Final Report

Transparency in professional fees

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Foreword

This report represents the culmination of a year long project looking at transparency in professional fees and commissions in the residential and commercial property sectors. As such, this report should not be seen in isolation but viewed alongside the consultation document (April 2009) and the summary report on the response to the consultation document (October 2009).

To take the work forward RICS established the Transparency Working Group[1] (TWG). The recommendations put forward in this report by the TWG are geared towards building upon the good practice that already exists and moving the issue of transparency forward.

President's introduction

One of the tests of a profession is whether it can raise standards to match or exceed public expectations, especially in the field of consumer protection. Against that background RICS set up the TWG to review concerns raised, particularly in the residential management sector.

The TWG consulted widely on a number of specific issues, but focused particularly on transparency in professional fees: first, by inviting submissions from a range of consultees and, second, by holding a series of stakeholder meetings. The consultation exercise was well received by all interested parties, whether members of the public, business clients, professionals working in the property sector, regulators or government departments.

This final report brings together the recommendations of the TWG. Some will be relatively straightforward to deliver, others will need further work with a range of stakeholders. I am in no doubt that implementation of the recommendations will raise standards and improve consumer protection.

I would like to thank all the consultees and members of the TWG for their contribution and commitment. In turn I know the TWG wishes to express its appreciation to David Pilling, RICS Regulation Policy Project Manager, for his dedicated and comprehensive support throughout its series of meetings and consultations. Special thanks are also due to Teresa Graham CBE, former Chair of RICS' Regulatory Board and Baroness Maggie Jones, Chair of the Surveyors Ombudsman Service Member Board, for so expertly chairing the policymakers' and consumers' stakeholder group meetings.

The current focus on transparency in so many areas of business and public life makes this final report particularly timely. I commend it to those who have an interest in taking forward the recommendations.

Max Crofts

RICS President
February 2010

[1]The members of the TWG are:
RICS Members: Max Crofts, President of RICS, Gerry Fox FRICS and Roger Southam FRICS;
Lay Members: James Purvis (Insurance Consultant) and Keith Richards (ABTA and independent member of RICS Regulatory Board);
RICS Staff: Paul Bagust, Assistant Director of the Commercial Professional Group, David Dalby, Director of the Residential Professional Group and Steven Gould, Director of Regulation.

Transparency - issues, responses and recommendations

Declaration of insurance remuneration and commissions

The consultation paper outlined the current position around disclosure of commission in insurance. Clearly there is evidence of a lack of transparency in the commercial insurance market – though the option taken by the Financial Services Authority (FSA) is to first look at an industry based solution and then review its effectiveness. The FSA has been continuing to monitor how firms have been responding to the five outcomes that it set down for a more competitive and efficient market, which are that consumers should:

1. Have clear and comparable information about the commissions intermediaries earn.
2. Have clear and comparable information about the services intermediaries provide.
3. Have clear information about the capacity in which an intermediary acts.
4. Be alerted to their right to request commission information.
5. Be aware where there is a chain of intermediaries.

The FSA will over 2010/2011 assess whether customers are receiving sufficiently clear and comparable information about their intermediaries' services, capacity and remuneration.

A number of respondents to the consultation were unsure as to why the FSA started by looking at the commercial market, rather than the consumer/retail sector. It seems obvious that if there is customer detriment happening in the commercial sector then there must also be customer detriment in the consumer sector. It appears that the main reason why the FSA looked at the commercial sector and not the consumer/retail sector, was that it considers that products are more standardised in the consumer sector and, therefore, more straightforward.

Industry best practice

British Insurance Brokers' Association (BIBA) Industry guidance

The FSA has agreed that it will initially seek an industry solution in the commercial sector but will be reviewing the position. BIBA has produced industry wide guidance[2], backed by the FSA, which represents an industry solution on transparency, disclosure and conflicts of interest in the commercial insurance market. The guidance outlines the kind of information that should be made available to commercial clients on just how the intermediary is remunerated. However, this is still, clearly, within the framework of an 'on-request' regime[3]. The guidance does go on to say that commercial clients should be made aware of the fact that they can request to know what commission the intermediary is receiving and that, where there is an ongoing relationship that this is brought to the attention of the client on a regular basis; at least once every 12 months.

The BIBA guidance also provides a template document for highlighting to commercial clients how the intermediary is remunerated and also a template document around the services and remit under which the intermediary is operating on behalf of the commercial client.

