potential implications for the cost of mortgages which would have required complex analysis to estimate with any degree of precision. As such any estimate would have been spurious. Our overall assessment is that competitive pressures would limit the degree to which firms would reduce then level of business they took on or increase their mortgage prices. Moreover, it is likely that the impact of such disruption would be to displace activity over time, rather than stop that activity happening at all. For that reason we think the impact would be small in the context of the wider costs identified under this option.

- **Consumers**

28. We have not identified any significant transitional costs to consumers as a result of option 1.

- **Wider society (including the public sector, individuals and civil society)**

29. Pursuing option 1 would require the Government to take over the responsibility of designing mortgage regulation from the FCA. There would be some transitional costs associated with managing this move. However, given that there have been no detailed plans set out on how such a transition would be managed it would be difficult to provide a full monetary cost. Furthermore, the scale of this change is likely to be extremely small

---

[3] Throughout this Impact Assessment where we refer to answers firms provided us with in respect to the costs they faced the questions were presented in a similar format. They asked lenders and intermediaries to consider all costs (including IT, staff training, compliance, familiarisation costs and others) that may arise as a result of HM Treasury's proposed course of action under that option. It was made clear what we were referring to and what should not be considered. Firms were then asked to rank these costs in order of their significance in driving any costs. These results are referred to explicitly in a number of places, but are also used more in a more nuanced manner throughout in order to inform the analysis presented in this impact assessment.

[4] Throughout this impact assessment all prices discussed are in terms of 2014 prices.

[5] This market share was calculated on the basis of outstanding residential mortgage balances at the end of Q2 2014 using CML data.

[6] Lenders were asked about possible disruptions to the market but could only provide illustrative comments due to the uncertainty involved in making any judgement on what would occur in such a case.

relative to the cost to lenders and intermediaries of this option and therefore it is unlikely to make any substantial change to the size or direction of the overall estimate of the cost of this option. As such, the Department decided it would not be proportionate to cost this change.

Ongoing costs:

- **UK mortgage lenders and intermediaries**

  Familiarisation, Compliance, IT and Staff costs

30. We set out in the consultation stage impact assessment our expectation that lenders may face lower ongoing costs due to the higher-level nature of the MCD requirements. However, this was not supported by evidence gathered from surveying lenders and intermediaries. The responses suggested that the key drivers of ongoing costs would be staff time spent on compliance and running IT systems. But these costs were not estimated to be significantly lower as a result of a copy out approach. There was a prevailing view that regulation is unlikely to change the underlying business models or consumer preferences, and as such, a consistent cost would be faced by firms. Our survey asked lenders and intermediaries to estimate the incremental cost or benefit from adopting the MCD.

31. As with the transitional costs, we added up the incremental costs provided by the survey results from lenders and intermediaries, which gave totals of £5.8m and £31k respectively. As before these totals represented a market share of 47.1% for lenders and 50% (best estimate) for intermediaries. This gave final estimates of the annual ongoing costs to lenders and intermediaries of option 1 of £12m and £81k (summarised in table 6).

32. There may be a small reduction in costs to business in terms of FCA fees, if under this option the FCA were (as expected) no longer responsible for the development of mortgage policy. However, for reasons discussed in more detail under the 'wider society' section, we expect the net impact of this change to be broadly neutral.

- **Consumers**

  Loss to consumers from inadequate consumer protection and a non-tailored regime

33. While we would not envisage significant transitional costs for consumers under option 1, other than the extent to which the costs imposed on lenders were reflected in prices charged to them, we do think that there would be some ongoing costs to consumers in terms of less effective and appropriate protections. The copy out regime would not be tailored to the UK market, which differs in many respects to other European markets, and therefore borrowers would lose many of the protections designed to address situations that arise in the UK but may not arise in other markets.

34. For example, the significant share of intermediary sales (more than 50% of mortgage sales) and the thousands of different products available make advice a key feature of the UK market. Existing FCA regulations set out a requirement for regulated advice to be provided in all interactive sales, and has detailed requirements about how that advice should be carried out. The MCD only includes some relatively high level standards, and no requirements about the circumstances in which advice must be provided.

35. Another area where UK borrowers would likely lose regulatory protections is around arrears and possession. This area is dealt with only briefly in the MCD, and so a copy out approach under option 1 would mean that many of the detailed protections provided by the existing regime, for example the requirement of lenders to consider a variety of forbearance options for those in payment difficulties, would be lost.

36. In our consultation satge impact assessment we also indentified equity release as an area where regulation would be removed were we to take a copy out approach, highlighting this an important area of consumer protection that the UK would not want to lose. However, we have concluded that this is not the right assumption to make in a copy out scenario. The MCD does not provide an exemption for equity release; rather it is simply out of scope. For that reason, we think that leaving the existing UK regulation of equity release intact would be consistent with a copy out approach, and so have not included its removal in the costs to the consumer of such an approach.

37. There is a question of whether firms might choose to continue many of these practices without a formal regulatory requirement, so that in practice borrowers continued to benefit from these firm behaviours. However, there are severe limitations to relying on a self-regulatory approach. The FSA was given the responsibility to regulate the residential mortgage market in 2004 in response to four key areas of detriment – poor information, certain product features, regulatory gaps and the treatment of arrears – which were not being adressed through a self-regulatory regime. A regime of self-regulation would therefore be highly unlikely to provide the same level of consumer benefits.

38. An accurate estimate of the cost to consumers from option 1 would require an article by article analysis of the differences between the existing FCA rules and the MCD, as well as an assessment of how far firms would continue these practices outside of a regulatory framework. This is significant piece of work, and we have judged it to be disproportionate given that feedback has not indicated that there is any meaningful support for option 1.

39. As such, we instead conducted a high level assessment of whether any of the major differences outlined in the paragraphs above would be likely to deliver costs to consumers that would be significant in the context of the overall costs identified so far. Through this analysis we made an estimate of the cost of removing the FCA requirements on advice, using information from a previous FCA cost benefit analysis. The total cost to consumers of the loss of these protections is estimated to be £47.5m, including both transitional and ongoing costs.[7] These costs are not included in the final cost of this option, but are included as a signifier of the approximate scale of this impact relative to the overall cost of the option as presented elsewhere.

Loss to consumers from adverse impacts on the price, choice, quantity of quality of mortgage products

40. A further cost we considered to consumers was that arising from changes to the prices and products offered by lenders and intermediaries. In our survey of lenders and intermediaries, we asked them to consider whether there would be any impact on the prices they charged, as well as the number of products they offered. Both lenders and intermediaries unanimously responded that this was unlikely to change the range of products they offered. However, some lenders (representing approximately 0.97% of the market) suggested they might have to increase the interest rates they charged. These lenders were unable to offer any estimate of by how much they would be forced to raise their rates, making it difficult for us to quantify this cost. Additionally, it was not clear whether this was simply the effect of these lenders passing on the costs they incurred from the proposed regulatory changes onto consumers, in which case any estimate would risk double counting. As such, we did not attempt to monetise this cost. However, given the size of those indicating they would raise their interest rates was small relative to the market, our judgement is that there could be a small increase in the costs faced by a relatively small number of consumers.

- **Wider society (including the public sector, individuals and civil society)**

Cost to Government and taxpayer from having to take over the responsibility for mortgage regulation

41. Pursuing option 1 would require the Government to take over the responsibility of mortgage regulation policy from the FCA. The monetary cost of this would be equivalent to the salaries of the required officials, and other resources needed to fulfil this responsibility effectively. Our best assessment is that this cost would be broadly similar to the cost when mortgage regulation fell under the FCA, therefore leading to a neutral impact overall. However, it would constitute a transfer of the burden of this cost from businesses (who pay FCA fees) to tax payers.

