# Briefing

# Mortgage fees

## Contents





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# Executive summary

## *The importance of choosing the right mortgage*

Total outstanding mortgage debt amounts to over £1.2 trillion in the UK.[1] With mortgage holders spending £1 in every £5 (18%) of their household budgets on their mortgages[2], buying a house is the single biggest purchase most consumers will ever make. This means that choosing the wrong product can have a significant impact on consumers' finances. Currently, four in ten (38%) mortgage holders in the UK are unsure whether or not there is a better value product on the market for them.

In a genuinely competitive mortgage lending market, it should be easy for these borrowers to compare mortgage deals, understand product features and overall costs and make their decisions with confidence. However, this is not currently the case in the UK market. Just half of consumers (56%) who have chosen a mortgage in the last 5 years say they found it easy to compare different mortgage products.[3] Overall, greater product complexity and opaque fees and charges mean that consumers can struggle to make the decisions that are right for them.

These issues become all the more important as improvements in the UK economy begin to point towards the time when there will be an increase in the Bank of England base rate. Combined with rising house prices and continued Government support for the demand side of the housing market, it seems likely that significant numbers of consumers will be looking to make difficult decisions over their choice of (re)mortgage in the coming months. This highlights the importance of consumers being able to easily compare mortgage deals against each other and to choose the right mortgage for their circumstances.

## *Barriers to making the right choice*

A key barrier is the lack of clarity over how fees and charges impact on the total cost of different products. Borrowers need to understand this information to be able to pick the right mortgage for their circumstances. Our research found examples of mortgage products with higher interest rates but lower fees that were actually cheaper over the deal period than other products with lower interest rates but higher fees.

Taking the potential impact of fees into account is difficult for consumers and, with the existing information provided on mortgage products, our research shows that consumers struggle to make optimum decisions. Which? tested how consumers use information in mortgages to choose products. When presented with five different two

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[1] Council of Mortgage Lending, Gross Mortgage lending £18.6 in August, says CML, September 2014. Accessed: http://www.cml.org.uk/cml/media/press/4018

[2] Which? analysis of ONS data.

[3] Which? Consumer Insight mortgages data, December 2013.

year fixed-rate mortgage deals, and the typical information[4] often presented (including APR), fewer than half (48%) of consumers were able to identify the cheapest deal. Just 3% could correctly rank all five deals.

When the total cost over 24 months was displayed alongside the typical information, the proportion getting the entire ranking correct across all five deals increased twelve-fold, to 36%. Consumers were also much more likely to predict the cheapest (62% versus 48%) deal under this option than the standard version.

We also found that, while APR is typically described as the 'overall cost for comparison', and the EU Mortgage Directive dictates that APR must be used in promotional material for mortgages, it can be a barrier to consumers identifying the cheapest option. When APR was removed from the information displayed alongside the total cost, the proportion identifying the cheapest option rose by eight percentage points (to 70%).[5]

Our research also identified product features and lender practices that make comparisons difficult. These included that:

- There are a confusing array of fees, with similar purposes, but with different names in existence across the industry;
- It is not always clear which fees are avoidable and unavoidable to the mortgage holder;
- There is large variation in the costs of non-product related (e.g. administration) fees that different lenders charge. This indicates that these are neither cost reflective nor being driven down by effective competition; and
- Providers' websites sometimes display confusing information or make it hard for consumers to navigate and compare the range of products available that might suit their needs.

## *Principles to make consumer choice easier*

As a result of the issues highlighted in this briefing, many borrowers could be taking out products that are not the cheapest or most suitable for their needs.

Which? believes that to improve transparency and allow for more informed comparison across the market, the Government and the Financial Conduct Authority (FCA) must urgently explore alternative approaches to presenting the total cost of the mortgage to consumers. This should include exploring whether APR could be adapted or supplemented. At the very least, the Government and FCA should ensure that lenders make it clear which fees are compulsory for the borrower to pay and that the total cost of compulsory fees is prominently displayed.

[4] Typical information refers to: the introductory interest rate, the rate type (two-year fixed), APR and fees.
[5] Which? Consumer Insight mortgages test, August 2014.

All non-product fees and charges that are incurred after the purchase of a mortgage, and largely fund administrative costs, should also reflect lenders' actual costs. There is already a provision[6] which requires mortgage arrears charges to be 'equal to or lower than a reasonable calculation of the cost of the additional administration required'. A similar approach should be taken for other non-product fees.