Association of Insurance and Risk Managers (AIRMIC) guidance

AIRMIC provides separate guidance on transparency, disclosure and conflicts of interest in the commercial insurance market. AIRMIC welcomes the industry guidance that has been approved by BIBA and acknowledges that it represents a step towards clarifying the status of intermediaries and the means in which they are remunerated for their professional services. However, AIRMIC is of the opinion that buyers of commercial insurance will require information in addition to the minimum disclosures set out in the industry guidance. In particular, information on how any potential conflicts of interest that do arise will be managed.

The AIRMIC guidance points out that the standard letters provided with the industry guidance for communicating with customers are not sufficient. The first letter around remuneration simply does not provide sufficient detail. AIRMIC recommends that insurance buyers should seek a more comprehensive account of the source, amount and nature of remuneration available to the insurance intermediary and how this additional income may be generated.

The second letter is concerned with the service provided by insurance intermediaries and the capacity in which they operate. The view of AIRMIC is that an insurance intermediary cannot act in the best interest of both the insurer and the insured at different times during the same insurance contract. This de facto raises the issue of conflicts of interest. Clearly, in such circumstances, the insured will need to decide whether the fact that the intermediary is the agent of the insured and the agent of the insurer at different stages of the insurance cycle is acceptable. If the insured decides to accept this split role, then they will inevitably require more detailed information on how conflicts of interest may arise and how they will be managed.

The AIRMIC guidance then provides a comprehensive checklist that insurance buyers should ask their insurance intermediaries to explain. By asking these questions the insured may recognise the potential for conflicts arising from the range of activities undertaken by the insurance intermediary.

Whilst the move made by AIRMIC is helping to advance transparency in the commercial insurance sector, the fundamental premise is that the customer must request the information, if they do not then there is no obligation of the insurance intermediary to disclose any of the information.

As explained, the FSA has indicated that it will be reviewing just what effect the industry solution has had in the commercial sector during the next year or two. Clearly, the results of this review will dictate whether the FSA takes any further action in the commercial sector.

[2]http://www.biba.org.uk/industryGuidance.aspx

[3]The FSA does not impose mandatory disclosure to clients of commission earned. Instead, it places an 'on-request' regime whereby the client must specifically request to know what commission is being earned before the intermediary is under an obligation to disclose that to the client.

Consumer/retail market

This leaves questions around the consumer/retail insurance market and whether the FSA will take a closer look at whether there is consumer detriment here. A number of responses to the consultation highlighted the lack of awareness when it comes to the options available to consumers. Indeed much of the information required is similar to that set out in the five requirements the FSA wants consumers to have in the commercial market above. Again, it seems axiomatic that if there is consumer detriment in the commercial insurance sector then there will be in the consumer/retail sector given the likely base level of customer knowledge. The consumer/retail market will consist of individuals who must be seen as vulnerable when compared to commercial clients, for example, elderly consumers or consumers buying insurance for the first time. It is certainly worth exploring that in greater detail.

Full disclosure requirements and 'on-request' disclosure requirements

One theme running through the consultation responses and the various stakeholder meetings was that due to a lack of consistency across the sector, it was difficult to obtain a clear picture as to whether a specific service provided or insurance placed was the best option for the client. The lack of consistency was to some extent driven by the different requirements for professionals and intermediaries on declaration of commission to their clients. For firms regulated directly by the FSA the requirement on disclosure of commission to the client is not mandatory, but is via an 'on-request' regime. For firms that are not regulated by the FSA directly, but for example, via a professional organisation's approved Designated Professional Body (DPB) scheme then the requirement is that the firm must disclose the level of commission to the client. The firm must also seek the informed consent that the client is content for the firm to keep the commission.

This difference seems both unnecessary and unhelpful to the public and while it may have arisen as an unintended consequence of the implementation of the Insurance Mediation Directive (IMD), there must surely be questions as to who actually benefits from the current approach. After all, consumers are consumers, whether they are using the services of a firm regulated directly by the FSA or not. If a firm is not regulated directly by the FSA then they will be regulated by a DPB scheme. The FSA and HM Treasury have agreed all DPB schemes and therefore are content with the rules of the schemes and the monitoring requirements by the professional body. Indeed, in this context it is possible that the monitoring requirements of individual DPBs are more comprehensive than the FSA's own monitoring. How are consumers to know this?

It does appear that there may well be a review of the IMD within the European Union (EU) in the future. This will provide an excellent opportunity for the FSA, industry, consumer organisations, professional bodies and other interested parties to feed into that review relevant information about whether consumer protection is being achieved.

Definition of commission and remuneration

A number of respondents did raise the point that there needs to be some clarity around what is meant by commission and remuneration in an insurance setting, since there are many different ways that intermediaries can receive commission and remuneration. It seems wholly appropriate that the client, whether commercial or consumer, should be made aware of what the professional fee is for the service they are paying for. This should include fees, commissions and any other payments received.