[7] The FSA were not required at the time to provide estimates of the benefits to the changes to their rules. However, they do provide estimates for the costs imposed by rule changes. For the changes to the FCA's distribution and disclosure rules (the main changes to improve intermediary standards), they estimated a £22m - £33m one off cost and £2m ongoing cost to firms. Assuming that the benefits of this change outstrip the costs over a ten year period (the usual time period of analysis for Governmental impact assessments) we arrive at an indicative figure of £47.5m lost from the removal of these benefits.

Cost to civil society groups with a mortgage market interest

42. An additional cost may arise for groups who provide support to borrowers who face detriment of some kind. We expect option 1 to lead to some consumer detriment (detailed above), this will mean an increase in demand for the support of groups such as the Money Advice Service, Citizens Advice and others.

Benefits of option 1

Transitional benefits:

43. The Department was unable to identify any significant transitional benefits from this option.

Ongoing benefits:

- **Mortgage lenders and intermediaries**

44. Responses to our consultation and surveys did not identify benefits to mortgage lenders and intermediaries from option 1. It was considered whether this was at odds with the fact that firms would not have to comply with such stringent regulations in a number of areas (intermediary standards, for example), hence potentially reducing costs. Our interpretation is that firms considered this in their estimate of the overall cost to their firm from this option and have therefore netted all benefits out when providing a final figure. This is on the basis that we would expect there to be benefits in some areas, but firms were very clear that this would not be of benefit for them.

- **Consumers**

Benefit to consumers from additional consumer protections

45. A consumer benefit we considered in our consultation stage impact assessment was that from the introduction of some regulatory protections for markets previously unregulated in the UK. For example, the MCD requires some small extensions to the scope of FCA regulation, as set out in chapter 4 of the consultation document. However, our assumption in the consultation, which has been supported by responses, is that these are largely technical changes and do not bring any significant market activity within the scope of FCA regulation.

46. There is a more meaningful extension of regulation in the area of consumer buy-to-let. The Government set out its proposed approach to introducing regulation to the buy-to-let market in chapter 3 of the consultation document published in September 2014 and the impact of these proposals are considered in more detail later in this impact assessment, under the analysis of option 2. Were option 1 to be pursued, the government would be very likely to follow the same approach on meeting our obligations with regard to buy-to-let lending as is being pursued under option 2. Therefore, the judgement reached as part of the analysis of option 2, that the new consumer buy-to-let regime will have a negligible benefit to consumers in terms of reducing detriment, holds equally for option 1.

- **Wider society (including the public sector, individuals and civil society)**

47. We have not identified any ongoing benefits to wider society that may occur as a result of the Government pursuing option 1.

Small and Micro Business Assessment (SaMBA)

48. Our analysis has suggested that small businesses[8] would be disproportionately affected by the regulatory changes made under option 1. Not only did the responses received from these firms suggest a higher cost relative to their size, but these firms indicated they would be less able to absorb this cost and would therefore be likely to raise the prices they charged (interest rates or brokerage fees). We have estimated that the cost to lenders and intermediaries with less than 1% market share would be £34m in transitional costs £7.1m in ongoing costs.

49. Given that the government does not believe that option 1 would be effective in meeting its objectives, the department does not think it is proportionate to consider the full range of options usually under consideration for mitigating any impact on Small and Micro businesses in detail.

Wider impacts

50. HM Treasury has not identified any wider impacts resulting from this proposal, including on our responsibilities under the Equalities Act 2010.

[8] AMI distributed our survey to a wide variety of mortgage intermediaries. However, we received no responses from intermediaries that would fall within the definition of a 'micro business'. As such, our SaMBA is based on the responses we received from small firms.

Option 2

51. Option 2 is the Government's preferred option. It involves the Government making a number of adjustments to the existing regulatory framework, so that the UK is able to put the appropriate rules in place to meet the requirements of the MCD. Many of these adustments are to the scope of FCA regulation so that they have the necessary powers to implement the changes required by the MCD. As such many of the changes required under this option will be implemented via changes to FCA rules, and so this impact assessment is best read in conjunction with the cost benefit analysis the FCA has recently published as part of its consultation paper CP 14/20 *Implementating the Mortgage Credit Directive and the new regime for second charge mortgages.*[9]

52. The following sections describe the areas where adjustments will be required and provides a high level summary of the key changes being proposed. More detail can be found in HM Treasury's consultation paper, the summary of responses and the accompanying legislation.

Second charge mortgage lending

53. Second charge mortgages are loans secured on property that is already acting as security for a first-charge mortgage. The terms first and second charge refer to the priority of securities held by the lenders. A second charge is subordinate to a first charge: in the event of default and the sale of a property a first-charge mortgage lender will recoup its money first and the second-charge mortgage lender's interests in the property are only activated after all liabilities to the first-charge mortgage lender have been settled. The term second charge mortgage is used here to refer to second and subsequent charge loans. Typical uses for second charge mortgages include debt consolidation and home improvements.

54. The second charge mortgage market grew rapidly in the decade prior to 2007, representing around 2% of the total mortgage market in that year. In 2009 it had dropped to around 0.25% of gross mortgage lending, or around 18,000 new second charge mortgages. This reduction was caused by a significant contraction in supply as second charge lenders struggled to secure funding in the wholesale markets and a reduction in homeowners' equity dampening demand. The market has grown since, with an increase of 14% in the value of new business in 2012 and an increase in the number of new contracts of 2%.

55. The scope of FCA mortgage regulation is currently limited to first charge mortgage lending while second charge mortgage lending is regulated as part of the consumer credit regime. This has been the case since 2004, when the current regulatory framework for mortgage lending was introduced. At that time the decision was made to keep second charge lending regulated by the Office of Fair Trading (OFT) alongside

[9] http://www.fca.org.uk/static/documents/consultation-papers/cp14-20.pdf
http://www.fca.org.uk/your-fca/documents/consultation-papers/cba-second-charge-lending

unsecured consumer credit. This remained the situation until April 2014 when responsibility for regulation of consumer credit transferred to the FCA. Since April, second charge lenders and intermediaries have been operating within the FCA's interim consumer credit regime.

56. The MCD applies to all loans secured against residential property and so its provisions apply equally to first and second charge mortgages. As such, the Government will move the regulation of both first and second charge mortgages within the same MCD compliant regime as of March 2016. It is plausible that second charge lending could be made MCD compliant while remaining under the consumer credit regime, with the appropriate FCA rule changes. Nevertheless, given that the FCA would incur the same additional costs in either scenario, and it would ultimately seek to recoup these from business, the difference between the two approaches is negligible. As such, these two options should be regarded as different but equivalent ways in which the UK can meet the minimum standards required by the MCD. The Government has opted for the former on the basis that it is additionally a long-standing policy goal (and request of industry) that all secured lending can fall within one regime.

57. There are approximately 300,000 existing second charge mortgage accounts in the UK. The number of second charge mortgage holders is unclear, as borrowers may have multiple loans secured on a property. Recent analysis of the market published by the FCA as part of their cost-benefit analysis suggests that there are currently about 25 lenders active in the second charge market. But it should be noted that second charge mortgage lending is a relatively small market compared to the overall mortgage market – by value second charge lending represents less than 1% of the total UK mortgage market at £0.45 billion.