### *Recommendations*

In order to improve effective competition and drive better outcomes for consumers in the mortgage market, the Government, FCA and industry must act together to implement the following:

### 1. Make mortgage price comparison easier for consumers:

- We have identified limitations and complexities associated with APR, including how consumers may be using it as a proxy for choosing fixed-terms deals. The Government and FCA should work with industry and consumer groups to explore alternative approaches to presenting the total cost of mortgage deals, including fees and charges. The research should explore the effectiveness of complements and potential alternatives to APR.

### 2. Make the full cost of a mortgage clearer for consumers:

- It will take time to develop and test a new approach to presenting the total cost of mortgage deals. To increase transparency now, all compulsory fees payable throughout the deal period in a mortgage contract should be expressed as a total of fees and included in the advertised costs. They should also be included in mortgage illustrations and contract documents.

- As well as showing fees and charges over the deal period, customers should always be provided with a tariff of charges that clearly lists all fees that the consumer may pay throughout the full life of the mortgage. The tariff of charges should clearly state which of these fees are compulsory and which are not.

### 3. Ensure additional mortgage fees and charges are cost reflective:

- Non-product fees and charges that are incurred after the purchase of a mortgage should reflect lenders' actual costs.

[6] FCA Mortgages and Home Finance: Conduct of Business sourcebook (MCOB :12.4): http://fshandbook.info/FS/html/FCA/MCOB

# Section 1:
# UK consumers and the mortgage market

For many consumers, there will not be a more significant long-term financial decision than buying a house and taking on a mortgage. Some 36% of UK households own their property with a mortgage[7] and, given that a mortgage is a long-term financial commitment that can tie consumers into repayments for decades, decisions made today can have long-term repercussions.

The scale of this market is also unparalleled in consumer finance. Total outstanding mortgage debt amounts to more than £1.2 trillion in the UK.[8] Our Consumer Insight data shows that three in ten (30%) mortgage holders owe between £50,001 and £100,000, and around one in ten (12%) owe between £100,001 and £200,000.[9] Out of their total spending, mortgage holders spend £1 in every £5 (18%) on mortgage payments.[10]

With mortgages taking up such a substantial portion of consumer spending, over a long timescale, it is clear that they significantly impact consumers' financial situation. As a result, it is vital that consumers are able to confidently and easily choose a mortgage product that is right for their individual circumstances. Choosing the wrong product can lead to significant detriment. For example:

- Just a 0.5 percentage point difference in the rate paid on a £200,000 mortgage over a 25 year period can equate to a difference in total payments of around £15,000; and

- Less-than-optimal decisions can also lead to consumers struggling to manage their finances. Our Consumer Insight Tracker has found that nearly half (46%) of mortgage holders believe they would encounter difficulty with trying to cope with a major unexpected financial expense.

While the importance of making the right choice in this market is clear, it does not seem to be a market that consumers feel serves them well. Nearly half (48%) of those that took out a mortgage or remortgaged in the last five years say that they found choosing the right mortgage stressful[11], and just half of mortgage holders (52%) report that they trust the mortgage industry to act in their best interests. Nearly two-thirds (64%) of mortgage holders are worried about mortgage rates.[12]

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[7] http://www.ons.gov.uk/ons/dcp171776_362811.pdf

[8] Council of Mortgage Lending, Gross Mortgage lending £18.6 in August, says CML, September 2014. Accessed: http://www.cml.org.uk/cml/media/press/4018

[9] Which? Consumer Insight Tracker data, September 2014

[10] Which? analysis of ONS data

[11] Which? Consumer Insight mortgages data, October 2014.

[12] Which? Consumer Insight Tracker data, September 2014.

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These issues become all the more important as improvements in the UK economy begin to point towards the time when the Monetary Policy Committee will take steps to increase the Bank of England base rate. While the Financial Policy Committee[13] and the FCA[14] have put measures in place in an attempt to mitigate some of the potential impacts on consumers, after five years of record-low rates of 0.5%, the extent of consumer worry and scale of potential detriment and financial distress means that this remains a great concern.

At the very least, it is possible that a rate rise will serve as a prompt for some to begin looking for alternative offers. A third (32%) of those who have taken out a mortgage or remortgaged in the last five years report they are likely to consider remortgaging when interest rates rise.[15] Those on standard variable rate (SVR) mortgages may also seek to switch to a fixed-rate deal that protects them against rate rises in the medium term.

