EXPLANATORY MEMORANDUM TO

THE MORTGAGE CREDIT (AMENDMENT) (EU EXIT) REGULATIONS 2019

2019 No. [XXXX]

1. Introduction

1.1 This explanatory memorandum has been prepared by Her Majesty's Treasury and is laid before Parliament by Act.

2. Purpose of the instrument:

2.1 This instrument is being made in order to address deficiencies in retained EU law in relation to the EU's framework of conduct rules for mortgage firms arising from the withdrawal of the United Kingdom (UK) from the European Union (EU). Specifically, this instrument addresses deficiencies in the Mortgage Credit Directive Order (S.I. 2015/910) to ensure the legislation continues to operate effectively at the point at which the UK leaves the EU.

What did any relevant EU law do before exit day?

2.2 The Mortgage Credit Directive Order 2015 (the 2015 Order) implemented the Mortgage Credit Directive (Directive 2014/17/EU) in the UK, updating where necessary the existing UK legislation. The 2015 Order was made under powers conferred by the European Communities Act 1972 and is therefore retained EU law within the meaning of the European Union (Withdrawal) Act 2018. The 2015 Order achieved three main policy intentions:

2.3 Firstly, prior to the adoption of the Mortgage Credit Directive, a loan was only regulated under the UK's regulatory regime for consumer mortgages if, at the time it was entered into, it was secured on land in the UK. However, when the Mortgage Credit Directive was transposed, the regulatory regime for consumer mortgages was expanded to include loans relating to land anywhere in the EEA.

2.4 Secondly, it brought second charge mortgage lending into the same regulatory regime as first charge mortgage lending. Prior to the 2015 Order coming into force, the scope of the Financial Conduct Authority's (FCA) mortgage regulation was limited to first charge mortgage lending (the primary loan that pays for a property, which has priority over all other claims on the property), and second charge mortgage lending (a loan that uses equity in a property as security, but is not used to purchase the home) was regulated as a part of the FCA's consumer credit regime.

2.5 Thirdly, the Mortgage Credit Directive allows member states to exempt buy-to-let lending to consumers from the detailed requirements of the directive, however it requires that member states exercising this derogation put in place an appropriate framework at a national level regulating buy-to-let lending to consumers. The 2015 Order set out these rules and gave the FCA power to register, supervise and enforce them.

Why is it being changed?

2.6 Once the UK has left the EU, some domestic law (including some provisions in the 2015 Order) will no longer operate effectively unless it is amended to address

deficiencies arising as a result of the UK's withdrawal from the EU. Although the UK had largely legislated domestically in line with the Mortgage Credit Directive prior to it being transposed, the 2015 Order still forms part of the current UK regulatory environment and so clarity and effectiveness is required to maintain compliant practices for UK mortgage lending activity.

What will it now do?

2.7 This instrument makes technical amendments to the 2015 Order to ensure that it continues to operate effectively in a no deal scenario after exit day.

2.8 Key amendments include:

- Amending the territorial scope of regulated consumer buy-to-let lending;
- Amending the rules for consumer buy-to-let foreign currency mortgages.

2.9 The instrument also makes provision for functions currently exercised by EU bodies to be exercised instead by UK bodies:

- Conferring on HM Treasury a power equivalent to that currently available to the European Commission, to update the remarks and assumptions that accompany the formula for the calculation of a standardised measure of the cost of borrowing;
- Revoking the existing EU delegated regulation which sets the minimum level of professional indemnity insurance or comparable guarantee to be held by mortgage intermediaries, leaving the level to be set in rules by the FCA.

2.10 Sections 7.9 – 7.16 set out the changes introduced in this instrument in more detail.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

3.1 None.

Matters relevant to Standing Orders Nos. 83P and 83T of the Standing Orders of the House of Commons relating to Public Business (English Votes for English Laws)

3.2 The territorial application of this instrument includes Scotland and Northern Ireland.

3.3 The powers under which this instrument is made cover the entire United Kingdom (see the European Union (Withdrawal) Act 2018) and the territorial application of this instrument is not limited by either the Act or by the instrument.

