Equity Release Council

Fair value frameworks and assessments under the Consumer Duty

Part A

Introduction

to a fair value assessment

The Equity Release Council has produced this guidance to set out the key considerations and inputs for equity release manufacturers and distributors when developing a fair value assessment framework and completing a fair value assessment under the Consumer Duty.

It has been split into three parts:

Part A
Introduction
to a fair value assessment

Part B
Completing
a fair value assessment

Part C
Governing
a fair value assessment

This is Part A.

Contents

Introduction to fair value assessments **4**

Purpose 5

Roles and responsibilities **6**

Defining roles and responsibilities 7

Funder and manufacturer relationships 7

Manufacturer and distributor relationships 8

Distributor and introducer relationships 9

Fair value assessment methodology **10**

Definition of fair value 10

Fair value assessment 10

Fair value dimensions 11

Fair value assessment: Commonality and variance 11

Introduction to fair value assessments

The Financial Conduct Authority (FCA) published its finalised rules for the Consumer Duty on 27 July 2022 with the intention of creating a 'paradigm shift' in the treatment of retail consumers and making firms' senior management more accountable for this treatment. Within these rules, the FCA introduced the new 'consumer principle', its three cross cutting rules and the four outcomes for the key elements of the firm-consumer relationship. The structure of the Consumer Duty can be found in the diagram below:

Consumer duty structure

Consumer principle

Overarching cross cutting rules
Firms must take all reasonable steps to:
- avoid causing foreseeable harm
- enable customers to pursue their financial objectives

Firms must act in good faith toward customers.

Four outcomes for the key elements of the firm-consumer relationship:
1. Products and services
2. Price and value
3. Consumer understanding
4. Consumer support

The completion of a fair value assessment is one of the key requirements of the new Consumer Duty rules under the price and value outcome and the Equity Release Council has produced this guidance, which comes in three parts, to support its members with this assessment. This assessment will enable a firm to understand whether there is a reasonable relationship between the benefits a consumer receives from a product and/or service and the price a consumer pays for that product and/or service. This relationship should be subject to ongoing review to ensure that the relationship between benefits and costs remains appropriate and reasonable. Firms must take action where it assesses that the product and/or service does not provide fair value.

The FCA has been clear that firms are expected to take a proportionate approach to the implementation of these requirements based on the size, scale and complexity of their business. This will allow firms a degree of flexibility considering the factors that may be relevant for their sector and the nuances of their business model.

The guidance documents will include the key considerations and inputs for equity release manufacturers and distributors when developing a fair value assessment framework and completing a fair value assessment under the Consumer Duty.

✕ The assessment of fair value is not intended to be used by manufacturers and distributors to justify their existing business models where this does not provide fair value.

✓ This process should enable manufacturers and distributors to unearth areas where there may be potential issues in business models and challenge the fair value of their products and/or services. If there are areas identified where it is determined that fair value is not being provided to consumers, firms should take appropriate actions to mitigate, and where appropriate, remediate any harm to existing consumers and prevent harm to new consumers.

Purpose

The guidance documents have been split into three parts:

Part A	Part B	Part C
Introduction to a fair value assessment	**Completing** a fair value assessment	**Governing** a fair value assessment

The three documents are aimed at assisting Equity Release Council member firms with the following:

> The key steps and considerations to be taken when designing a fair value assessment framework and the key inputs and considerations that will be required when completing a fair value assessment.

Each part should be read in conjunction with each other and is not intended to be exhaustive. They should also be read and used in conjunction with the FCA's Consumer Duty rules (PS22/9: A New Consumer Duty) and guidance (FG22/5 Final non-handbook Guidance for firms on the Consumer Duty) and the Equity Release Council standards. Firms will need to tailor the fair value assessment to their individual business models, taking into account the products and/or services provided and the value chain in operation.

Part A will provide an introduction to the requirements required by the FCA on outcome two (price and value) in relation to the assessment of fair value. It will also explain the different parties within the price and value chain and outline key considerations for firms when defining their roles and responsibilities under the Consumer Duty. This section will also provide guidance relating to the methodology firms should consider when developing their fair value assessments.

Roles and responsibilities

There are typically a number of different stakeholders involved throughout the value chain of an equity release product and/or service which normally includes the following:

Term	Definition	FCA defined role?
Funder(s)	Firms that invest resources including the capital required to provide manufacturers with the means to bring the product or service to market.	No
Manufacturer	Firms are considered manufacturers under the Consumer Duty if they create, develop, design, issue, manage, operate, carry out, or underwrite a product or service.	Yes
Co-manufacturer	Firms are considered co-manufacturers under the Consumer Duty where they can determine or materially influence the manufacture of a product or service. This would include a firm that can determine the essential features and main elements of a product or service, including its target market.	Yes
Distributor	Firms are considered distributors under the Consumer Duty if they offer, sell, recommend, advise on, arrange, deal, propose, or provide a product or service, including at renewal.	Yes
Introducer	An individual appointed by a firm to carry out either or both of the following activities: effecting introductions; and/or distributing non-real time financial promotions.	This is the definition used in the FCA glossary terms.