There are also other factors pointing towards a number of consumers either looking to take on mortgages for the first time, or exploring opportunities to remortgage:

- A number of Government schemes have already supported the demand side of the housing market. For instance the government-backed *Help To Buy* equity loan scheme has helped more first-time buyers to get on the housing ladder, while the *Help To Buy* equity guarantee scheme has led to an increased availability of high loan-to-value (LTV) mortgage deals.[16]

- While still far from its 2007 pre-crisis peak, according to the Council of Mortgage Lenders (CML), gross mortgage lending reached £17.8 billion in September of this year, 10% higher than September last year (£16.2 billion). Overall, gross mortgage lending for the third quarter of 2014 was an estimated £55.5 billion; a 8% increase from the second quarter of this year.

- With house price increases of around 6.4% in the year to June 2014[17] and predictions of continued rises over the coming years[18], more mortgage deals will also be available to existing borrowers as their LTV falls.

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[13] The Financial Policy Committee has stated that, as of October 2014, only 15% of new mortgages that are more than 4.5 times of a borrowers' income will be approved, and all lending will be subject to extra affordability tests. This is in addition to a stress-test exercise currently being run by the UK banking sector, to assess whether borrower's could still afford their mortgages if their interest rates were to rise by more than 3% in the first five years of the loan.

[14] A recent thematic review by the Financial Conduct Authority also concluded that there have been some improvements in arrears management, including offering a wider range of forbearance options[14], which may have helped customers struggling to meet repayments. However, the FCA review also indicated that mortgage lenders and administrators must do more to proactively assist customers susceptible to potential rate rises.

[15] Which? Consumer Insight mortgages data, October 2014.

[16] Help to Buy Equity loan scheme and Help to Buy: NewBuy statistics: data to 30 June 2014, England; Bank of England, Financial Stability Report, June 2014, Issue No. 35, pp. 25-26

[17] Land Registry, House Price Index, Headline Statistics, June 104, pg. 3. http://www.landregistry.gov.uk/__data/assets/pdf_file/0010/96805/HPIReport20140721.pdf

[18] http://www.savills.co.uk/research/uk/residential-research/forecasts.aspx

These factors suggest that significant numbers of consumers will be looking to make difficult decisions over their choice of mortgage in the coming months. This makes it even more important than ever that consumers are able to easily compare mortgage deals against each other and to choose the right mortgage for their circumstances.

This briefing explores the current features of the mortgage market that impact consumers' ability to do just that. It shows that choosing mortgage products is unnecessarily complicated by opaque fees and charges and the way information on mortgage deals is presented. It demonstrates that these practices can result in borrowers struggling to identify the cheapest products and argues that this diminishes competitive pressure in the market. Together, it shows that there is clearly scope for improvement in this market and suggests reforms to ensure that consumers are able to choose the right mortgage with minimal hassle and stress.

# Section 2:
# Fees and charges obscure the total cost of mortgages

Section 1 outlined that mortgages are a significant financial commitment for consumers and that, in the current climate, it is vital that they are able to confidently compare products accurately and easily. However, our research of consumers that have taken out a mortgage or remortgaged in the last five years suggests that consumers find engaging in this market difficult:

- Just half (52%) trusted the mortgage industry to act in their best interest;
- Only 56% said they found it easy to compare different mortgage products;
- Four in ten (38%) were unsure whether or not there is a better value mortgage product on the market than the one they have; and
- Half (48%) reported they found the process of choosing the right mortgage stressful.

As a result, borrowers could be taking out products that are not the cheapest or most suitable for their needs.

## Lenders charge a confusing variety of fees and charges

One of the key factors that drives this problem is the unnecessary product complexity that stems from opaque fees and charges. In the current mortgage market, many lenders are offering very low interest-rate mortgage deals and are advertising these rates widely; there has been significant media coverage of the ‘record low mortgage rate’ environment. However, often underpinning these low interest rates is an array of fees and charges. The result is that the advertised interest rate is not necessarily the best way to judge the true cost of a mortgage product, and the total cost of a mortgage is extremely difficult to compare for consumers.

Lenders have fees for a wide variety of purposes and tasks – from set-up fees through to arrears fees, overpayment fees and fees to change the length of the mortgage term. Some are related to the product itself and can be payable at the outset and some are incurred at the end of the mortgage term or when the mortgage is paid off (such as redemption Fees). Others are not related to the core product design and typically depend on the actions and behaviours of the individual borrower (such as arrears fees and copy statement fees).