58. The second charge mortgage market is characterised by a high level of intermediary activity. However, it is difficult to build an accurate picture of the numbers of intermediaries active in the second charge market. FCA data from their consumer credit interim permissions exercise has shown that there are 4500 intermediary firms that have registered for second charge broking. However, it is likely this number is a significant overestimate of those active in the market, and who we would expect to seek a permission under a new regime. This is because the cost to firms of registering for an interim permission for second charge broking alongside other consumer credit activities was negligible. Recent data collected by the FCA has confirmed this. It suggests that a more reasonable estimate of the number likely to apply for a new mortgages permission is more likely to be 200-400 intermediaries. As with first charge lending, second charge mortgage intermediaries are involved only with new loans, not the ongoing administration of loans.

Buy-to-let mortgage lending

59. Buy-to-let lending accounts for a significant part of the UK mortgage market. In 2013, 151,000 buy-to-let mortgages were taken out for house purchase or remortgaging in the UK, making up 12% of total mortgage lending for these purposes. This number is significantly higher than the trough in buy-to-let lending that the UK experienced immediately after the financial crisis, but is still below the peak of buy-to-let lending in 2007 where 339,000 such mortgages were taken out representing 15% of the market at that time.

60. Most buy-to-let mortgage lending is currently outside of the scope of FCA regulation. When mortgage regulation was introduced in October 2004, the Government drew a distinction between owner-occupiers who face losing their home if things go wrong and buy-to-let landlords, who tend to be conducting a business activity and do not require the same protection.

61. The scope of the MCD is wider than existing UK regulation and encompasses all mortgage lending to consumers. However, the Directive does recognise that buy-to-let lending is not the same as lending to individuals who are buying their own home, and provides Member States with the option to exempt buy-to-let from the detailed requirements of the Directive, and instead put in place an alternative appropriate framework for the regulation of these mortgages.

62. The Government has set out its intention to use the 'appropriate framework' exemption to put in place the minimum requirements to meet the UK's legal obligations in its recent consultation document "Implementation of the EU Mortgage Credit Directive". The Government proposed that it introduce a framework in legislation setting out new conduct regulation standards for buy-to-let lending to consumers, with the FCA being given the appropriate powers for supervision and enforcement. Because this involves the introduction of conduct regulation to a new and distinct area of mortgage lending, the Government is taking an approach based on 'copy-out', making some adaptations so that the regulations are 'appropriate' for the buy-to-let market. As such, the content of the legislation broadly mirrors that of the Directive itself, with some adjustments where the actual MCD text did not make sense in the context of the buy-to-let market. Following the introduction of this regime, firms would be under a legal obligation to:

- register with the FCA in order to carry out this type of lending

- act fairly and professionally, taking account of the rights and interests of the consumers
- advertise products in a manner that is fair and not misleading, with certain standard information included where specific rates are being quoted;
- make certain disclosures to the consumer ahead of a contract being concluded;
- conduct an affordability test, based on the rental income from the property, to determine whether the mortgage loan is affordable;
- follow minimum standards where advice is provided to consumers;
- ensure consumers are given a right to be able to exit a mortgage before it reaches the end of the term; and
- exercise reasonable forbearance to customers in payment difficulties before initiating repossession proceedings;

63. Based on survey and consultation responses, in particular from mortgage lenders and intermediaries, the Government estimates that around 11% of their current buy-to-lending would fall within this regime. This gives a market sizing of around 18000 mortgages per year, with a value of approximately £2,339m.

Other adjustments to the scope of FCA mortgage regulation

64. There are a number of further legislative adjustments required to ensure the scope of FCA regulation is aligned with that of the MCD. These are small differences in the definition of what constitutes a 'regulated mortgage' and require the Government to make a number of changes to UK legislation so that the FCA have the necessary powers to make and enforce the rules necessary to comply with the MCD. These changes include:

- Bringing equitable mortgage lending into regulation
- Bringing secured lending on timeshare properties into regulation
- Amending the existing exemption from FCA regulation for lending by government
- Alignment of UK regulations with MCD requirements on the location of the property
- Clarification of the definition of the regulated activity of 'arranging regulated mortgage contracts'
- Limiting the application of some existing regulatory exemptions for mortgage firms

65. These changes will apply to all regulated mortgage lenders and intermediaries. Currently there are around 260 lenders and 5000 intermediaries with FCA mortgage permissions.

Approach to analysis of costs and benefits

66. The sections below look at the costs and benefits of these changes to UK mortgage lenders and intermediaries, where appropriate breaking this down to describe how different firms might be affected in different ways. It also considers the impact on consumers. As with the estimates provided for option 1, these figures have been collected from a variety of sources including our survey of the market, data collected from the FCA and CML, as well as other information received by respondents to the consultation. We have fully monetised all the costs and benefits we have identified as being significant in size given that this is the Government's preferred option.

67. This section does not consider the impact of changes to FCA rules which will be covered in their own cost benefit analyses. The rationale behind this decision is that much of the impact of this option is dependent on the way in which the FCA decides it needs to change its rules in order to meet the requirements set out by the MCD. The FCA is independent of the Government and is required by the legislation that underpins it to conduct a cost benefit analysis of any changes it makes to its rules. As such, the Government would be undermining the FCA's independence by pre-empting any changes that the FCA decides to make to meet the UK's obligations under the MCD, which are still either unannounced or subject to consultation.

68. Understanding which costs and benefits are driven by decisions made by the Government or the FCA is complex, since it often requires reading all consultation documents, impact assessments and cost benefit analyses in conjunction with one another. As such, the key changes to regulation are summarised below in table 2, as well as the rationale behind which impacts are included in this impact assessment.

Table 2 – Responsibility for Option 2 changes between HM Treasury and the FCA

Market	Change needed	Institution responsible for relevant change	Responsibility for analysing impact	Relevant publications
First charge	Changes to align UK conduct regulation of the 1st charge market with the MCD	FCA	FCA	FCA consultation paper CP 14/20.
Second charge	Moving second charge mortgage lending from the FCA regulated activity of consumer credit lending to FCA regulated activity of mortgage lending	HM Treasury	HM Treasury	HM Treasury consultation paper (Chapter 2) and this impact assessment
Second charge	Changes to the conduct regulation of the 2nd charge market to align current rules with those for first charge mortgages.	FCA	FCA	FCA consultation paper CP 14/20 and the accompanying KPMG cost benefit analysis
Buy-to-let	Ensuring the application of an appropriate framework for buy-to-let mortgage lending to consumers	HM Treasury	HM Treasury	HM Treasury consultation paper (Chapter 3) and this impact assessment. The FCA will also publish a consultation on the changes to their handbook that may be required in order for them to implement and monitor the new regime.
Further adjustments to scope of mortgage regulation to align UK regulation with the MCD	Ensuring that the FCA has the power to regulated the right loans so that the UK is compliant with the MCD.	HM Treasury	HM Treasury	HM Treasury consultation paper (Chapter 4) and this impact assessment (considered under "other changes to the scope of FCA mortgage regulation")

Compliance with the Government's guiding principles for EU legislation

69. The Department has designed the option 2 proposals in order to both comply with the Government's guiding principles for EU legislation, and minimise the impact on UK lenders and intermediaries.

70. While copy-out principles are used in our transposition of the buy-to-let requirements under this Directive, we have not taken this approach across the board since to do so would run counter to the Government's established approach to regulating financial services. The Government does not want to undermine the robust system for the conduct regulation of financial services established in the UK, with a strong independent regulator at its heart.