It is very helpful that the BIBA guidance around commercial customers does set out a template that shows the various ways that an intermediary can earn commission and/or remuneration. The AIRMIC guidance goes on to include a disclosure checklist that intermediaries should complete. By undertaking this, it is claimed that there is full transparency. This should be seen as best practice, although it must be remembered that this is within the context of the 'on-request' regime.

Recommendations

- **That the appropriate authorities should undertake to review whether there is consumer detriment in the consumer/retail insurance market. Depending on whether there is detriment and its extent those authorities should look to take appropriate action.**
- **That the FSA should be invited to review the current different approaches to disclosure of commission regimes that it operates. This information and lack of consistency should be brought to the attention of the EU.**
- **That there should be greater emphasis placed on making sure clients, especially consumer clients, are made aware of the relevant remuneration, commission and any other payments paid through purchasing insurance.**
- **That regulators should impose requirements to improve transparency in relation to insurance and that they should review the advice provided to clients, especially consumer clients, to ensure it is sufficiently informative and is provided to clients when needed.**

Service charges in leasehold property

Residential

It is clear that transparency lies at the very heart of this issue. Good practice focuses on agents building ongoing and lasting professional working relationships with clients and leaseholders[4]. Each party should be under no illusion about the service that has been agreed, who will provide that service, what the cost will be and who is paid what.

Good practice

A number of responses highlighted that the revised RICS Code of Practice for Service Charge Residential Management was seen as representing good practice in the sector. It is approved by the Department for Communities and Local Government. The Code is followed by RICS members and is supported by other professional bodies and followed by their members, for example, by members of the Association of Residential Managing Agents and others. The Code also has recognised status by courts and tribunals for evidential purposes.

A number of respondents questioned why RICS charges for the Code. The view put forward was that in order to help promote the Code further, and to increase its use and coverage, it should be made freely available. Whilst, the Code was modestly priced at £19.99, the point was made that it wasn't just property professionals that use the Code. It was used by individual leaseholders, the Leasehold Valuation Tribunal (LVT) and potentially ombudsmen and other redress providers and consumer and advice agencies. Whilst there was no objection to RICS covering its costs for producing and printing the Code, it was considered that, at the very least, a free online version should be made available.

In the summary of responses to the transparency in professional fees consultation a number of points were highlighted that amounted to good practice amongst managing agents in providing their services to leaseholders. It is worth outlining those again:

- Agents providing sound advice to their clients and leaseholders.
- Agents taking instructions from clients and implementing those instructions.
- Regularly meeting with clients and building a professional working relationship.
- Agents dealing with all aspects of management, such as the property and accounting.
- Agents setting out clearly what clients and leaseholders can expect and this is fully explained to the clients and leaseholders.

Like most good practice, this list provides a common sense approach.

Retirement accommodation leaseholders

There has been considerable media coverage around the issue of retirement accommodation leaseholders being overcharged for the installation of expensive equipment and insurance charges. It has yet to be proven whether or not this is the case. However, these cases raise two very interesting points. The first is around vulnerable residents, in this particular case residents who are retired and therefore elderly. The second point is around companies within the same group being awarded contracts, for example, to install equipment or arrange insurance. These are emotive issues and demand the utmost transparency and openness in terms of cost and who is paid what. Such information needs to be made as clear as possible and communicated in an appropriate manner.

Reasonableness of fees and commissions and the LVT

Another unsatisfactory situation highlighted during the consultation process is where a lack of transparency in fees charged to leaseholders, makes it difficult for them to assess whether they are reasonable or not. This has a 'knock on' effect if the leaseholder then takes the issue to the LVT. A response to the consultation, from someone who sits on the LVT, highlighted that in many cases allegations of unreasonable fees and commissions were unfounded when all the information was looked at. If the information had been made available to the leaseholder from the start then they may not have decided to go to the LVT. However, the fact they did and then had a decision go against them can only go to damage the relationship between the agent and the leaseholder.

However, a number of responses to the consultation did highlight that there was a good number of decisions from the LVT on reasonableness and those decisions were available for leaseholders to look at as markers. There are, also, organisations, for example, the Leasehold Advisory Service (LEASE) and the Federation of Private Residents' Association that can provide advice to leaseholders. But the difficult decision for leaseholders to take a case to the LVT should not be underestimated. Indeed other responses to the consultation explained that in cases where it may be necessary to obtain expert testimony then the overall case costs can be considerable.