Below are some examples of the fees borrowers may come across when taking out a mortgage:

| **Fees charged before (set-up fees)** | **Fees charged during the length of the mortgage** | **Fees charged at the end of the mortgage** |
|---|---|---|
| Administration Fee | Porting Fee | Mortgage Account Fee |
| Application Fee | Transfer of Title Fee | Mortgage Exit Admin Fees Total |
| Letting Property Fee | Arrears Fee | Deeds Release Fee |
| Assessment Fee | Arrears Letter Fee | Release of Part Security Fee |
| Chaps Transfer Fee | Conversion of Mortgage Type Fee | Redemption Admin Fee |
| Arrangement Fee | Copy Statement Fee | Final Repayment Fee |
| Insurance Fee | Deeds Enquiry Fee | Sealing Fee |
| Reservation Fee | Unpaid Standing Order Fee | Redemption Fee |
| Mortgage Reference Fee | Mortgage Term Change Fee | |
| Product Fee | Solicitor Arrears Fee | |
| Booking Fee | Repossessed Property Fee | |
| Revaluation Fee | Unpaid Direct Debit Fee | |
| Reinspection Fee | Unpaid Cheque Fee | |
| Lenders Fee | Unpaid Ground Rent Fee | |
| Withdrawal Fee | Arrears Breakdown Fee | |
| Completion Fee | | |
| Mortgage Questionnaire Fee | | |

A common theme is that fees charged for the same or similar purposes are called different things between lenders. This immediately adds a layer of complexity for consumers if they are trying to compare mortgage products between different providers. For example, a ‘booking’ fee is a set-up fee paid after a mortgage application has been completed to ‘book’ or ‘reserve’ mortgage funds while the application is being completed. However some lenders may call this fee a ‘reservation’ fee or an ‘application’ fee.

As well as the existence of a wide variety of fees, the costs of some fees have increased over time. For example, the average arrangement fees on a mortgage increased from £878 in 2009 to £1,588 in October 2014.[19] Combined with less prominence in advertising and media commentary, this has made it difficult to both assess whether the true cost of mortgages has really come down as low interest rates suggest, and for consumers to compare different deals.

[19] Moneyfacts data. This is looking at the average of flat arrangement fees (i.e. of specific arrangement fee amounts rather than a percentage of the loan) across the mortgage market.

*Example: Complexity in 'Set- up' fees*

Arrangement fees are just one example of broader set-up fees. Set-up fees are charged when consumers first take out a mortgage. In September 2014, 84% of the 3,331 mortgages on offer from 82 mortgage lenders came with some kind of set-up fee.[20] As highlighted previously, these set-up fees were often referred to in a variety of terms between providers, including 'arrangement' fee, 'mortgage account' fee and 'product' fee. Some lenders charge more than one set-up fee.

The table below shows the mortgage products with the highest set-up fees in August 2014. The fees are based on a £100,000 loan and reflect fees charged by lenders on at least one of their mortgage products.

| Lender | Arrangement fee | Arrangement Admin fee | Booking fee | Completion fee | Total set-up fees |
|---|---|---|---|---|---|
| West Bromwich BS | £0 | £0 | £199 | £2300 | £2499 |
| Precise Mortgages | £2495 | £0 | £0 | £0 | £2495 |
| TSB | £1995 | £0 | £0 | £265 | £2260 |
| Teachers BS | £1999 | £0 | £99 | £0 | £2098 |
| MBS Lending Ltd | £150 | £0 | £0 | £1895 | £2045 |
| HSBC | £0 | £0 | £1999 | £0 | £1999 |
| Skipton BS | £0 | £0 | £195 | £1800 | £1995 |
| Accord Mortgages | £0 | £130 | £0 | £1845 | £1975 |
| Platform | £1499 | £0 | £0 | £0 | £1499 |
| Woolwich from Barclays | £1499 | £0 | £0 | £0 | £1499 |
| Scottish Widows Bank | £0 | £0 | £1499 | £0 | £1499 |

**Source: MoneyFacts, August 2014.**

[20] Source: Moneyfacts, September 2014.

## Evaluating fees and charges is essential for understanding the total cost of a mortgage

The presence of fees and charges can have a significant impact on the overall costs of taking out a mortgage. Box 1 outlines scenarios to demonstrate the impact that set-up fees can have.

### Box 1: the impact of set-up fees on the costs of a mortgage

One of the lowest rates for a two-year fixed deal at 65% LTV was from West Bromwich BS at 1.59%. However, this comes with product and valuation fees totalling £1,999. This means that over the two-year deal period, this would cost £11,999 for a £100,000 mortgage.

In contrast, Norwich and Peterborough BS offered a higher rate at 2.14%, but with lower fees meaning that the total cost over a two year deal period would amount to £10,496. This means a saving of £1,503 for the borrower compared to West Bromwich's deal.[21]

We saw a similar situation with three-year fixed 65% LTV deals. With a £100,000 mortgage, a borrower could save more than £800 by opting for Norwich and Peterborough's 2.94% deal instead of First Direct's 2.79% rate which included product fees of £1,450 on top.[22]

Source: Moneyfacts, August 2014. The calculations refer to deals available in August 2014.