71. Bearing this in mind the Government's approach for implementing most of this Directive has been to make changes to ensure that the scope of the FCA's regulatory authority post March 2016 will match up to the scope of the MCD (set out in Article 3). The FCA will then make the necessary changes to the conduct regulations pertaining to these mortgages in order to ensure they meet the requirements of MCD.

72. Table 3 below is designed to set out HM Treasury's approach at a more granular level to demonstrate that there has been very little gold-plating, and where it does occur, the implementation approach has been to maintain the regulatory status quo as far as possible, rather than increase the burden of regulation and so the changes remain outside of the scope of one-in two-out. It sets out the scope of lending to which the MCD requires its rules to apply, set out in Article 3 of the Directive, and how this relates to the Government's proposals under option 2.

Table 3 – Comparison between the scope of the MCD and the scope of the UK mortgage regulation

MCD Article	Content	Interpretation	Relation to option 2 proposals
Article 3(1)(a)	Requires the Directive to apply to all credit agreements which are secured either by a mortgage or by another comparable security commonly used in a Member State on residential immovable property or secured by a right related to residential immovable property	Requires the UK to regulate 1st and 2nd charge mortgage lending, as well as secured time-share lending	Option 2 ensures that the FCA can regulate both 1st and 2nd charge mortgages within the same MCD compliant regime. It also proposes extending the scope of the FCA to include secured time-share lending
Article 3(1)(b)	Requires the Directive to apply to all credit agreements the purpose of which is to acquire or retain property rights in land or in an existing or projected building	Requires the UK to regulate secured and unsecured credit agreements that are used for buying property	No changes are being proposed since the FCA already has the power to regulate these agreements
Article 3(2)(a-f)	States the types of lending that the MCD should not apply to, including equity release lending and number of types of credit which are at favourable terms to the borrower.	Does not require the UK to apply the MCD to any of the types of lending it lists.	While the Government does not regulate the majority of these types of credit, it does regulate some including equity release, to which the FCA's rules on lifetime mortgages apply. The UK is not proposing to make any changes to the existing regulatory treatment of any of these types of lending - wherever possible we are seeking to maintain the status quo. In this way there is no additional regulatory burden arising from our approach. In addition, this does not constitute gold-plating as this section simply

			describes the scope of the MCD rather than setting out exemptions.
Article 3(3)(a-e)	States the types of lending which Member States can choose to exempt from the MCD requirements. This includes bridging loans, buy-to-let lending and lending to a restricted public.	The UK can take the choice to not ensure that these markets have MCD compliant regulations in place.	The UK is unable to take advantage of the first exemption, 3(3)(a) as it only applies where Member States have decided to apply the Consumer Credit Directive to some specific types of mortgage lending. The UK did not do this and as such is out of scope of this exemption. We have taken advantage of the exemption in article 3(3)(b) (buy-to-let). On exemptions 3(3)(c) (loans to a restricted public), 3(3)(d) (bridging loans) and 3(3)(e) (loans by credit unions) the Government has used the exemption to limit any extension or change to regulation in the areas affected. This does constitute gold-plating because the Government is not using the exemption to remove all existing regulations affecting such loans to the full extent permitted by the MCD. However, there is not a net cost to business as a result, and so it does not affect the application of one-in, two-out.

Costs of option 2

Transitional costs:

- **UK mortgage lenders and intermediaries**

First and second charge mortgage lending – cost from changes to FCA rules

73. As explained previously, this impact assessment does not consider the costs or benefits of changes to FCA rules. However, it is important to recognise that there will be a cost to lenders and intermediaries from their proposed changes. More detail on these can be found in the FCA's consultation paper, CP 14/20 *Implementating the Mortgage Credit Directive and the new regime for second charge mortgages*[10], and are summarised in annex B. The FCA estimates of key transitional costs are £6.7m for lenders and £1.7m for intermediaries.

Second charge mortgage lending – cost of gaining a mortgage permission

74. The legislative changes will mean that second charge firms (lenders and intermediaries) will need to obtain the same FCA permissions that currently apply to first charge firms. This impact assessment does not seek to quantify costs driven by the detailed rules that lenders will be required to meet under this regime, including any additional costs incurred by the FCA (which would be passed onto firms). These are quantified in the cost benefit analysis published by the FCA.

75. The FCA has undertaken analysis to establish the population of second charge lenders based on those that applied for interim authorisation as a second charge lender under the new FCA consumer credit regime. The analysis showed that 161 firms (excluding house builders) are currently involved in the second charge mortgage market, either as an active lender, an administrator of a back book or as a non-core activity. Of the 161, 69 are already authorised as first charge lenders or administrators and will not be required to extend their existing permissions. This leaves 92 who may apply for authorisation as a lender or administrator of second charge loans. Shared equity loans are also captured by the MCD which means that house builders may also seek authorisation; the latest estimate is that 177 have registered for an interim consumer credit authorisation as a second charge lender. However, consultation with house builders has suggested that few are likely to apply for a full mortgages permission at this stage.

76. In order to obtain a consumer credit or mortgage permission, firms are required to undertake an application for which a fee is incurred. Different permissions are subject to different fees, reflecting the cost to the FCA of assessing those applications (although in practice some of the costs are also covered by ongoing fees levied on all firms, because this both reduces barriers to entry and because all firms benefit from the

[10] http://www.fca.org.uk/static/documents/consultation-papers/cp14-20.pdf
http://www.fca.org.uk/your-fca/documents/consultation-papers/cba-second-charge-lending

integrity of a market with specific entry conditions). Fees also vary according to the level of complexity of the firms' activities, again to reflect the different cost to the FCA of assessing the application. There are three categories of complexity: 'straightforward', 'moderately complex' and 'complex'. The FCA have indicated that an application from a second charge intermediary will be categorised as 'straightforward' while an application from a second charge lender will be categorised as 'moderately complex'.

77. Under the Government's legislative changes, from March 2016 second charge firms will be conducting a regulated mortgage activity and so will need to apply, and pay the associated fee, to secure an FCA mortgage permission. Depending on whether they are a lender or an intermediary they will have to pay the fees either for a 'moderately complex' or 'straightforward' application respectively. The decision to bring second charge lending into the FCA mortgages regime therefore may have a cost impact for second charge firms, as the fee for the mortgage application may be different from that they would otherwise have incurred to apply for the full consumer credit regime.

78. The application set by the FCA for the new consumer credit regime varies according to the income the firm generates from their consumer credit activity, between £600 and £5000 for a straightforward application and between £800 and £10,000 for a moderately complex application. The FCA has also now set out that second charge firms are integrated into the existing mortgage regime, so will pay application fees in the same way as other mortgage firms. The costs of permissions under the two different regimes are set out below in Table 4 for clarity.

Table 4 – Cost of FCA permissions under the Consumer Credit (CC) and Mortgages regimes

Consumer Credit[11]

Category	Up to £50k	£50k-£100k	£100k-£250k	£250k-£1m	Over £1m
Straightforward	600	750	1000	1500	5000
Moderately complex	800	1000	1500	5000	10000
Complex	1000	1250	2000	7000	15000

Mortgages[12]

Category	Cost
Straightforward	1500
Moderately complex	5000
Complex	25000

[11] http://www.fca.org.uk/your-fca/documents/consultation-papers/cp13-14-supplement

[12] Subject to final FCA decisions.