The level of complexity involved in completing a fair value assessment will vary depending on the number of parties within the value chain and the roles and responsibilities of each party within the manufacturing/distribution of the product and/or service.

Before completing the fair value assessment, it is important that the parties involved in the value chain understand their roles and responsibilities as a fair value assessment is only required for the parts of the process for which a party is responsible. The specific role a firm plays within the value chain will need to be appropriately captured as part of the fair value assessment including what information should be requested/provided to enable the assessment to be completed.

Defining roles and responsibilities

The FCA defines different roles and responsibilities which they expect firms to take within the manufacturing and distribution chain. Firms should take steps to ensure that the key responsibilities and accountabilities are clearly defined between all parties (funders, manufacturers, distributors and introducers) and that all relevant parties agree with the allocation of the responsibilities. This is not expected to be in the form of a written or contractual agreement other than for manufacturers and co-manufacturers which is discussed later in this document.

Firms may find it useful to map out the typical consumer journey for each product and/or service and record which party has responsibility for the individual components of this journey or where firms will share this responsibility. Firms should be clear what role they are undertaking in the overall journey and where the business model is more complex and firms have multiple roles and responsibilities, these should be clearly mapped out and regularly reviewed to ensure there is adequate oversight in place between firms.

Firms should also consider their role throughout the journey against each outcome of the Consumer Duty requirements and their ability to influence the outcome that a consumer may receive before determining whether they have a sole, joint or no responsibility for the requirements of the Consumer Duty. The ability to influence a consumer outcome is not limited solely to the price of a product and/or service or which product features or services will be available to consumers. Firms may be able to influence the service level which is provided to consumers through contractual arrangements which can materially influence the consumer outcome. In some circumstances it may bring that party within the manufacturing sphere and therefore it is important that firms clearly understand the roles and responsibilities they have and that the other parties in the business model have the same level of understanding.

Manufacturers and co-manufacturers must have a written agreement outlining their respective roles and responsibilities to comply with the Consumer Duty rules. This agreement must reflect how roles and responsibilities are applied in practice. The FCA expect the agreement to be a confirmation of which firm is responsible for meeting different aspects of the rules under the outcomes for Consumer Duty.

Funder and manufacturer relationships

One of the nuances that is specific to the equity release market is the funding model for these mortgages. Depending on the contractual arrangements in place between manufacturers and funders, funders can have a significant influence over the price, features and service levels provided to consumers throughout the product lifecycle. Where funders influence these items, firms should record the influence that an external party has within the fair value assessment and consider whether this involvement results in the funder being classified as a co-manufacturer.

There are two types of funders, those which are regulated by the FCA and those that are unregulated, some of which may also operate in different jurisdictions to the UK. If the funder is an unregulated entity, the regulated entity will remain solely responsible for ensuring that the products and/or services comply with the new Consumer Duty rules. In these instances, the manufacturer as the regulated entity should ensure they have sufficient access to information from the unregulated entity to enable them to complete the fair value assessment as well as have sufficient oversight controls in place to effectively monitor that the unregulated entity is discharging its responsibilities as defined by any written agreement/contract. If unregulated firms are not willing to provide this information or agree to this level of oversight, regulated firms should consider whether working with an unregulated entity may lead to too great a risk of poor outcomes.

If the funder is a regulated entity, manufacturers and funders will need to agree their respective roles and responsibilities for complying with the Consumer Duty requirements and whether the funder will be considered as a co-manufacturer. In these instances, the funder should provide the manufacturer with sufficient access to information to enable the manufacturer to complete the fair value assessment and allow the manufacturer to have sufficient oversight controls in place to effectively monitor this an on ongoing basis; or

The FCA expects written agreements to confirm which firm is responsible for meeting different aspects of the rules under the specific outcomes. Manufacturers and funders will need to agree their respective roles and responsibilities for complying with the Consumer Duty requirements and whether the funder will be considered as a co-manufacturer. Firms should also review existing contractual arrangements to ensure that the newly agreed roles and responsibilities are appropriately reflected in the contractual terms between the parties.

Manufacturer and distributor relationships

The role of the manufacturer and distributor should also be clearly defined. The manufacturer will be responsible for the design, approval, testing and regular review of products/services and must identify the target market (including identifying vulnerable customers) for their products and/or services and select appropriate distribution channels. The distributors will be responsible for developing and reviewing distribution arrangements on an ongoing basis. These parties must share information with one another so that each can discharge their respective obligations.