The fact that providers can charge multiple fees adds to the impact of fees on mortgages and the difficulty in making an accurate comparison. Overall, it is clear that, if consumers are to make the right choice for them, decisions need to consider the total costs. However, many consumers do not do this; Which? research reveals that of consumers that had taken out a mortgage or remortgaged in the last five years, just 16% ranked the total costs of the mortgage over the fixed/deal period as the most important factor when choosing.[23]

[21] This includes a rebate of £500 from Norwich; however even without this the deal still works out cheaper for the consumer compared to West Bromwich's offer.

[22] These calculation assume the fees are paid separately to the mortgages. The First Direct mortgage is an offset mortgage.

[23] Which? Consumer Insight mortgages data, October 2014.

### *Difficulties in determining whether a fee is avoidable or unavoidable*

It can also be unclear whether fees are unavoidable (i.e. the borrower has no choice but to pay the fee) or avoidable (such as fees incurred when a borrower requests something from the lender). Of note are fees incurred at the end of a mortgage. For example, we found that some lenders charged for deeds fees, whereas others didn't. Deeds fees were historically charged for the lender to release the physical copy of your title deeds and send them to you at the end of the mortgage. Today, title deeds are accessible as electronic copies. With a number of charges holding a variety of names, the term deeds fees may be used to refer to an exit fee; or the term may refer to a service that includes, but may not be exclusive to, providing a copy of title deeds.

For example, as stated in their tariff of charges, Leeds Building Society currently charges £65 for a 'despatch of title deeds'. It is unclear on the tariff whether this is a compulsory or non-compulsory fee. When we spoke to them, they specified that this fee would not be charged when a customer remortgages or switches their mortgage, but it would be charged in certain circumstances e.g. when a customer needs a copy of their title deeds for divorce proceedings or transfer of equity.

This is not made clear to the customer in the information available through their tariff of charges, making it difficult for consumers to compare different deals at the initial stage of looking for a mortgage. This is due to a lack of clarity on which fees are compulsory. We also found this when looking at the tariff of charges of other providers, including Newcastle Building Society, Ulster Bank and Progressive Building Society.

Deeds fees are even more confusing when we consider that, for those who have a mortgage on a registered property (80% of properties are registered), title deeds are held digitally by the Land Registry. Owners can request a copy from Land Registry for just £7. Some consumers may be unaware of this and so may end up paying an unnecessary amount by requesting these from their lender instead of Land Registry.

These factors highlight the need for increased transparency on what fees are unavoidable for the borrower and will consequently affect the total cost of their mortgage, and whether or not they are cost reflective.

### *Extra fees vary significantly and aren't cost reflective*

As well as a lack of clarity over the basis (avoidable or unavoidable) of some of these fees, we also found significant price dispersion among fees from different providers. As these fees are not related to the core product features and are simply paying for administrative activities, this suggests both that they are not cost reflective and that competition is failing to drive down these costs effectively.

One example of this dispersion is sealing fees. These fees are charged by the lender for legally 'sealing' the documents at the end of the mortgage term. 18 lenders charged this sealing fee, representing 280 mortgage products and an average fee of £97 (an increase of 16% from the average fee in May 2013).[24] The most expensive were:

| Provider | Sealing fee |
|---|---|
| Beverley BS | £175 |
| Hinckley & Rugby BS | £150 |
| First Trust Bank (NI) | £150 |
| Allied Irish Bank (GB) | £150 |
| Leek United BS | £125 |
| Manchester BS | £120 |
| Earl Shilton BS | £100 |
| Buckinghamshire BS | £100 |
| Vernon BS | £100 |

**Source: MoneyFacts, August 2014.**

The cheapest of those who charged was from Furness BS at £50.

Examples of other fees that revealed large price dispersion between lenders included:

- While Kent Reliance charge £25 for a bounced cheque or failed direct debit, The Cooperative bank charges £8 and Norwich and Peterborough Building Society charge just £5 and £2 respectively.
- The Cooperative Bank charges £32 plus VAT for a second mortgage questionnaire whereas Principality BS charges almost three times more at £91 for a second mortgage questionnaire.
- Nationwide BS charge £20 for an amendment to the mortgage term while Virgin Money charges £50.
- Yorkshire BS charges £10 for a breakdown of mortgage transactions; The Cooperative Bank charges £18.

## *Better information can improve decision making*

The annual percentage rate of charge (APR) is typically described as the 'overall cost for comparison' and the EU Mortgage Directive, which came into effect in February 2014, dictates that APR must be used in promotional material for mortgages. However as Box 2 indicates below, APR is not always fit for this purpose.