79. The difference in the cost of permissions paid by firms under option 2 against the 'do nothing' counterfactual will therefore be dependent on the distribution of the income that second charge lenders and intermediaries earn related to their consumer credit permission under the existing regime. But the total cost to firms will also be dependent on whether these firms continue to undertake other consumer credit business, that is not second charge, so that they will need to continue to hold a consumer credit permission alongside their mortgages permission. If that is the case, the cost of the mortgages permission will be additional to their existing costs (albeit firms with an existing permission do pay half of the usual fees to get a permission for a different regulated activity, in a process known as a 'variation of permission'). If it is not the case, the net cost of the change to firms will be lower, as the mortgages permission will be replacing the consumer credit permission.

80. However, there are a number of areas of uncertainty that make calculating the cost of firms gaining this permission more difficult. First, neither the FCA nor industry has been able to provide an assessment of the distribution of income among second charge firms. Second, we do not know how many of the firms that have applied for an interim consumer credit permission will in fact require a mortgages permission to undertake second charge activity. And third, we do not have an estimate of how many such firms will continue to take other consumer credit activity following the transfer of second charge to the mortgages regime. We have dealt with these uncertainties by calculating a high and low case for each of these uncertain factors, i.e. varying:

- the distribution of the income firms earn from their consumer credit permission;
- the number of intermediaries that will apply for a mortgages permission (the estimate provided by the FCA is 200 to 400); and
- whether the firms will continue to hold a consumer credit permission, and therefore whether the mortgages permission should be seen as an additional cost, or netted against the cost of the consumer credit permission.

81. Table 7 (in annex a) sets out two scenarios with the combination of assumptions that would deliver the highest and lowest cost for lenders and intermediaries with consumer credit permissions. Scenario 1 delivers the lowest total cost for a consumer credit permission, £233k for lenders and £258k for intermediaries. This based on an income distribution skewed towards a lower income firms, with only 200 intermediaries having to apply for consumer credit permissions. Scenario 2 is effectively the opposite. The income distribution is skewed towards the higher income firms, while 400 intermediaries have to apply for consumer credit permissions and this results in a cost to lenders of £439k and intermediaries of £899k. These scenarios effectively represent the variety of costs that lenders and intermediaries may have had to incur under the 'do nothing' case. These can then be compared relative to the cost of mortgages permission, as set out in table 8.

82. The final range is then determined by two cases. The highest cost is where all second charge firms that need a mortgages permission will still need to hold a consumer credit permission and as such the cost to lenders will be relative to a ‘do nothing’ cost of £0. This means that it will cost lenders £460k and intermediaries £450k. However, if in reality, all lenders and intermediaries require a consumer credit permission, and this cost is at its highest (i.e. under Scenario 2 of table 7), this means that the cost should be netted off against this, resulting in a cost of £20k to lenders and a saving (benefit) of £449k for intermediaries. Taking the average of these two cases for both lenders and intermediaries’ results in a best estimate of a net cost of £240k to lenders and £500 to intermediaries. This is summarised in table 12.

Second charge mortgage lending – familiarisation and compliance costs

83. In our consultation stage impact assessment we set out the view that it is reasonable to assume that there would still be some associated costs for firms, for example, around having to familiarise themselves with a new application and complete the necessary documents to gain a permission. However, the evidence provided by our survey of lenders and intermediaries did not support this. Many respondents did point to increased costs as a result of the different FCA rules that would apply. However, on the administrative impact of requiring a mortgages permission as opposed to a consumer credit permission the majority of lenders and intermediaries suggested that there would be virtually no incremental cost given that the processes are expected to be broadly similar when compared to the counterfactual. We therefore concluded it would be most appropriate to calculate a range for these familiarisation costs, with £0 as the lower bound.

84. In order to arrive at an upper bound, we used the survey responses from the limited number of firms that had provided a cost estimate and extrapolated these results. However, as with the calculations we completed for the cost of second charge permissions to firms and lenders, this was complicated by the lack of market share data and accurate estimates of the number of intermediaries that would join the mortgages regime. As such, we used costs taken from the survey responses of a group of firms that all earned over £1m from their consumer credit permission and then scaled this down relative to the different categories. The distribution of firms income (and as such this corresponding cost) were then skewed to provide a range, as well as varying the number of intermediaries that would operate in this market (in the same manner as for consumer credit permissions). This gives two scenarios (summarised in table 9) of which scenario 2 provides the greatest cost to lenders (£1m) and intermediaries (£902k). This then becomes the upper bound for this cost and average is calculated to give a final best estimate of this cost of £451k to lenders and £531k to intermediaries. This is summarised in table 12.

Buy-to-let mortgage lending - familiarisation, compliance, IT and staff costs

85. The introduction of the Government's proposed regulatory regime for buy-to-let lending to consumers will mean that lenders and intermediaries engaged in this market will have to put in place compliance procedures, make changes to IT systems and potentially provide additional training to their staff. Information gathered using our survey suggested that these factors would be the key elements driving an expected increase in costs to lenders both during transition, and on an ongoing basis.

86. In order to estimate these costs, we have used a similar methodology as under option 1, scaling up the findings from the sample we surveyed to the level of the market. Our survey asked lenders to estimate costs by choosing one of a number of different cost ranges we provided. As with previous elements of this impact assessment, we used this to create an upper and lower bound of the total cost estimated by these firms. These total costs were then scaled up to the market level based on data showing the lender responses received represented 56.9% of the market, and the intermediary responses received constituted in between 74% and 26% of the market.[13] The total costs based on the responses received and the associated market shares are summarised in annex a – table 10. This results in a best estimate of transitional costs of £2.1m for lenders and £858k for intermediaries.

Buy-to-let mortgage lending -registration costs

87. In addition to any transitional costs dervied from the new requirements, lenders and intermediaries will face a cost in terms of registering with the FCA to undertake consumer buy-to-let business. The FCA will announce fees in due course but for the purpose of this impact assessment we have estimated the cost to lenders based on the fees summarised in annex a – table 11. These fees are based on those charged under the payment services regulations which may represent a reasonable proxy. Based on these fees and an estimated 102 lenders[14] and 4150[15] intermediaries participating, 95% of whom are assumed to already have an FCA authorisation in one form or another [16], this gives us an estimate for the total one-off fee costs of £12k to lenders and £498k to intermediaries.

- **Consumers**

88. The Department has not identified any significant transitional costs to consumers.

[13] Similarly to under option 1, this was also used to create an upper and lower bound of the estimates.

[14] The number of lenders used here is the total number of buy-to-let lenders (Source:CML). It is assumed that *all* buy-to-let lenders will take part in this regime on the basis that all lenders and intermediaries surveyed suggested that they would do so.

[15] The number of intermediaries is the total number of mortgage intermediaries since there is not a more accurate estimate of the number of buy-to-let intermediaries available.

[16] This assumption is based on HM Treasury and FCA data and is relevant since firms with another permission will have to pay the lower fee set out in annex a – table 12.

- **Wider society (including the public sector, individuals and civil society)**

89. There may be some transitional costs to civil society groups with a mortgage market interest in providing support where customers are affected by the move to the new regime. However, given that we expect the overall impact of option 2 to be both small and not particularly visible to consumers, we expect the real cost here to be negligible.

Ongoing costs:

- **UK mortgage lenders and intermediaries**

First and second charge mortgage lending – cost from changes to FCA rules

90. There will be an ongoing cost to UK mortgage lenders and intermediaries under option 2 that arises from changes to FCA rules. KPMG's cost benefit analysis, while mainly focussed on the changes to second charge, gave a best estimate of £3.1m for lenders and £1m for intermediaries. There are some additional benefits that the FCA expects to accrue as a result of the changes needed to ensure regulation of the first charge market is MCD compliant. However, no monetary estimates are provided and general analysis suggests any benefits will be minimal. All of these impacts are summarised in annex B and does not enter in to HM Treasury's overall assessment of the cost of option 2 for the purposes of this impact assessment for the reasons explained above.

