

# PARLIAMENTARY DEBATES

HOUSE OF COMMONS  
OFFICIAL REPORT

First Delegated Legislation Committee

## DRAFT FINANCIAL SERVICES AND MARKETS ACT 2000 (REGULATED ACTIVITIES) (AMENDMENT) ORDER 2016

*Monday 7 March 2016*

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**not later than**

**Friday 11 March 2016**

STRICT ADHERENCE TO THIS ARRANGEMENT WILL GREATLY  
FACILITATE THE PROMPT PUBLICATION OF  
THE BOUND VOLUMES OF PROCEEDINGS  
IN GENERAL COMMITTEES

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**The Committee consisted of the following Members:**

*Chair:* Ms KAREN BUCK

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|---|--|
| † Baldwin, Harriett ( <i>Economic Secretary to the Treasury</i> ) | † Knight, Julian ( <i>Solihull</i> ) (Con)                           |
| † Bruce, Fiona ( <i>Congleton</i> ) (Con)                         | † McGinn, Conor ( <i>St Helens North</i> ) (Lab)                     |
| † Burgon, Richard ( <i>Leeds East</i> ) (Lab)                     | McKinnell, Catherine ( <i>Newcastle upon Tyne North</i> ) (Lab)      |
| † Burns, Conor ( <i>Bournemouth West</i> ) (Con)                  | † Mak, Mr Alan ( <i>Havant</i> ) (Con)                               |
| † Cartlidge, James ( <i>South Suffolk</i> ) (Con)                 | † Spellar, Mr John ( <i>Warley</i> ) (Lab)                           |
| † Cooper, Julie ( <i>Burnley</i> ) (Lab)                          | † Stride, Mel ( <i>Lord Commissioner of Her Majesty's Treasury</i> ) |
| † Fysh, Marcus ( <i>Yeovil</i> ) (Con)                            | Thomas, Mr Gareth ( <i>Harrow West</i> ) (Lab/Co-op)                 |
| † Hollinrake, Kevin ( <i>Thirsk and Malton</i> ) (Con)            | Jonathan Whiffing, <i>Committee Clerk</i>                            |
| † Jenkin, Mr Bernard ( <i>Harwich and North Essex</i> ) (Con)     |  |
| † Kerevan, George ( <i>East Lothian</i> ) (SNP)                   | † <b>attended the Committee</b>                                      |

# First Delegated Legislation Committee

Monday 7 March 2016

[MS KAREN BUCK *in the Chair*]

## Draft Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) Order 2016

6 pm

**The Economic Secretary to the Treasury (Harriett Baldwin):**

I beg to move,

That the Committee has considered the draft Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) Order 2016.

It is a pleasure to be here under your chairmanship this evening, Ms Buck. The draft order makes changes to the respective regulatory frameworks for mortgage and peer-to-peer lending. I will talk about the provisions on the regulatory framework for mortgages first.

In March 2015, Parliament approved the Mortgage Credit Directive Order 2015, which ensures that the UK implements the EU mortgage credit directive on time and with a limited impact on the UK mortgage market. The order is due to come into effect on 21 March this year. Since that order was made, the Government have been monitoring the progress of the mortgage industry towards implementation. In that ongoing monitoring, it came to light that in some areas the order did not achieve what was intended, or could be improved on. The Government acted quickly and laid a statutory instrument, which was made in November 2015. It made a small number of amendments to the scope of regulation, to ensure that the regulatory framework continued to operate as intended.

Today's draft order makes further changes designed to ensure that the legislation delivers on previously agreed policy. It clarifies the regulatory status of a number of categories of loan entered into before April 2014. Specifically, it clarifies that the regulatory status of the loans depends on their regulatory status under the consumer credit regime before the transfer of regulatory oversight to the Financial Conduct Authority.