[24] Which? analysis of Moneyfacts data.

### Box 2: Limitations of the Annual Percentage Rate of Charge (APR)

Which? argues that APR on its own is not an adequate measure for comparing all mortgage products, for instance, for calculating how much the cost of repayments will be over a given period. This is due to the following limitations:

*APR is not an accurate indicator of the total overall costs of a mortgage product*

- The calculation of APR assumes your lender's standard variable rate (SVR) won't change during the term of the mortgage, and therefore does not show the impact of increases (or decreases) in SVR over time.
- Furthermore, post-application fees are not included in the calculation even where they are unavoidable.

*APR does not account for the high likelihood of switching during at least some point in the term*

- APR assumes you will keep the same mortgage for the whole term (usually 25 years), with fees spread over that period. However, many borrowers do not hold their mortgage for the whole term. Previous research has shown that consumers, on average, remortgage every five years.[25] More recent Which? customer satisfaction data also suggests a similar story: in March 2014, 40% of those surveyed reported having remortgaged in the last five years, with their average mortgage tenure being 7.9 years.
- In addition, other costs incurred when switching mortgage products (for example, the impact of additional set-up fees) are not designed to be captured within the APR calculations and need to be factored in separately.

*APR is not appropriate for ranking the costs of fixed-rate deals*

- Lastly, given that APR is designed to show the cost of a product over a 25 year term, it is not designed to compare the total costs of a product incurred during a fixed-rate deal period.

**What this means in practice …**

As one example of the potential limitations of APR, we can consider the impact of set-up fees when paid up-front. These may not seem significant in percentage terms, but could quickly add up if a consumer remortgages every few years. For example, if a borrower with a £200,000 mortgage, over a ten year period, were to switch their mortgage deal every two years – keeping a rate of 1.99% but paying £1,500 in arrangement fees with every switch- over a ten year period they would accrue £6,000 of costs not anticipated by the initial APR on the first mortgage taken out by the consumer.

[25].CML Market Briefing. Accessed: https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=1&cad=rja&uact=8&ved=0CCQQFjAA&url=http%3A%2F%2Fcml.org.uk%2Fcml%2Ffilegrab%2Fpdf_pub_misc_mbadhoc2004-

5.pdf.pdf%3Fref%3D3579&ei=HrUzVPOQK4TwaMrDgLAD&usg=AFQjCNGIW5KNE9auG12iRbawql-uzBPLLw&sig2=Md-ldBxVi0wl2lUyGFbY9A&bvm=bv.76943099,d.ZWU

To test the effect that this might have on consumer decision making, Which? undertook research to understand how different information impacts the choices consumers make in the mortgage market. Overall, we found that consumers struggle with finding and ranking the cheapest fixed-rate mortgage deals. Our results also show that consumers tend to be over-confident and over-reliant on APR as a measure of comparison. This contributes to consumers making less accurate decisions.

In our tests, consumers were presented with five two year fixed-rate mortgage deals, and were asked to rank them according to which would be cheapest over two years. They were told to assume that these were interest-only mortgages and that all fees would be paid up-front. We tested three different scenarios for how the information was displayed:

- With the introductory fixed-rate interest rate, the APR and the applicable fees – in much the same way that mortgage deals are typically presented.
- The same as the typical presentation but with an additional column on the table showing the total cost over 24 months (including fees); and
- The same as the typical presentation but with an additional column with the monthly costs and the fees.

Table 1 highlights the results from the trials. It shows that, when provided with the typical information, fewer than half (48%) of consumers were able to correctly identify the cheapest mortgage deal. Just 3% could correctly rank all five deals.

When the total cost over 24 months was displayed alongside the typical information, the proportion getting the entire ranking correct increased from 3% to 36%. Consumers were also much more likely to predict the cheapest (62% versus 48%) deal under this option than the standard version.[26]

*Table 1: Results from tests from tests of mortgage information impacts*

| Option | % with cheapest correct | % with cheapest and most expensive correct | % with entire ranking correct |
|---|---|---|---|
| Typical presentation | 48% | 22% | 3% |
| Total cost over 24 months | 62% | 46% | 36% |
| Monthly cost | 36% | 19% | 9% |

[26] Populus, on behalf of Which?, interviewed 2042 GB adults online between the 15th and 17th August 2014. Data were weighted to be demographically representative of all GB adults. Populus is a member of the British Polling Council and abides by its rules.