Second charge mortgage lending – ongoing cost of a mortgage permission

91. UK mortgage lenders and intermediaries with an FCA mortgage permission will have to pay an ongoing (periodic) fee to the FCA to cover the costs of mortgage regulation. An accurate estimate of the incremental cost to lenders as a result of the changes to second charge was complicated by the fact that the ongoing costs for firms are determined by the amount as well as the complexity of their activities. In the case of a consumer credit permission this is determined by the firms income from consumer credit activities, whereas for a mortgage permission this is determined on an individual basis based on factors such as the number of new mortgage loans entered into per year and the size of the mortgages back book.

92. We were not able to secure sufficient detail about the volume of historic and ongoing activity of the range of firms operating in the second charge market through our consultation. This makes it very difficult to make a detailed calculation of the incremental costs of periodic FCA fees under the mortgages regime. However, our best estimate is that the incremental costs are negligible. This is based on the reasoning that FCA periodic fees are set so that, over the long term, they recoup the supervisory and enforcement costs that arise from regulating that activity. While it is not the case that these calculations are done at a highly granular level in each individual case, this is the broad principle that is used to guide the process of setting FCA fees. The changes that HMT is making to the legislation do not change the underlying nature of the activity. It is therefore not unreasonable to assume that the costs to second charge firms will be largely the same under the mortgages

regime as they would have been under the consumer credit regime, particularly over a 10 year period.

93. HM Treasury acknowledges that there is likely to be a higher degree of scrutiny over second charge mortgages from March 2016, under the mortgages regime, which is likely to have a cost impact. But these are driven by the rules the FCA decides to apply, and are rules that they could equally choose to apply under the consumer credit regime. This cost is therefore reflected in the FCA cost-benefit analysis, summarised above, and are therefore not included in this impact assessment.

Buy-to-let mortgage lending – familiarisation, compliance, IT and staff costs

94. The survey also asked firms for information on their estimate for the ongoing costs of a buy-to-let regime for consumers. These were calculated using the same method as the transitional costs, and are estimated at an annual cost of £800k for lenders and £314k for intermediaries. These calculations are summarised in annex a – table 10.

Buy-to-let mortgage lending – registration costs

95. Using the same methodology as set out previously we also then considered the ongoing costs to lenders and intermediaries due to the periodic fees that will be charged by the FCA for firms to remain on the consumer buy-to-let register. As mentioned above, these will be announced by the FCA in due course, but we have made an estimate for the purpose of this impact assessment based on the fees charged under the payment services regulations. These are annual fees of £100 for lenders and £100 for intermediaries (annex a – table 11). Based on these fees and an estimated 102 lenders[17] and 4150 intermediaries participating in the market this gives us an estimate for the total annual ongoing fees costs of £10k for lenders and £415k for intermediaries.

96. One cost we considered in addition to this was the potential cost to the FCA of having to supervise this regime. However, we have not provided a monetary estimate of this since this cost will be funded by the fees discussed above and as such this would be double counting.

Other adjustments to the scope of FCA mortgage regulation

97. In our survey of the mortgage market, we asked lenders and intermediaries to consider the impact on their firms of the proposals contained in Chapter 4 of the Government's consultation paper on the implementation of the MCD. The vast majority made it clear that they did not operate in these markets, and we did not get any clear estimates of the potential cost impact.

[17] The number of lenders used here is the total number of buy-to-let lenders (Source:CML). It is assumed that *all* buy-to-let lenders will take part in this regime on the basis that all lenders and intermediaries surveyed suggested that they would do so.

98. One or two firms suggested there could be more significant costs resulting from these changes, although they provided no estimate of this. In particular there was a misunderstanding about the implications of changes to the legislation around the location of the property. However, this has been clarified in the Government's summary of responses, which we believe will address these concerns. On this basis we estimate that there is a negligible cost to firms arising from these adjustments to the scope of FCA regulation.

- **Consumers**

Second charge mortgage lending

99. There is unlikely to be any cost to consumers from our proposed changes to the legislation so that second charge mortgage lending is regulated as a mortgage activity rather than a consumer credit activity. Any costs and benefits to consumers from changes in the second charge market will be determined by the changes to the FCA rules that apply to second charge mortgage lending, and are therefore reflected in the FCA's cost-benefit analysis.

Buy-to-let mortgage lending

100. We asked lenders and intermediaries whether they expected there to be increases in interest rates or brokerage fees as a result of the proposed changes. The clear response from firms was that this was unlikely to happen. There were two reasons for this. First, many firms suggested that competitive pressures would ensure that costs were not passed onto lenders in a fairly price-elastic market. Second, it was the judgement of most respondents that regulation was rarely a driver of changes in the price or quantity of products in this market unless the changes proposed are extremely costly. In this instance, the estimated costs are small and as such firms stated that they were more likely to bear these costs through a slight reduction in their margins.

Other adjustments to the scope of FCA mortgage regulation

101. On the basis of our survey results, consultation and HM Treasury analysis, we have not found evidence of cost to consumers from the other adjustments we are making to the scope of FCA mortgage regulation.

- **Wider society (including the public sector, individuals and civil society)**

102. Both the results of our survey and responses received from consultation confirmed there is unlikely to be any cost or benefit of option 2 to wider society.

Benefits of option 2

Transitional benefits:

- **UK mortgage lenders and intermediaries**

  Buy-to-let mortgage intermediaries

103. Following consultation the Government has decided to make a change to the regulation of broking on buy-to-let mortgage lending, so that it is removed from the scope of 'credit broking' within the consumer credit regime. The Government has arrived at the conclusion that, with the introduction of a MCD compliant regime for consumer buy-to-let, the case for retaining protections through the consumer credit regime falls away, and risks creating confusion for firms. This means buy-to-let intermediaries will no longer need to hold a consumer credit permission in order to under take buy-to-let mortgage activity.

104. Although this measure will be delivered through the same legislation as the MCD, it is not required by the Directive and as such is a deregulatory measure, within scope of one-in two-out. In order to avoid confusion within this impact assessment, by including changes that are both within and out of scope of one-in two-out, the Department has made the decision to separate these measures out into two separate impact assessments. The removal of buy-to-let intermediaries will deliver both transitional and ongoing benefits from firms that operate in this market no longer being required to pay the relevant consumer credit fees.

- **Consumers**

105. The Department has been unable to identify any significant transitional benefits to consumers from option 2.

- **Wider society (including the public sector, individuals and civil society)**

106. The Department has been unable to identify any significant transitional benefits to consumers from option 2.

Ongoing benefits:

- **UK mortgage lenders and intermediaries**

  Second charge mortgage lending

107. In our consultation stage impact assessment we posited that there may be some benefits of option 2 to second charge firms already doing first charge lending, as there could be efficiencies to be gained from operating under a single regulatory regime. However, this was not supported by the data we gathered over the consultation, which suggested that the markets were sufficiently distinct as to preclude the emergence of such synergies. We also asked whether the changes might make some first charge firms more likely to enter the second charge market. Only one firm suggested that this might be the case. As such, our

best estimate of the net benefit to second charge firms and intermediaries from option 2 is £0.

- **Consumers**

Second charge mortgage lending

108. The key benefits to consumers will be driven by the FCA rules, and quantified in their cost benefit analyses.

Buy-to-let mortgage lending

109. We analysed the possibility that greater benefits would accrue to buy-to-let mortgage customers whose mortgages will in future fall within this regime. However, we found little evidence that there will be any significant consumer benefits for several reasons.

