

February 2015

FCA Consultation: Buy-to-Let Mortgages: the Mortgage Credit Directive Order 2015

Following the passing of the EU Mortgage Credit Directive in February, the FCA is now in the advanced stages of implementing this into the UK. It has recently issued a consultation on how it will approach the most complex aspect of the Directive: how it will oversee Buy-to-Let Mortgages: <http://www.fca.org.uk/news/cp15-03-buy-to-let-mortgages>

- The government's legislation uses an exemption in the MCD that allows the UK to not have to apply the Directive to buy-to-let activity provided it has an appropriate framework for regulating these mortgages.
- The government intends to use this exemption through the establishment of an appropriate framework set out in legislation.
- Having consulted on the detail of its appropriate framework, the government published its summary of responses and the legislation on 26 January 2015, and is now taking forward implementation, particularly how the FCA will manage its powers in relation to Consumer Buy-to-Let (CBTL) activity.

Next steps: the consultation closes on 19 March 2015. It will then publish a policy statement in June 2015 to allow the industry enough time before the rules come into force in March 2016.

Background: regulating the buy-to-let sector

The European Directive on credit agreements for consumers relating to residential immovable property -- commonly known as the "Mortgage Credit Directive" (MCD) -- was passed in February 2014 and must be implemented across the EU by 21 March 2016. In the UK, the Treasury and FCA consulted in September on enacting the MCD's provisions, and set out some proposed legislative changes to enable the effective implementation of the MCD.

Currently the FCA mortgage regulation covers lending related to properties which are at least 40% occupied, or intended to be occupied, by the borrower or a relative. This means that the vast majority of buy-to-let mortgages are unregulated.

The European directive imposes some requirements on member states for buy-to-let mortgage activity. In keeping with the UK Government's active decision not to regulate the entire buy-to-let market, it has sought to put in place a regime that satisfies the minimum requirements to meet the UK's legal obligations. This regime isolates creates a sub-category of buy-to-let called Consumer Buy-to-Let (CBTL), undertaken by individuals as an activity outside their main area of business. The legislation sets out a series of circumstances which would constitute a buy-to-let customer acting by way of business:

a buy-to-let credit agreement which is not entered into by the borrower wholly or predominantly for the purposes of a business carried on, or intended to be carried on, by him.

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The FCA's approach to implementing the UK legislation

Having consulted on the detail of its appropriate framework, the government published its summary of responses and the legislation on 26 January 2015, and is now taking forward implementation, particularly how the FCA will manage its powers in relation to Consumer Buy-to-Let (CBTL) activity:

- The registration processes that firms, with or without existing FCA permissions, will need to follow to register with us as CBTL firm;
- Aggregated data reporting from CBTL lenders to support our risk-based approach to supervision and inform our understanding of CBTL activity;
- Complaints handling rules to support the government's widening of the Financial Ombudsman Service's (the ombudsman service) compulsory jurisdiction to capture CBTL firms; and
- Modifications to other Handbook modules to incorporate CBTL, including changes the Supervision Manual (SUP), Enforcement Guidance (EG), Decision Procedures and Penalties Manual (DEPP), Perimeter Guidance (PERG), and the Glossary.

Registration

From 21 March 2016, firms engaged in lending, intermediating, administering, arranging or advising in relation to Consumer Buy-to-Let must be registered by the FCA.

The government has established a series of conditions that firms must satisfy in order to become registered. These conditions are more prescriptive where a firm:

- is not already FCA authorised
- does not hold an interim permission or
- has otherwise had its CBTL registration revoked

The FCA will therefore tailoring their registration processes to account for these different situations. Analysis of the buy-to-let market suggests that the vast majority of firms that conduct CBTL activity will already hold either an FCA permission to carry out regulated activities (such as entering into, advising on or arranging home finance activity) and/or an interim permission for consumer credit.

Fees

Fee amounts will be determined in the March 2015 fees consultation but are currently not anticipated to be more than £100 for CBTL firms and £500 for other firms.

Once a better idea of the number of CBTL firms is understood, the FCA will revise its fee process. While an activity-based calculation is not anticipated, a flat fee is being considered – one for lenders and one for intermediaries. This proposal is likely to form part of the March 2016 fees consultation and amounts are not expected to exceed £500 for lenders and £250 for intermediaries.

Complaints & redress

The Government will bring CBTL firms into the Ombudsman's formal compulsory jurisdiction. Presently the FOS "can consider complaints against authorised mortgage lenders relating to buy-to-let mortgages and authorised buy-to-let credit brokers", but this is under the voluntary jurisdiction.

Once a complaint is considered by the ombudsman service, it is proposed that CBTL firms are subject to the same case fee arrangements that apply to other firms in the compulsory jurisdiction. Firms would therefore not pay a case fee for the first 25 cases referred to the ombudsman service each year, with each case after that attracting a case fee, currently £550.

The new rules provide that the ombudsman service can recommend that a firm should pay redress, and the FCA will be able to act against a firm that refuses to do so.

The FCA propose to apply the majority of our complaints handling rules to firms' CBTL activity. These rules, which are set out in the Dispute Resolution section of the FCA Handbook (DISP), cover a range of issues including complaints handling procedures and controls, timeframes for resolving complaints, the requirement for final response letters and how the regulator expects firms to cooperate with the ombudsman service. The vast majority of CBTL firms are expected to already hold FCA permissions that bring them into scope of the CJ for those activities, they should already be familiar with the complaints handling rules.

Supervision

The legislation requires that the FCA supervise firms' CBTL activity and that firms cooperate. The conduct standards which firms will be expected to follow are set out in the government's legislation and are based largely on MCD Articles. The FCA will be refining its supervisory approach from March 2016, but broadly it will apply the standard risk-based approach.

They propose collecting data to help understand more about the effects of the distinction in the BTL market created by legislation, the volumes of CBTL business and any supervisory issues at an early stage. At this stage, some amendments to the FCA Handbook to effect the regulator's new supervisory powers in this area, including a CBTL appointed representatives regime for CBTL arrangers and advisers (not CBTL lenders) that works in a similar way to our current process for regulated activities.

Enforcement

The legislation also affords the FCA powers to take enforcement action against firms when necessary. Providing a credible deterrence is at the heart of the FCA's approach to enforcement. Proposed changes are made to the Enforcement Guidance describing how the regulator could take enforcement action against CBTL firms in line with existing FCA processes. They also propose changes to DEPP, which describes the FCA's decision-making procedures relating to statutory notices¹⁰, financial penalties, or suspension.

Next steps

The consultation closes on 19 March 2015. This is shorter than the usual three-month period as the consultation concerns the operational Handbook changes to implement the CBTL regime in line with the powers and limitations the regulator has under the legislation, rather than detailed policy proposals. The FCA will then publish a policy statement in June 2015 to allow the industry enough time before the rules come into force in March 2016.

Laurence Baxter
CII Group Policy & Public Affairs
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