### *Displaying APR can make decision making more difficult*

This demonstrates that displaying information on the total cost of mortgages can improve consumer decision making. To assess the impact of APR itself, we also compared responses from consumers presented with each option both with and without APR. Our results suggest that APR can be detrimental to decision making.

Figure 1 shows that removing the APR figure from the information provided to a consumer increased the likelihood of them correctly identifying the cheapest and most expensive products by between 24% and 53% depending on the scenario.

*Figure 1: Removing APR improves likelihood of consumer identifying cheapest and most expensive*

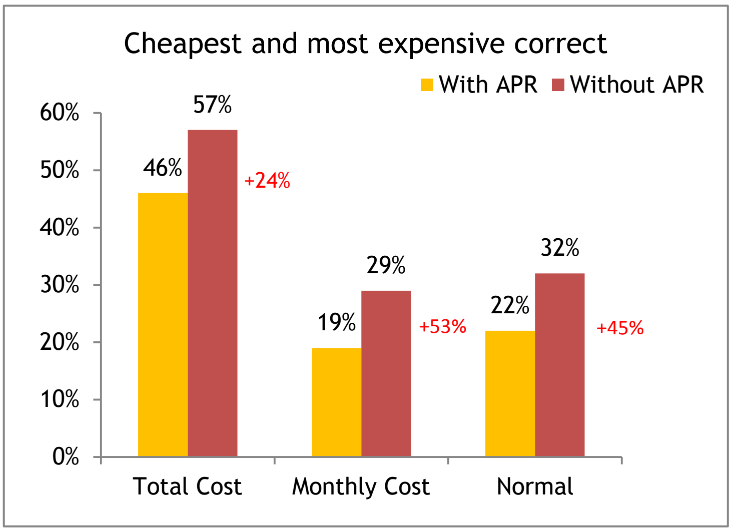
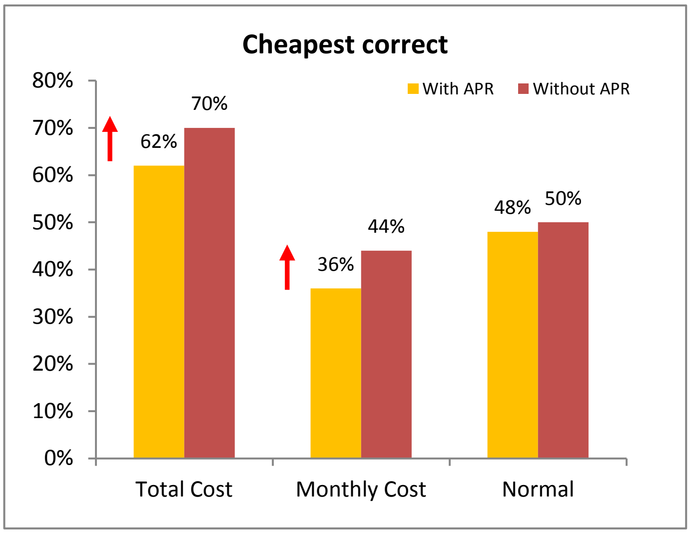



Figure 2 shows the same information, but only considering the impact on the proportion of consumers correctly identifying the cheapest product. It suggests that, combined with showing the total cost over 24 months, removing the APR figure increases the proportion of consumers identifying the cheapest deal by eight percentage points to 70%.

*Figure 2: Combined with total costs, removing APR significantly improves likelihood of consumer identifying cheapest deal*




However, simply removing the APR from the normal presentation of information has no statistically significant impact on the proportion identifying the cheapest option.

Overall, this suggests that, while consumers are using APR as a proxy to understand the total costs of mortgages, in some circumstances it can be quite misleading, particularly for fixed-term deals. Some of the reasons why this may be the case have been captured in Box 2.

### *Even confident consumers can still struggle to compare products*

Nearly half (47%) of those who took part in this research said that they found the task difficult when shown the typical information. However, even those participants who said they found the task easy (23%) often struggled to correctly identify the cheapest options. Of this group:

- Just half (48%) correctly identified the cheapest deal;
- Only 6% were able to correctly rank all five deals in order of price; and
- Despite the problems with using APR as a comparison tool, more than half (55%) said that APR was the piece of information they found most useful.

# Section 3:
# Other practices that make consumer decisions difficult

As in any properly functioning, genuinely competitive market, consumers should be provided with the information to enable them to compare mortgage deals accurately and with ease. Consumers use a range of sources for information when choosing mortgage products, and they should be able to access the comprehensive information they need from any of the sources they choose to support the decision making process.

We have already shown that, even with access to accurate information, consumers may not always make the best decisions for their circumstances. This situation is compounded by practices which make it difficult to gather the relevant information or that make that information more complex than necessary.