110. First, we do not think that there is strong evidence of detriment in this market. Data from the Council of Mortgage Lenders shows that the average rate of repossessions in the buy-to-let market since the second half of 2005 has only been 0.16% compared to 0.14% in the residential market, which is subject to extensive conduct regulation. And it is the Government's judgement that where buy-to-let properties are repossessed, the detriment is not as severe as when owner-occupiers lose their property. Second, we believe that the requirements set out in HM Treasury's proposed framework are largely in line with current market practice.

111. On this basis, we do not have the evidence to support a contention that the introduction of this framework will bring about a substantial benefit to consumers, and have therefore assumed this to be negligible.

Other adjustments to the scope of FCA mortgage regulation

112. Given the small number of transactions identified by our survey as being affected by these changes, we would expect a negligible benefit to consumers as result of any additional consumer protection.

- **Wider society (including the public sector, individuals and civil society)**

113. Both the results of our survey and responses received in response to our consultation confirmed there is unlikely to be any cost or benefit of option 2 to wider society.

Small and Micro Business Assessment (SaMBA)

114. The Directive does not provide Member States with flexibility with regard to the application of the requirements to micro and small businesses. It is clear from a legal perspective that the MCD must be applied consistently regardless of the size of the firm.

This means the Government is limited in its ability to offer tailored treatment to mitigate the impact on these businesses. The Government's proposed approach seeks to minimise the impact on business where possible, which will also benefit micro and small businesses.

115. However, even given the constraints of the Directive, the Department has made an effort to ensure that all options for mitigating the impact against Small and Micro businesses are fully explored. The conclusions of this exercise are summarised in table 5.

Table 5: Analysis of small and micro business mitigation options

Option	Reason for rejection
Partial exemption	Partial exemptions are not allowed within the MCD.
Extended transition period	The MCD only provides some transitional flexibilities for some very specific firms and under some specific circumstances. It does not include this flexibility for small or micro businesses.
Temporary exemption	Temporary exemptions are not allowed within the MCD.
Varying requirements by type and/or size of business	The MCD has no provisions to allow the UK to vary its legislation by type and or size of business.
Specific information campaigns or user guides, training and dedicated support for smaller businesses	The Government's main action in this respect is to confirm its final policy approach as far in advance of the implementation date as possible, so that firms have as much time as possible to understand and implement the changes. The FCA, who will be implementing the detailed changes, have been carrying out roadshows across the country to speak to firms and make them aware of the changes.
Direct financial aid for smaller business	The Government does not believe that there is a case for direct financial aid, and does not believe this would represent good value for money, in light of the wider approach to minimise the impact on business wherever possible. Moreover, the responses to consultation have not suggested that the problem for small and micro-businesses are sufficient as to justify this kind of intervention.

116. While the specific options above were rejected, the Government has taken a number of steps to reduce the impact on small and micro businesses, including, but not limited to:

- The removal of buy-to-let broking from regulation. This is a change that will disproportionately benefit smaller and micro firms (covered in a separate IA).

- Designing the regulatory regime for buy-to-let lending to consumers such that it imposes minimal cost on business. While the Government is confident it has met the aims of the MCD in this regime, it has also used the flexibility the MCD to exempt buy-to-let lending from its detailed requirements to ensure the burden of the regime is minimised.

- Finalising the Government's policy position and legislation as far in advance of the transposition date (March 2016) as possible, and well ahead of other member states, to allow lenders and intermediaries more time to implement any costly and complex changes.

117. The Government is therefore strongly of the opinion that it has taken all steps possible to reduce the cost to business of the MCD, which has been from the outset, a key policy objective of our transposition efforts. But, this is not to say that there is not a cost to small and micro businesses from option 2. By disaggregating our earlier cost estimates we have been able to assess the impact of option 2 on lenders and intermediaries where their share of the mortgage market is less than 1%. Using the same method as previously, we calculated that the cost to lenders and intermediaries falling within this definition is £226k in one-off costs and £60k annual ongoing costs.

Wider impacts

118. HM Treasury has not identified any wider impacts resulting from this proposal, including on our responsibilities under the Equalities Act 2010.

Preferred option and implementation plan

119. The Government's preferred option is option 2 as it best meets the Government's objectives:

- to meet the UK's legal obligations – both options 1 and 2 achieve this.

- to minimise the disruption to UK mortgage lenders and intermediaries – option 2 meets this objective more effectively than option 1 as it supplements the existing regulatory framework, making adjustments to a regime developed for the UK market over many years, rather than replacing it with a new and unfamiliar approach. It also seeks to minimise the changes that firms need to make wherever possible.

- to ensure the UK mortgage regime continues to provide a high level of consumer protection – option 2 meets this objective more effectively than option 1 as it ensures that the existing regime to protect mortgage consumers remains intact, and does not remove a number of valuable protections.

120. The Government has now published the final legislation, which will now be subject to scrutiny by both Houses of Parliament. There is still further work to be undertaken by the FCA to consult on and finalise its rules implementing the MCD. As previously explained, our aim is to finalise all these details as early as possible in order to give firms clarity as early as possible so that they have sufficient time to implement these rules ahead of the deadline set out by the Commission of 21 March 2016.

Annex A – Summary sheet

Table 6 – Option 1 – Summary of costs to lenders and intermediaries

Type of cost	Total cost (Survey responses)	Market share of respondents	Implied total cost to the market
Transitional cost – lenders	£247,200,000	47.80%	£516,902,362
Transitional cost–intermediaries	£1,190,000	50% (Best estimate)	£3,092,516
Ongoing cost – lenders	£5,820,000	47.80%	£12,169,789
Ongoing cost – intermediaries	£31,250	50% (Best estimate)	£81,211

Table 7 – Option 2 – Summary of the transitional cost of consumer credit permissions to lenders and intermediaries under different scenarios

Scenario 1						Total
Consumer credit categories	Up to 50k	50k–100k	100k–250k	250k–1m	Over 1m	n/a
Percentage of lenders/intermediaries in each category	30%	25%	20%	15%	10%	100%
Implied number of lenders in each category	27.6	23	18.4	13.8	9.2	92
Implied number of intermediaries in each category	60	50	40	30	20	200
Cost of FCA permission (Lenders)	£800	£1,000	£1,500	£5,000	£10,000	n/a
Cost of FCA permission (Intermediaries)	£600	£750	£1,000	£1,500	£5,000	n/a
Cost to lenders (by category)	£22,080	£23,000	£27,600	£69,000	£92,000	**£233,680**
Cost to intermediaries (by category)	£36,000	£37,500	£40,000	£45,000	£100,000	**£258,500**

Scenario 2						Total
Consumer credit categories	Up to 50k	50k–100k	100k–250k	250k–1m	Over 1m	n/a
Percentage of lenders/intermediaries in each category	10%	15%	20%	25%	30%	100%
Implied number of lenders in each category	9.2	13.8	18.4	23	27.6	92
Implied number of intermediaries in each category	40	60	80	100	120	400
Cost of FCA permission (Lenders)	£800	£1,000	£1,500	£5,000	£10,000	n/a
Cost of FCA permission (Intermediaries)	£600	£750	£1,000	£1,500	£5,000	n/a
Cost to lenders (by category)	£7,360	£13,800	£27,600	£115,000	£276,000	**£439,760**
Cost to intermediaries (by category)	£24,000	£45,000	£80,000	£150,000	£600,000	**£899,000**