[4]It is perhaps useful when dealing with transparency and openness to distinguish between the relationship between the managing agents and the client (i.e. the freeholder, the landlord or the residents managing company) and the relationship between the managing agent and leaseholders. The client will have the authority to issue instructions to the managing agent and be responsible for such decisions, but leaseholders' views, including those of a Resident's Association, should be considered in a consultative manner.

Consistency in approach

There was considerable discussion both during stakeholder meetings and the written responses around the issue of consistency in approach among managing agents in the marketplace. Whilst many managing agents follow the service charge code and meet the high standards set out by their regulatory body; others are under no such obligations. Any agent or landlord who has not voluntarily signed up to be regulated can effectively operate as they wish, as long as that is within the scope of any relevant legislation. This obviously leads to differences in what is offered in the marketplace.

The view of many of those who commented was that the choice came down to cheap fees as opposed to quality of the service provided including access to free independent redress, i.e. an ombudsman if things did go wrong. Or to put it more simply, the cheapest price does not necessarily provide the best option in the long term. The difficulty identified was just how aware of the differences are clients, leaseholders and others consumers and more to the point how much of an informed choice can they make about which professional service to use?

A number of responses did highlight that there had been a considerable amount of legislation put in place by successive UK governments concerning managing agents. The complication around this was that some of the legislation had been enacted but not all of it, i.e. implementation has been piecemeal. This situation is considered to be unhelpful, not only to clients and the public generally, but to professionals working in the sector, such as agents and solicitors.

What is interesting here is that this part of the residential property sector, i.e. managing agents, is heavily covered by legislation, especially, when compared to the lettings area, but there still remains inconsistency in approach. Whilst, the argument in certain sectors of the residential property market, such as in lettings, is for the introduction of legislation; for managing agents the call is for consolidation of legislation and regulation.

Wider residential policy issues relating to general transparency issues

Although, it was not envisaged that the remit of this project would go wider than transparency of fees and commissions, the responses received and the comments made at stakeholder meetings highlighted that there is a need to look at the residential sector more holistically. Unlike many other areas of professional practice, in certain parts of the residential market there is no transparent “floor” because of a lack of legislation. This leads to a lack of transparency about how particular businesses operate with knock on effects that go beyond fees.

It was considered that to achieve consistency in approach around transparency in fees and commissions, that there needed to be similar basic requirements on all professionals working in the residential sector. Time and time again, the point was made that without consistency in approach, transparency in fees and commissions was difficult to obtain.

The issue of consistency in transparency of fees and commissions brings into play wider points around consistency in standards, regulation and access to consumer redress in the residential property sector. Whilst for some property professionals standards, regulation and providing free redress to consumers when things go wrong are all core to what they do, for others there are no such requirements or guarantees around their activities. Coupled with this is the fact that the residential property landscape is confusing to government, policymakers and professionals and must be a maze to most consumers. The risk of potential consumer detriment, involving some of the most expensive products and services that consumers will have to pay for in their lifetime, must be considerable.

The situation has not been helped by the approaches taken by successive UK governments. Whether the approach has been to safeguard competition in the sector or to try and put in place better regulation; consumer protection has not been greatly enhanced.

There have been a number of recent studies of the sector. All have, in some way or another, covered the transparency of fees issue but have related it to wider structural and regulatory gaps in the sector which clearly assist the lack of transparency. It is worth just looking at some of the more recent initiatives within the residential property sector.

Regulation of letting agents, managing agents and landlords:

There was strong support from the responses received that there should be regulation of all letting agents, managing agents and landlords. This is hardly surprising, given that similar comments have been made via other independent pieces of research and reports, for example, Sir Bryan Carsberg in his Review of Residential Property – Standards, Regulation, Redress and Competition in the 21st Century; the Rugg Review of the private rented sector, carried out by Julie Rugg and David Rhodes of the centre for Housing Policy at the University of York.

Carsberg’s recommendation was that letting agents, managing agents and landlords should be subject to appropriate regulatory requirements in order to achieve consumer protection, efficient markets and cost effectiveness. Whilst Rugg identified six policy directions, which included:

- **Promoting housing management** – the proposal here was for full, mandatory and independently led regulation of letting and managing agents.
- **Light touch licensing with effective redress** – essentially a licensing system for all landlords, where the licensing fee would fund enforcement action against landlords and put in place effective redress for tenants.

UK Government’s response to the Rugg Review

It is encouraging that the UK Government does accept the arguments for full mandatory regulation of letting and managing agents. Indeed, the view that such regulation should be undertaken by an independent body that builds upon the already good work of the industry is reassuring.

The more recent policy statement on 3 February 2010 by the UK Minister for Housing and Planning (Rt. Hon. John Healey) is also welcomed. The Minister outlined that the Government remains committed to legislating at the earliest opportunity to increase the protection for tenants in the private rented sector.