Since the transfer of the consumer credit regime from the Office of Fair Trading to the FCA in 2014, much of the industry has assumed that the legislation applied the principle of "once regulated, always regulated" to loans entered into before April 2014. That is a different test from the one generally applied under the FCA regulatory regime, where regulation is applied to ongoing activities with the regulatory status of those activities changing over time. Following engagement with the industry and the FCA, we have been made aware of the ambiguity about which test now applies to loans entered into before April 2014. There is also ambiguity about the loans that are to be moved across to the mortgages regime when the mortgage credit directive comes into force on 21 March. The draft order removes that ambiguity.

Providing clarity as to the regulatory status of the loans will also ensure that the holders of the loans are able to assess accurately what regulatory permissions

they require. Furthermore, it will ensure the continuation of consumer protections, preventing consumers from inadvertently losing regulatory protections that they had at the point they took out a loan.

In 2014, the Government removed English and Scottish housing associations' new second-charge mortgage lending from the scope of conduct regulation. The draft order also exempts second-charge mortgage loans made from April 2014 by Northern Irish and Welsh housing associations.

The peer-to-peer lending-related amendments in the draft order extend the scope of the regulated activities relating to the operation of peer-to-peer lending platforms and providing advice on lending through such platforms. In changes to the provision of advice on peer-to-peer loans, the Government are committed to supporting savers and to increasing the choice available to ISA savers. To support that aim, the Government announced at Budget 2014 that loans made through peer-to-peer platforms will become ISA-qualifying investments. From 6 April repayments of interest and capital made to lenders on new peer-to-peer loans will qualify for tax advantages where such loans are held in a new type of ISA, the innovative finance ISA. The Government anticipate that that could significantly increase the provision of advice to investors on peer-to-peer lending.

The draft order aligns the treatment of advice on peer-to-peer loans with advice on other ISA-qualifying investments by making the provision of advice to lenders on entering into a peer-to-peer loan a regulated activity. The consultation on the changes identified broad, industry-wide support for that change, which will ensure that the FCA is able to make rules to ensure that firms providing advice to investors on peer-to-peer loans act properly and in the best interests of their customers. That will mitigate the risk of unregulated firms setting up and acting improperly in providing advice to consumers.

The draft order also extends the scope of the peer-to-peer regulation to ensure that all the relevant activities are included within this framework. In particular, it brings the activity of facilitating the transfer of rights under a peer-to-peer loan between lenders on a secondary market within scope of article 36H regulated activity. That will mean that a peer-to-peer loan brought on the secondary market is subject to the same regulatory framework as new loans originated by peer-to-peer platforms.

The draft order also clarifies the definition of an article 36H agreement, or peer-to-peer loan. The change clarifies that if the peer-to-peer platform is the lender or borrower on its own platform, the agreement is not a peer-to-peer loan. That ensures that peer-to-peer lending remains exactly that—peer to peer. These amendments are an example of the Government's proportionate and flexible regime in action, providing the space for peer-to-peer platforms to grow and providing competition to the major banks, while maintaining the right level of protection for consumers.

Finally, the draft order makes a minor amendment to the Small and Medium Sized Business (Finance Platforms) Regulations 2015, which set out the circumstances in which designated banks must refer unsuccessful SMEs that have applied for finance to online platforms, to assist in finding other sources of finance. The amendment clarifies that when a small business is already using a broker to seek finance on its behalf, unsuccessful applications by that broker do not need to be referred to finance platforms.

Taken together, the changes in the draft order are another important step to ensuring that the UK's financial system is competitive, resilient and works for the good of the country. I hope that hon. Members will therefore support the order.

6.7 pm

**Richard Burgon** (Leeds East) (Lab): It is a real pleasure to serve under your chairmanship this evening, Ms Buck, and it is always a pleasure to serve opposite the Minister. As she says, the draft order amends provisions in the Financial Services and Markets Act. The House of Commons Library tells me this is the 34th order amending that Act. The draft order is about the regulation of a number of activities, including peer-to-peer lending and mortgage lending.

On peer-to-peer lending, we are aware that the innovative finance ISA will launch next month, following the Treasury consultation at the end of 2014 and the policy announcement in last summer's Budget. Peer-to-peer lending is already a fast-growing sector of our financial services industry and the Government anticipate that the launch of the new ISA could significantly increase the number of individuals making use of the sector.