As part of the price and value outcome, manufacturers within the equity release market will have to determine the potential impact that distributors may have on the overall value provided to consumers as part of the advised sale of their products and/or services. As part of this assessment, it will be important for manufacturers to consider the impact that advice fees charged by distributors may have on the overall value to the consumer and whether the distribution channels are appropriate to ensure the products and/or services can be distributed to the manufacturers' target market. Likewise, distributors will need sufficient information from the manufacturers to understand the outcome of the value assessment and to enable them to recommend a proposition that is fair value to the consumer. The distributor will also need to assess whether the price the consumer is paying for the advice service is considered reasonable and that the remuneration they receive does not result in the product providing poor value to consumers. The decision to maintain/approve new products on a distribution panel should be guided by the value of the product relative to the specified target market rather than solely by commercial considerations. In order to facilitate this, manufacturers will have to share information from their fair value assessment to enable the distributor to identify the following:

- The benefits the product is intended to provide to a consumer.
- The characteristics, objectives and needs of the target market.
- The interaction between the price paid by the consumer and the extent and quality of any services provided by the distributor.
- Whether the impact that the distribution arrangements (including any remuneration it or (so far as the distributor is aware of it) another person in the distribution chain receives) would result in the product ceasing to provide fair value to consumers.

There is further guidance within Part C in relation to information sharing and how this might work in practice.

Distributor and introducer relationships

There will be some distributors that accept introductions to consumers from introducers who do not provide advice on equity release products such as estate agents and pension advisers. In some instances, there will be a commercial arrangement in place whereby a distributor pays a fee to the introducer for this introduction which may be a fixed or variable amount depending on the loan size. These fees may have a direct influence on the price a consumer pays for the advice and ultimately the product and/or service they purchase and therefore should be included within the distributor fair value assessment. As part of this assessment, distributors should assess the impact that these fees have on their overall pricing structure and whether these fees are commensurate with the level of cost and effort required to provide an introduction.

Fair value assessment methodology

The FCA defines value as the relationship between the overall price the consumer pays and the quality of the product(s) and/or services provided. The requirement under the price and value outcome that this guidance focuses on is the need for firms to complete a fair value assessment which should include an assessment of whether the amount paid for a product is considered reasonable and relative to the benefits the consumers will receive in return. To enable firms to fully assess the product offering in light of the Consumer Duty requirements the below steps have been suggested to assist firms with the formulation of the fair value assessment.

Definition of fair value

Firms need to establish how they will assess fair value within their organisation and use the assessment to validate whether they are achieving this aim. Irrespective of whether a firm is a manufacturer or distributor, they will need to be able to evidence that consumers are receiving fair value from the product and/or service that is being provided. This will require all firms throughout the value chain that are defined as a manufacturer or distributor to commit to assessing the fair value of the products and/or services they are offering. This will include where they are distributed as part of a package and acting where risks are identified to good consumer outcomes. As a result, the firm's processes including remuneration, distribution arrangements and services provided by third parties should be considered.

If there are areas identified as part of this process where it is determined that fair value is not being provided to consumers, firms should take appropriate actions to mitigate, and where appropriate, remediate any harm to existing consumers and prevent harm to new consumers.

Fair value assessment

To assess the fair value of a product and/or service, firms need to build a fair value template which links back to the requirements of the Consumer Duty in relation to the price and value outcome which can be split into the following sections:

- Benefits
- Monetary costs
- Non-monetary costs
- Distribution
- Commercial

Firms will be able to complete their fair value assessment by working through the guidance provided in relation to the dimensions of value which have been mapped to these sections within Part B, appendix 1. There are also key questions highlighted within Part B, appendix 2 which firms will need to consider in relation to these sections.

Fair value dimensions

Firms should consider the key dimensions of value as part of the fair value assessment which can impact on the benefits a consumer receives from a product and/or service, the overall price paid by a consumer and the overall cost to a firm in providing the product and/or service. The suggested dimensions are summarised in the diagram below:

Dimensions of value

Product and consumer base: The characteristics of the product including its purpose, utility and design. The characteristics of the customer base including vulnerability and differential pricing between consumer cohorts.

Price and cost: The price paid by the consumer and the costs associated with manufacturing the product.

Service: The quality of the service consumers receive including non-financial costs.

Distribution: The expected distribution costs of the product or service.

These four dimensions can be used to form the baseline principles of the fair value assessment and will be covered in greater detail in the fair value dimensions section in Part B.

Fair value assessment: Commonality and variance

Firms may offer multiple products and/or services that have significant commonality and products and/or services which vary fundamentally. Where products and/or services are similar when considering the funding model, pricing, intended consumer base, complexity, and risk of consumer harm, firms may group similar products and/or services together provided that the grouping does not impair the firm's ability to assess each product or service adequately. Where there are significant variances however a separate assessment may be necessary. When determining whether it may be appropriate to group products and/or consumers together to avoid creating multiple fair value assessments, the following items could be considered:

- Funding approach
- Revenue, costs and profitability
- Target market
- Features of a product (use cases, benefits, utility, limitations)
- Distribution approach and remuneration arrangements.

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