What is slightly curious about the UK Government's response to the Rugg Review is its comments around the regulation or licensing of landlords. The UK Government proposes to establish a national register of landlords. They hold that this is in direct contrast to a licence-based approach. The register would, to all intents and purposes, just be a list of landlords, with no entry requirements to actually get onto the register and no monitoring once on the register. The argument put forward is that the vast majority of landlords are well intentioned and offer a good service to tenants.

What seems odd here is that the register idea is almost a half way house. Either there is consumer detriment by landlords who do not have to comply with mandatory regulation to protect consumers or there isn't; or the detriment is so small as to make it disproportionate to do anything about it. The idea of a register will go to do very little, except, increase costs to the landlord and in turn to the tenants. It will confuse the general public as to its status, many of the public already think letting agents, managing agents and landlords are regulated. The public will have unrealistic expectations around what membership of the register will provide. It is also difficult to envisage how standards will be driven up by merely asking people to belong to a register with no enforcement behind it. It would appear that such a proposal introduces the transparency of entry on a register with no substance behind it.

Office of Fair Trading's (OFT's) Scotland Study

There is also the OFT's market study into property managers in Scotland, published in February 2009. This study found that many consumer clients did not understand their rights and obligations and did not know what service to expect from property managers. In such circumstances, it seems somewhat irrelevant to focus solely on fees.

The OFT made a number of recommendations including the establishment of an effective independent complaints and redress mechanism which is easily accessible to the owners of shared property. Also, that there should be a framework which lays down minimum requirements for best practice so that complaints are assessed against clear standards. It is interesting, and rather reassuring, to note the response to the study by the Scottish Government. Essentially, the Scottish Government is looking to go further than the OFT's recommendations and put in place industry wide self-regulation, backed up with redress and an advice scheme for consumer clients. The OFT wants to see this implemented within a reasonable timescale, if not then it will consider the case for statutory regulation.

Property Standards Board (PSB)

To try and aid consistency across the sector in terms of standards, the PSB has been set up. Initially, put in place by the National Association of Estate Agents, the Association of Residential Letting Agents and RICS; the PSB has consumer and other independent representatives sitting on the Board. A very straightforward option would be for the PSB to be given statutory backing by UK Government. This would then provide the PSB with a remit to approve a range of codes across the sector. Those codes would then have a mandatory requirement. This would certainly improve consistency across the sector and provide certainty for consumers. One such code could, of course, be the RICS Code of Practice for Service Charge Residential Management.

With all this work going on and the potential to raise standards and consumer protection, it is disappointing that the legislative measures introduced into the current year's Parliamentary business did not include any specific provision in relation to letting agents, managing agents and landlords. This does seem to be a missed opportunity.

Recommendations

- **That the appropriate bodies should review the information they provide to consumers and professionals with the aim of ensuring that it is readily available and is either free or appropriately priced.**
- **That letting agents, managing agents and landlords should be subject to appropriate regulatory requirements in order to achieve consumer protection, efficient markets and consistency across the sector.**
- **The proposed approach to regulating property managers in Scotland should be monitored to see how it works in practice.**
- **That any appropriate regulatory framework should involve an independent body, for example, the PSB. That body should hold the agreed code(s) of practice that the industry follows, that regulators should enforce the code and redress providers use the code to deal with complaints.**
- **That the UK Government should look to legislate to provide the PSB with the authority and backing to ensure that all letting agents, managing agents and landlords comply with appropriate regulatory requirements.**
- **That the LVT and other redress mechanisms should look to ensure that between them all consumer complaints can be covered by their scope.**
- **That the UK Government should undertake a review of existing legislation in the residential sector with a view to looking at what works best, what does not work well and any gaps. The aim must be to have a proportionate and coherent legislative framework that provides consistency in approach by professionals and protects consumers.**

Commercial

Of the responses to the consultation that commented on this issue, there was broad agreement that the 2006 Service Charge in Commercial Property: RICS Code of Practice represents good practice in the sector.

The main issues raised were around the coverage, penetration into the market and monitoring of the Code. Certainly, the more widely the Code is used then the more consistency in approach there will be. The problem is the Code is voluntary and as such professionals can only be encouraged to use and follow it.

It was also pointed out that it is still early days for the Code and that RICS plans to update it during 2010. This will provide an opportunity not only to improve on the Code but to also to re-launch it and gather extra publicity to raise awareness of the Code amongst professionals and business clients. RICS will consult fully on updating the Code.

