MORTGAGE AND CREDIT UPDATE

The Mortgage Credit Directive

On 21st March 2016, the Mortgage Credit Directive was implemented into English law, introducing a single regulatory regime for mortgages and secured lending.

Prior to the implementation of the Directive, lending secured by a first charge legal mortgage was subject to regulation under the Financial Services & Markets Act 2000 (the "**FSMA**"). Lending secured by a second or subsequent charge was separately regulated under the consumer credit regulatory regime, including the provisions of the Consumer Credit Act 1974, (the "**CCA**").

Significantly, all lending secured by a mortgage or charge over residential property now falls to be regulated under the FSMA regulated mortgage regime, which has absorbed the secured lending regime under the CCA. With effect from 21st March 2016, secured loans which were previously CCA – regulated agreements are now treated as 'regulated mortgage contracts'.

In this context it is important not to overlook the fact that for the purposes of the Financial Services & Markets Act 2000 (Regulated Activities) Order 2001, (the "**RAO**") it is regulated activity not only to enter into a regulated mortgage contract as lender, but also to administer a regulated mortgage contract. 'Administer' essentially refers to activities relating to the post contractual administration and enforcement of a regulated mortgage contract.

This means that with regard to existing CCA regulated secured loans entered into prior to March 2016, a person who wishes to administer and enforce that existing secured loan will need to check whether or not they carry on the regulated activity of administering a regulated mortgage contract and whether or not they need to be authorised and regulated by the Financial Conduct Authority, ("**FCA**"). This is the case even if, at the time the secured loan was entered into, the person held the requisite consumer credit permissions.

In contrast to the position prior to implementation of the Directive, the definition of 'regulated mortgage contract' now covers first, second and subsequent charges over residential property and captures both legal and equitable mortgages and charges. Further, a loan secured by a charge over residential property can be made available for any purpose and still qualify as a regulated mortgage contract.

Whilst mainstream firms providing mortgages and secured loans should be equipped to cope with the changes, the definition of regulated mortgage contract is sufficiently wide to mean that a person who takes a mortgage or charge over residential property as security for a debt owed to them will now need to consider whether or not they undertake the regulated activity of entering into a regulated mortgage contract.

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There are exemptions and exclusions which operate to carve out certain contracts and certain activities from the regulated mortgage regime. For example, special rules apply to secured bridging loans and certain exemptions apply to loans made available to commercial borrowers. Notably, consumer 'buy to let' mortgage lending is subject to a special 'light touch' regulatory regime provided that certain conditions are fulfilled.

However, it is vital to note that some exemptions under the RAO which operate to exempt the activities of persons such as professional firms, trustees and personal representatives from the regulatory regime are 'switched off' in respect of regulated mortgage activity within the scope of the Directive and so those exemptions will not be available in respect of regulated mortgage contracts within the scope of the Directive.

In summary, the introduction of the Directive means that lenders, administrators, mortgage advisers, mortgage intermediaries and professional persons who carry on activity in relation to mortgages and secured loan contracts will need to check whether or not the relevant contract comprises a 'regulated mortgage contract', whether or not they carry on regulated activity for the purposes of the RAO and whether or not they need to be authorised and regulated by the FCA.

Review of retained provisions of the Consumer Credit Act 1974

Following the transfer, in February 2014, of supervisory responsibility for the consumer credit regulatory regime from the Office of Fair Trading to the FCA, the Government committed to undertaking a review, by 2019, of the provisions of the CCA which were retained on the statute book and not repealed as part of the supervisory transfer process.

As part of the planning process for the review, the FCA circulated a 'call for input' on the retained provisions of the CCA and invited comments on, amongst other topics, the scope and mode of conduct of the review, the timetable for the review and whether or not any particular provisions of the CCA should be prioritised for earlier review.

The call for input closed in May and the FCA will consider the responses and circulate its response later this year.

Brexit

Finally, no bulletin on mortgage or consumer credit would be complete without mentioning the impact of Brexit.

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Whilst very little will change immediately, the most obvious impact of Brexit will be on mortgage, consumer credit and payment services firms which rely on passport rights to supply services from other EU member states into the UK and from the UK into other EU member states. In essence, the passport system allows a firm to rely on its home state permission to authorise the supply of financial services to other EU member states without the need separately to be authorised and regulated in each member state in which the firm operates. Passporting rights will be extinguished upon Britain's exit from the EU.

It is too early to speculate on the extent to which the UK will be able to negotiate the preservation of inbound and outbound passporting rights for financial services firms, or the type of system which might replace the existing rights. Firms which offer mortgages and secured lending, consumer credit, consumer hire and payment services on an EU wide basis will need to monitor this topic carefully and make contingency plans should it become necessary to seek authorisation in an EU member state in order to preserve passporting rights in the remaining member states.

Similarly, even mortgage, credit and payment services firms with a purely domestic focus will not be immune from the Brexit fall-out. First if, as seems likely at the time of writing, Scotland presses for a second referendum on independence and manages to remain within the EU, the mechanism by which financial services firms authorised in England and Wales may continue to offer financial services cross border into Scotland is potentially subject to the same uncertainties which affect the future ability of UK firms to continue to offer services to other EU member states.

Second, a substantial portion of the FSMA regulated mortgage regime, the consumer credit regulatory regime and the payment services regulatory regime derives from EU Directives. A huge and highly complex task lies ahead in terms of identifying the legislation which will remain in place upon Brexit and the legislation which automatically will fall away upon Brexit and repeal of the European Communities Act 1972. It will then be necessary for the Government to propose the necessary replacement legislation. The process will undoubtedly take several years creating a prolonged period of uncertainty for the financial services industry.

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