The next section sets out that more needs to be done to give the right information to consumers and remove difficulties with the way information is presented, to enable consumers to make optimal decisions in this market.

### *Lenders' online information does not enable consumers to easily compare and choose deals*

Which? checked the websites of 14 of the largest mortgage lenders[27] to find out whether costs were presented in a way that enabled consumers to easily compare mortgage deals. We found that the way in which information is presented can often add an additional layer of complexity for consumers, making it difficult for them to judge the true cost of a mortgage and to compare accurately between lenders.

For example, given the findings in Section 2, it is concerning that, while lenders show the interest rate and some of the fees chargeable on their mortgage range, they rarely combine the two. There is also a lack of standardisation as to how this information is displayed across different providers. As well as this, some lenders' online mortgage finder tools insist that borrowers select a particular product type before they see the available options. However, until borrowers understand the costs of the different products they will not be in a position to decide whether they want a fixed or variable rate deal, or how long they want the initial mortgage deal to last.

[27] Barclays, First Direct, HSBC, Leeds BS, Lloyds Bank, Metro Bank, Nationwide, NatWest, Principality BS, Santander, The Co-operative Bank, Virgin Money, Yorkshire & Clydesdale Banks and Yorkshire BS

- Mortgage comparison tools from NatWest and Principality BS insist that you choose between a fixed and variable or tracker deal before they show results, while Yorkshire and Clydesdale Banks ask users to choose between fixed and offset deals before it searches. Similarly, Yorkshire BS asks users to choose between a fixed-rate, offset and tracker deal before showing options.

- However, the most restrictive tool is that of Leeds BS. Once users have put in information about the value of the property, how much they wish to borrow, and the length of time, a drop down list of available products appears and the user must select one to continue. This is without explaining the different products types or giving any further information of costs, fees or suitability of the product to the customer's situation.

# Conclusions and recommendations

Choosing the right mortgage can have a significant impact on household finances. The best deal for each individual will depend on how much they're borrowing, the length of the deal, the fees charged on each deal and whether they keep the mortgage once the initial deal period has expired. It is a long-term and potentially challenging financial decision.

However, in a genuinely competitive mortgage lending market, it should be easy for borrowers to compare mortgage deals, understand the features and costs of each and make decisions with confidence. This is not currently the case in the UK market. Greater product complexity and opaque fees and charges mean that consumers can struggle to make the decisions that are right for them.

Our research has shown that a lack of information on the total costs of each deal and the reliance on APR can distort consumer decisions in some circumstances. In our tests using fixed-term deals, when adding information on the total costs, including fees, and removing reference to the APR, significantly more consumers were able to identify the cheapest fixed-rate mortgage deal from the options we presented them.

We also found that the information and tools provided by providers can be unhelpful for consumers looking to compare products, and that the range and opacity of fees and charges levied make comparison difficult and potentially limit competition.

As a result, many borrowers could be taking out products that are not the cheapest or most suitable for their needs. With mortgage holders spending £1 in every £5 (18%) of their household budgets on their mortgages[28], buying a house is the single biggest purchase most consumers will ever make, and mortgage repayments are likely to be their largest single monthly expense.

[28] Which? analysis of ONS data.

In order to improve effective competition and drive better outcomes for consumers in the mortgage market, the Government, Financial Conduct Authority (FCA) and the industry must act together to implement the following:

1. **Stop making it hard to compare prices/Make mortgage price comparison easier for consumers:**

   - We have identified limitations and complexities associated with APR, including how consumers may be using it as a proxy for choosing fixed-terms deals. The Government and the FCA should work with industry and consumer groups to explore alternative approaches to presenting the total cost of mortgage deals, including fees and charges. The research should explore the effectiveness of complements and potential alternatives to APR.

2. **Don't hide the full cost from customers/Make the full cost of a mortgage clearer for consumers:**

   - It will take time to develop and test a new approach to presenting the total cost of mortgage deals. To increase transparency now, all compulsory fees payable throughout the deal period in a mortgage contract should be expressed as a total of fees and included in the advertised costs. They should also be included in mortgage illustrations and contract documents.

   - As well as showing fees and charges over the deal period, customers should always be provided with a tariff of charges that clearly lists all fees that the consumer may pay throughout the full life of the mortgage. The tariff of charges should clearly state which of these fees are compulsory and which are not.

3. **Stop stinging customers with rip off additional charges/Ensure additional mortgage fees and charges are cost reflective:**

   - Non-product fees and charges that are incurred after the purchase of a mortgage should reflect lenders' actual costs.