An example of good practice that came out of the responses was where a firm had invested in putting in place an online service tracker so that clients have easy access to information as and when they need it. The same firm then backed this up with quarterly expenditure reviews with their clients. Although this may have cost implications and might not be workable for every firm, it is a good example of improving transparency and maintaining effective working relations with clients.

Recommendations

- **That RICS consults all those with an interest in the 2006 Service Charge in Commercial Property: RICS Code of Practice with a view to updating it.**
- **That RICS works with other appropriate bodies to try and increase the use of the Code.**
- **That the RICS Service Charges in Commercial Property – a guide for occupiers should be promoted to clients by appropriate organisations and professionals.**

Commission on letting renewals

The decision by the High Court in the case of the Office of Fair Trading (OFT) v Foxtons Ltd was outlined in the TWG's summary report on the responses to the consultation. The case involved the Unfair Terms in Consumer Contract Regulations 1999 and the focus was purely on residential letting renewals. Mr Justice Mann in his decision made it very clear, that whilst he thought the particular terms in dispute were unfair, he was not making a ruling that renewal commissions were always unfair.

Reassuringly the test he used relied upon whether the terms are clear, transparent and expressed in plain language. Much of the information and comment can be related straight back to these two points. Mr Justice Mann, thought it intrinsically unfair that a sales commission was payable when a rented property was sold to the tenant, unless it has been specifically and unequivocally agreed by the landlord at the time of instructing the agent to let the property.

However, at the time of writing this final report, the situation is that Foxtons Ltd has been granted an appeal against the High Court decision. This right of appeal comes after the Supreme Court decision that the OFT could not use the Unfair Terms in Consumer Contract Regulations 1999 to decide if bank charges were unfair. In that case it was ruled that overdraft charges were part of the price that customers agreed to pay for the package of services their banks provided, and as such were excluded from the scope of the Regulations.

As the High Court decision in the Foxtons' case is based on the same Regulations, a similar outcome may be likely. A watching brief will be kept on progress of this appeal by all those with an interest. That said, good practice must dictate that consumers should always be made fully aware of the service that is being provided to them, by whom, and what the fees and commission payments are that will be received for providing those services.

Recommendations

- **That all relevant professional bodies and other authorities should bring to the attention of their members the High Court decision in the case the OFT brought against Foxtons Ltd and any future appeal outcomes. They should provide information about what the decision means and what letting agents need to do in order to comply with the ruling.**
- **That professional organisations should consider the scope for providing their members with model terms of reference that they can follow.**
- **That professional and consumer organisations should look at the consumer information they make available and ensure that it is updated in the light of the High Court ruling and any appeal decision.**
- **All agents, in particular residential letting agents, should review their terms to make sure that they are clear and transparent and can be easily understood by all clients, particularly, consumer clients.**

Commission on Home Information Packs (HIPs) and the Energy Performance Certificates (EPCs)

From the information obtained through the consultation, it is clear that HIPs and EPCs are still relatively recent requirements. Many consumers are unclear as to what a HIP or EPC is and why they need one, let alone how they can obtain one and what their options are in doing so. These factors may explain why complaints around HIPs/EPCs are only recently coming to light as sellers discover they were not told that there are a range of ways they can obtain a HIP/EPC.

In May 2009, Channel 4 News ran a report that raised several complaints on this issue. As a result of that programme, the transparency consultation and stakeholder meetings, a number of other complaints have been received. Whilst the complaints did not say that taking a commission for the commissioning of a HIP or EPC by the agent was wrong per se, there were concerns around the seller not being made aware that alternative options were available, i.e. they can shop around if they wish to do so. After all, it may well be that the option put forward by the agent was the speediest and most reliable one open to the seller, but how is the seller to make an informed decision?

A number of responses highlighted that it was not appropriate to expect agents to run through all the options available to sellers in relation to obtaining a HIP or EPC. Whilst, this may be the case, it must be good practice for agents to highlight that, although they can arrange for the service to be put in place, the seller does not have to use that service. Where any commission is likely to be received for obtaining a HIP/EPC then this should be made clear to the seller. If the absolute figure is not known then an approximation or percentage might be more appropriately given.

Another valuable learning point identified when considering this issue is that where new requirements are introduced, there is an inevitable time lag between the product being used and professional and consumer knowledge about it. Where this is the case, it seems there should be significant emphasis to raise awareness as much as possible and requirements on all involved to be open and transparent in that process.

Whether HIPs continue to be part of the property selling and buying process remains to be seen, but we have to go forward on the basis that they will be. It may be that as time goes on and sellers become more aware of the product, that they do start to exercise informed choice. On the other hand as most people are infrequently involved in the selling and buying of a property then that will take considerable time to work through. This issue is also part of the OFT's homebuying and selling study that is due to be published during 2010.