There is ongoing debate about the merits and potential pitfalls of peer-to-peer lending, about the significant returns that can be made on loans in an age of low interest rates and about the risks to lenders. The proposal to make the provision of advice to lenders on entering into a peer-to-peer loan a regulated activity appears to be entirely sensible, although, as ever, we have a number of questions.

First, I note that the Yorkshire Building Society has estimated that over 400,000 savers are expected to invest in this field, but there are questions about the readiness of the financial advice sector to advise on the new products. The Treasury consultation found that the majority of existing ISA managers said that they were not currently considering offering peer-to-peer loans within ISAs. The "Alternative Finance" report produced by Intelligent Partnership found that of 130 advisers, just 9% expect the peer-to-peer sector to form part of their advice process in the next 12 months.

The Association of Professional Financial Advisers' response to the Treasury consultation states:

"We believe that this is a very nascent industry and that until it has an established track record, it should not be considered a mainstream investment for retail clients. We therefore welcome the fact that firms, holding themselves out as independent financial advisers, will not be required to consider investment in P2P agreements when making personal recommendations to clients."

The FCA has since said in its consultation document on changes to its handbook that

"we are not proposing that firms holding themselves out as independent should be obliged to consider P2P agreements when recommending retail investment products to a retail client."

It says that the sector is

"at an early stage of development".

With that in mind, will the Minister set out why advice about the peer-to-peer ISA is being treated in such a way? Will there be a future review about a change of approach? When might one be carried out?

In addition to our questions about advisers' requirements and their awareness of the products, we have general questions about the timing of the launch and ongoing

developments in regulating the peer-to-peer sector. Adair Turner, the former Governor of the Bank of England, who raised concerns in interview on the "Today" programme, is the most prominent individual to do so in recent weeks. There has also been significant coverage of the collapse of the unregulated Swedish peer-to-peer firm TrustBuddy. I am aware that peer-to-peer lending firms have issued robust responses in their defence. In particular, Christine Farnish of the Peer-to-Peer Finance Association did so in the media and when I met her recently.

Sue Lewis from the Financial Services Consumer Panel was among a number of people who responded to the Treasury's consultation. She said that investors must be aware of the risk:

"It is important that anyone considering saving in a peer-to-peer ISA understands the risks associated with it, and they should be covered by appropriate levels of protection."

She flagged up the FCA's intention to consider whether the remit of the financial services compensation scheme should be expanded to include peer-to-peer lending in 2016. The Treasury's summary of the responses to the consultation said that a minority of respondents made the case for its inclusion. Will the Minister clarify the Government's opinion of covering peer-to-peer investments with the financial services compensation scheme? When will the FCA carry out that review? Would it have been sensible to have concluded such a process before the launch of the innovative finance ISA?

This is the second order on the implementation of the mortgage credit directive, which will come into force this month. The first was debated in Committee in March 2015, before the general election. The explanatory memorandum to that order says that the UK is already in advance of many European countries in adopting the directive. The European Mortgage Federation stated that the UK's mortgage market review already goes beyond the core provisions of the directive. The Council of Mortgage Lenders stated that UK lenders are ahead of most of their European counterparts in implementing the directive. UK firms have been given the opportunity to adopt the revised rules up to six months early. Many have chosen that option, and are therefore already complying with the directive's requirements.

On the second-charge lending market becoming regulated by the FCA and subject to its mortgage rules, in 2014 the Financial Services Consumer Panel said that it is "odd" that that is not already the case, given that

"the second charge market has consistently suffered from a higher rate of repossessions than first charge mortgages."

The panel said it was concerned that there is a regulatory gap between the consultation date and the directive's implementation date this month, and that the FCA will not collect performance or sales data on second-charge mortgages. Will the Minister comment on the effect of that gap? Has the Department since responded to those concerns?

Furthermore, the directive distinguishes between business buy-to-lets and consumer buy-to-lets, which are classified as such if the borrower or an immediate relative of theirs has ever lived in the property or intends to live in it in the future. How does the Minister expect that to be implemented? How many mortgages does she expect will be affected in that way, and is there any possibility

[Richard Burgon]

of misidentification or misallocation of the distinctions between consumer and business buy-to-let? What are the risks of that occurring?