Table 8 – Option 2 – Summary of the transitional cost of mortgage permissions to lenders and intermediaries

Group	Number expected to apply for permissions	Expected cost of FCA mortgages permission	Total
Lenders	92	£5,000	**£460,000**
Intermediaries	300	£1,500	**£450,000**

Table 9- Option 2 – Transition costs for lenders and intermediaries under different scenarios

Scenario 1						Total
Consumer credit categories	Up to 50k	50k-100k	100k-250k	250k-1m	Over 1m	n/a
Percentage of lenders/intermediaries in each category	30%	25%	20%	15%	10%	100%
Implied number of lenders in each category	27.6	23	18.4	13.8	9.2	92
Implied number of intermediaries in each category	60	50	40	30	20	200
Estimate of familiarisation costs (Lenders)	£625	£1,250	£2,500	£6,250	£25,000	n/a
Estimate of familiarisation costs (Intermediaries)	£313	£625	£1,250	£3,125	£5,000	n/a
Cost to lenders (by category)	£17,250	£28,750	£46,000	£86,250	£230,000	**£408,250**
Cost to intermediaries (by category)	£18,750	£31,250	£50,000	£93,750	£100,000	**£293,750**

Scenario 2						Total
Consumer credit categories	Up to 50k	50k-100k	100k-250k	250k-1m	Over 1m	n/a
Percentage of lenders/intermediaries in each category	10%	15%	20%	25%	30%	100%
Implied number of lenders in each category	9.2	13.8	18.4	23	27.6	92
Implied number of intermediaries in each category	40	60	80	100	120	400
Estimate of familiarisation costs (Lenders)	£625	£1,250	£2,500	£6,250	£25,000	n/a

Estimate of familiarisation costs (Intermediaries)	£313	£625	£1,250	£3,125	£5,000	n/a
Cost to lenders (by category)	£5,750	£17,250	£46,000	£143,750	£690,000	**£902,750**
Cost to intermediaries (by category)	£12,500	£37,500	£100,000	£312,500	£600,000	**£1,062,500**

Table 10 – Option 2 – Summary of costs to lenders and intermediaries related to the introduction of regulation for buy-to-let lending to consumers

Type of cost	**Total cost (Survey responses) – High**	**Market share of respondents**	**Implied total cost to the market**
Transitional cost – lenders	£1,200,000	56.94%	**£2,107,403**
Transitional cost– intermediaries	£429,000	50% (Best estimate)	**£858,000**
Ongoing cost – lenders	£456,000	56.94%	**£800,813**
Ongoing cost – intermediaries	£157,000	50% (Best estimate)	**£314,000**

Table 11 – Option 2 – Summary of the costs to lenders and intermediaries from having to register for with the FCA in order to conduct buy-to-let lending to consumers

Cost	Number expected to register	Registration fee – where firms are not already FCA authorised	Registration fee– where firms are already FCA authorised	Annual fee	Total (Best estimate)
Lenders – initial registration fee	102	£500	£100	n/a	**£12,200**
Intermediaries – initial registration fee	4150 (maximum)	£500	£100	n/a	**£497,800**
Lenders – annual fee	102	n/a	n/a	£100	**£10,200**
Intermediaries annual fee	4150 (maximum)	n/a	n/a	£100	**£415,000**

Table 12 – Option 1 and 2 – Summary of transitional and ongoing costs

Category	Transitional cost (High)	Ongoing cost (High)	Transitional cost (Low)	Ongoing cost (Low)	Transitional cost (Best)	Ongoing cost (Best)
Option 1 - Lender costs	£516,902,362	£12,169,789	£516,902,362	£12,169,789	£516,902,362	£12,169,789
Option 1 - Intermediary costs	£4,576,923	£120,192	£1,608,108	£42,230	£3,092,516	£81,211
Option 2 - CBTL - Lender costs	£2,897,678	£1,080,044	£1,317,127	£521,582	£2,107,403	£800,813
Option 2 - CBTL - Intermediary costs	£858,000	£314,000	£858,000	£314,000	£858,000	£314,000
Option 2 - Second charge - permissions- Lender costs	£460,000		£20,240		£240,120	
Option 2 - Second charge - permissions- Intermediary costs	£450,000		-£449,000		£500	
Option 2 - Second charge - familiarisation - lenders	£902,750		£0		£451,375	
Option 2 - Second charge - familiarisation - intermediaries	£1,062,500		£0		£531,250	
Option 2 - BTL - Costs from registering - Lenders	£12,200	£10,200	£12,200	£10,200	£12,200	£10,200
Option 2 - BTL - Costs from registering - intermediaries	£497,800	£415,000	£497,800	£415,000	£497,800	£415,000
Option 1 Total Costs	£521,479,284.66	£12,289,980.92	£518,510,469.69	£12,212,018.34	**£519,994,877.18**	**£12,250,999.63**
Option 1 Total Benefits	£0.00	£0.00	£0.00	£0.00	**£0.00**	**£0.00**
Option 2 Total Costs	£7,140,928.47	£1,819,243.79	£2,256,366.58	£1,260,782.12	**£4,698,647.52**	**£1,540,012.96**
Option 2 Total Benefits	£0	£0	£0	£0	**£0**	**£0**

Annex B – Summary of FCA cost/benefit analyses

The FCA have published their own cost-benefit analysis of both the changes they are making under their powers as an independent regulator to regulate certain sections of the mortgage market, as well as those changes required to meet the conditions in the MCD. This cost benefit analysis has been completed using a high level estimate of costs and benefits. However, alongside this, they have also commissioned KPMG to publish a separate cost benefit analysis (covering mainly the changes to second charge lending) that is more appropriate to summarise for the purposes of this impact assessment.

While the KPMG cost benefit analysis includes a lot of detail on the precise drivers of the any impact, the key figures it provides are the overall costs and benefits from MCD related changes. These are summarised below in table 13.

Table 13 – Summary of KPMG cost benefit analysis of the FCA's proposed changes to its rules

Cost	Estimate
Changes to FCA rules needed to meet maximum harmonising elements of the MCD. Predominantly, the introduction of the European Standardised Information Sheet (ESIS)	UK mortgage lenders: transitional cost- £5.3m, ongoing cost- £1.9m UK mortgage intermediaries: transitional cost- £1m, ongoing cost- £1m
Changes to FCA rules and Directive copy-out required to meet non-maximum harmonising elements of the MCD	UK mortgage lenders: transitional cost- £1.4m, ongoing cost- £1.2m UK mortgage intermediaries: transitional cost- £0.7m, ongoing cost- £0
Changes to FCA rules made in line with the FCA's discretionary power to regulate certain aspects of the mortgage market	UK mortgage lenders: transitional cost- £1.4m, ongoing cost- £0.6m UK mortgage intermediaries: transitional cost- £0.1m, ongoing cost- £0.6m [18]

The top two sections of table 16 are the most relevant for this impact assessment. They are the costs that UK business will face as a result of implementing the MCD in line with option 2. The bottom section summarises the costs that businesses will face as a result of additional rule changes the FCA has decided to make at the same time.

The FCA is generally positive about the changes it is making on a discretionary basis which it believes will lead to a net benefit (with consumers benefiting, at a cost to lenders and intermediaries), while it supports the Government's contention that the changes required to meet

[18] This estimate is largely driven by an estimate of £120,000 from a broker to comply with this requirement. If this particular estimate was excluded this figure would fall to £36,005.

the MCD do not add much to the existing regime in terms of benefits from increased consumer protection.