There is no consistency in approach across the sector when it comes to receiving commission for HIPs/EPCs. Indeed, there seems to be great disparity ranging from some agents not accepting commission to some claims that commission could be as high as £200. Though a specific example of an agent receiving £200 was not provided there was a case study that showed that the commission taken by the agent was £100 for referral to a firm of solicitors to undertake a HIP/EPC. From the information provided it seems that the agents in question did not inform the sellers that they would receive a commission if the sellers used the particular firm of solicitors suggested. Indeed, it only came to light that a commission of £100 was paid to the agent once the firm of solicitors wrote to the sellers.

This example goes to highlight the very problem when there is a lack of transparency. It may well have been the case that the agent in question has built good working relations with the firm of solicitors and knew that their service is very reliable and timely and therefore probably represents the sellers' best option. The fact that the commission payment only became apparent after the agreement had been reached and made available by the third party – the solicitors – will certainly cast doubt around the professionalism and integrity of the agent.

The key to avoid this must be that agents are open and transparent with their clients. There is nothing wrong with earning a commission when ensuring that, on behalf of a client, an agent is organising a HIP that will be done properly and on time. The agent will be adding value to the service they are providing to the client.

Recommendations

- **Appropriate bodies, such as government departments and agencies, regulators, professional bodies, consumer organisations and others with an interest in this area should ensure that the advice they provide to consumers on this issue is up to date and clear. Also, that it is provided at the appropriate time when the consumer needs it most.**
- **When new requirements are introduced within the property sector, by statute, the relevant government department or agency responsible for implementing that legislation should provide clear guidance to those who might be affected. This includes consumers, professionals and other interested parties.**
- **Good practice suggests that agents should make clear to the consumer that there are a number of ways that they can commission a HIP and EPC and that the consumer might wish to look into those.**
- **That any fees quoted to consumers should be open and transparent and that includes whether or not the firm in question receives a commission. Ideally the level of commission should be disclosed.**

Valuation fees

As outlined in the consultation paper, there is a long-running debate in the residential sector about both valuation fees and fees charged for the arrangement of valuations for consumers. Sir Bryan Carsberg, in his Review of Residential Property Standards, Regulation, Redress and Competition in the 21st Century highlighted the mortgage applicant may be paying £400 to the mortgage lender for a valuation when the cost to the lender is £140. Sir Bryan was clearly of the opinion that this kind of charging was excessive and recommended that action should be taken by the appropriate authorities to ensure that lenders fairly describe fees for mortgage applicants and for valuations. That was in June 2008.

It is important to review just what is happening around this issue. A recent article by Which? in December 2009 commented that '…when you [the mortgage applicant] try and take out a mortgage you have to get a valuation, which enables the mortgage lender to make sure that the property you are buying is worth the money. Even though the valuation is for the lender's benefit, you have to pay for the valuation.' This must be a difficult concept for mortgage applicants to fully understand. Instinctively, they will view the valuation as theirs, after all they have paid for it, and therefore, the valuation is there to protect them. So it is important that mortgage applicants are made aware of the actual position from the start of the process.

There is then the issue around the true cost of the valuation. Put simply, does the mortgage applicant know what they are paying for and who gets what? It seems that the answer to that has to be sometimes, but not always. The Which? report highlighted that the variation in administrative fees charged by mortgage lenders can be dramatic. The report suggests that such variance is difficult to equate with true costs.

This inconsistency across the sector is surprising given the recommendation made by the Monopolies and Mergers Commission in 1994 that lenders should clearly specify the administrative charge they make and what the fee is that is paid to the valuer.

Unfortunately the FSA's Key Facts Illustration only suggest that valuation fees are included in the information provided to mortgage applicants as part of the mortgage related fees. It does not require them to be. As a result, it certainly does not require the breakdown of the valuation fee into administrative costs and the cost of actually carrying out the valuation.

It is interesting to note that in May 2005, the FSA made a statement about working with the industry (mortgage firms) to improve the quality of their key facts documents. The FSA, in that statement highlighted that key facts documents are important as they are intended to deliver clear, simple and user-friendly information to consumers.

Unfortunately, there has been no real change in the approach to the explanation of valuation fees. Recently, the FSA issued a discussion paper entitled Mortgage Market Review. That paper invited comments around unfair charging practice and price regulation and collecting better data from mortgage lenders, such as arrangement fees. Taken together with the work the FSA is doing around transparency as a regulatory tool, and its treat customers fairly regime, this would seem like an ideal time for the FSA to look to provide certainty, clarity and transparency in fees paid by mortgage applicants.