Finally, on small-firm lending, the order will exempt from referral to finance platforms applications made by a broker instead of directly by a business. What impact might that have on small and medium-sized enterprises' access to finance, given the ongoing concerns, of which we are all aware, about bank lending to small businesses, which we know are vital for innovation in our economy? I have no doubt that we could discuss the development of alternative finance, the mortgage markets and small-business lending at further length, but I will draw my comments to a close.

6.15 pm

**Harriett Baldwin:** I note that the shadow Minister started with the second section, on peer-to-peer ISAs. I was not clear from his remarks whether he welcomes the development of peer-to-peer lending in this country and the introduction of the innovative finance ISA, but it is worth stressing how important the Government believe this area of lending is to consumers and small and medium-sized businesses. It offers them a potential alternative source of funding locally. I am sure he shares my aspiration for a competitive and diverse range of funding to be available to growing companies in this country.

If I may, I will plug my own local peer-to-peer lending platform in Worcestershire. It is called ThinCats.com—the antithesis of the fat cats in the banking industry that so aggravate the hon. Gentleman occasionally. He is right that this is a nascent market. We are expecting that, as of the date in April when it becomes possible to invest in an innovative finance ISA, there will be seven firms available in which consumers can invest their ISA allowance, and that is on top of the range of different peer-to-peer lending platforms already growing in this country.

The hon. Gentleman asked about the perimeter of regulation in terms of peer-to-peer lending, the Financial Services Compensation Scheme and whether we ought to consider guaranteeing the first £75,000 invested in peer-to-peer platforms, just as the FSCS guarantees the first £75,000 put in a bank. We think it is important that the peer-to-peer lending industry falls within the perimeter of regulation. That is much better for consumers and for the long-term success of the industry, but the extent of the regulation is fairly light, in the sense that if people invest in such platforms, they can lose the amount that they invest. Obviously, most platforms will compete on diversification of investments, the allocation that

they hold back to withstand losses and so on, and on making that transparent to consumers, but it is definitely an alternative source of funding in an innovative area where the market is developing a range of solutions.

I gently correct the hon. Gentleman: Adair Turner is not the former Governor of the Bank of England; he was the chairman of the Financial Services Authority. He was right to highlight to consumers that this is a different kind of investment from investments in a bank, which are guaranteed up to £75,000—that is why the returns are higher—but to pour scorn on it and deter informed investors from investing in such platforms would be wrong. Obviously, we have worked closely with Christine Farnish, whom the hon. Gentleman mentioned, and the peer-to-peer industry on supporting the aspiration for the industry to be regulated and for consumers to be given clear information when they make such investments.

The hon. Gentleman also asked questions about the mortgage credit directive, along with a question about when second-charge mortgages will come into regulation, asking, “If not, why not?” As he will understand, it has been pretty clear for some time that the European mortgage credit directive will include second-charge mortgages, so it makes sense to wait for that regulation to come into force to include second-charge mortgages, which is why there has been a timing difference in bringing the regulation of second-charge mortgages into line with that for first-charge mortgages. We did not want to disrupt firms and customers excessively by predated regulations that are clearly on their way.

The hon. Gentleman asked about the treatment of advice and whether it will be subject to a future review—that was with reference to peer-to-peer regulations. Of course, we will continue to keep that under review in the light of developments. He asked about the risk of misidentification of consumers or businesses in the buy-to-let regulations, and it will be for lenders and brokers to identify the type of lending. That means that lenders and brokers will need a system in place to collect the relevant information from the borrower but, with the main implementing order having been in place for a year, they will have had time to do so, which is the benefit of our publishing the regulations last March and being able to work with the industry during the transition period to ensure that, by the time we get to implementation day on 21 March, all the questions that the hon. Gentleman rightly asked today have been answered.

I trust that answers all the hon. Gentleman's questions. I commend the draft order to the Committee.

*Question put and agreed to.*

6.22 pm

*Committee rose.*