Since the start of the TWG's consultation, the banking sector both in the UK and globally has changed considerably in terms of governments' intervention. In the UK, this has been done in two main ways: first to shore up the financial sector and secondly, the Government has become a significant shareholder of a number of banks and building societies. The focus is on sensible lending, proper management of risk and the change of emphasis from profit at all cost to banking with a more social conscience. If ever there was a right time to look at ensuring consumers are treated fairly, given appropriate information about services and costs, to enable them to make an informed choice, then it is now.

Recommendations

- **That RICS works with relevant authorities to ensure that there is greater transparency and clarity in the description of mortgage and valuation fees for mortgage applicants.**
- **That RICS shares with the FSA the main findings on the valuation fees issue that have come out of this project.**
- **That the appropriate authorities look at the current information, help and advice that they provide to consumers [mortgage applicants], and consider whether the issue of valuation fees is clearly and appropriately explained, easily accessed and available to the consumer when they need them the most.**
- **That best practice suggests that fees and commissions that are charged by the various agencies involved in the process are appropriate and reflect the added value provided by those parties.**

The agreement of fees for commercial loan security valuations

The issue here involves the mortgage lender allowing its customer to agree the valuer's fee and sometimes the method of fee payment. This can lead to questions being raised as to what exactly the relationship is between the valuer and the lender's customer.

The information provided through the consultation does highlight that this scenario is not standard practice. It is much more common practice for lenders to take responsibility for agreeing the valuer's terms of engagement. Indeed, good practice would include lenders obtaining a number of quotes, say three, from valuers, and then deciding which valuer they will use and for what fee. Where this situation arises then it appears to provide the appropriate level of transparency and independence needed by all parties to ensure that there can be no accusations levied at the valuer of undue influence by the borrower.

Recommendation

- **That RICS' relevant Professional Group should work with others, in particular with lenders, regulators and relevant professional bodies, to look at developing and implementing an industry wide protocol to be followed in this area.**

Dilapidations

As part of the consultation exercise there was a general invitation to respondents to identify any other issues around transparency in fees and commissions. One respondent did raise an issue in relation to the professional practices within the field of dilapidations.

The issue relates to the RICS Dilapidations Guidance Note and questions whether that note provides adequate or appropriate guidance in relation to a number of areas. The points raised included things like:

- The expert status and role of surveyors preparing admissible claim/defence documents.
- The conflict of interest posed by performance related incentivised contingency fees.
- The need for informed consent for an appointment where the fee terms are anything other than on a time-resource basis.

RICS' Dilapidations Working Group considers that the points raised are covered by the Guidance Note and/or by additional guidance provided by RICS. Despite this, RICS has taken seriously the concerns expressed and following the issue being discussed by the TWG it has been agreed that RICS will seek expert independent legal advice on the points made.

Recommendation

- **That RICS seeks independent legal advice around the suitability and coverage of its guidance note on dilapidations.**

General comments on commissions

The consultation exercise also highlighted a number of general comments on commission payments. The responses were interesting. There was clear acceptance that commissions should be earned, represent remuneration for work done, or involve some added value to the service provided to the consumer. Despite a number of responses highlighting that interpretation of 'earned' may well vary from agent to agent or firm to firm, there may well be mileage in putting down some guiding principles that agents should at least consider before taking commission.

It is also clear that where commission is earned and taken then this should be transparent to the consumer or in effect the person paying for the service, i.e. the end user. It is also quite clear that the concerns expressed were around the quality of information provided and whether it gave the consumer an accurate picture of what was happening. This was seen as particularly important when it came to commission going to companies within the same group, or in the example of valuation fees, where the cost the mortgage applicant pays to the lender for the valuation is made clear, but the breakdown of the actual fee charged by the surveyor or the arrangement fees is not.

Again, there were strong calls for consistency across the sector. The view was that if some agents acted professionally and were transparent in terms of the commissions they received but other agents were not, then how can consumers be expected to make a quick decision based on price let alone an informed decision. As highlighted under the issue of service charges in residential property issue, to obtain consistency in transparency of fees and commissions will need investment from the UK Government in terms of legislation.

Put simply, best practice would dictate that there should be transparency around the service that firms are providing to their clients and this should make it clear what the scope of the service is that they are offering, the charges they make and the circumstances under which they become chargeable and what other payments the agents receives and from whom. This information should include the existence of any connected businesses, reciprocal relationships and introductory commission agreements, together with reference to alternatives available.

The goal must be to have well informed consumers who are able to assess for themselves the relative value and quality of the services offered. This may mean that the consumer opts for the lowest cost but not necessarily, they may well prefer the security of a professional service.

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