4. Extent and Territorial Application

4.1 The territorial extent of this instrument is the whole of the United Kingdom.

4.2 The territorial application of this instrument is the whole of the United Kingdom.

5. European Convention on Human Rights

5.1 The Economic Secretary to the Treasury (John Glen MP) has made the following statement regarding Human Rights:

"In my view the provisions of the Mortgage Credit (Amendment) (EU Exit) Regulations 2019 are compatible with the Convention rights."

6. Legislative Context

6.1 Part 2 of this instrument makes amendments to the Mortgage Credit Directive Order 2015 to correct deficiencies arising from the UK's withdrawal from the EU.

6.2 Part 3 revokes Commission Delegated Regulation (EU) No. 1125/2014 of 19 September 2014 supplementing Directive 2014/17/EU of the European Parliament and of the Council with regard to regulatory technical standards on the minimum monetary amount of the professional indemnity insurance or comparable guarantee to be held by credit intermediaries. This allows the FCA to set the level in its own rules after exit.

6.3 It also confers a power on HM Treasury to make regulations relating to the annual percentage rate of charge (APRC) (in place of a power for the European Commission to adopt delegated acts in Article 17(8) of Directive 2014/17/EU of 4 February 2014 on credit agreements for consumers relating to residential immovable property and amending Directives 2008/48/EC and 2013/36/EU and Regulation (EU) No 1093/2010 (OJ No. L 60, 28.2.2014, p. 34.)). The APRC is a standardised calculation of cost of credit. Its purpose is to provide the borrower with the total cost of the mortgage over its full term on a comparable annualised basis.

7. Policy background

What is being done and why?

7.1 The UK will leave the EU on 29 March 2019. The UK and EU negotiating teams have reached agreement on the terms of an implementation period that will start on 29 March 2019 and last until 31 December 2020. This will provide time to introduce the new arrangements that will underpin the UK-EU future relationship, and provide valuable certainty for businesses and individuals. During the implementation period, common rules will continue to apply. The UK will continue to implement new EU law that comes into effect and the UK will continue to be treated as part of the EU's single market in financial services. This will mean that access to each other's markets will continue on current terms and businesses, including financial services firms, will be able to trade on the same terms as now until 31 December 2020. UK firms will need to comply with any EU legislation that becomes applicable during the implementation period.

7.2 The government is seeking a deep and special future partnership with the EU, which should be greater in scope and ambition than any such agreement before and encompass financial services. Given the highly regulated nature of financial services, the volume of trade between UK and EU markets, and a shared desire to manage financial stability risks, the UK proposes a new economic and regulatory arrangement that will preserve mutually beneficial cross-border business models and economic integration for the benefit of businesses and consumers. Decisions on market access would be autonomous in our proposed model, but would be underpinned by stable institutional processes in a bilateral agreement and continued close regulatory and supervisory cooperation.

7.3 While the government has every confidence that there will be a deal and an implementation period in place, it has a duty to plan for all eventualities, including a 'no deal' scenario. The Government is clear that this scenario is in neither the UK's nor the EU's interest, and the Government does not anticipate it arising. To prepare for this unlikely eventuality, HM Treasury intends to use powers in the European

Union (Withdrawal) Act (EUWA) to ensure that the UK continues to have a functioning financial services regulatory regime in all scenarios.

7.4 The EUWA repeals the European Communities Act 1972 and converts into UK domestic law the existing body of directly applicable EU law (including EU regulations). It also preserves UK laws relating to EU membership – e.g. legislation implementing EU Directives. This body of law is referred to as "retained EU law". The EUWA also gives ministers a power to prevent, remedy or mitigate any failure of EU law to operate effectively, or any other deficiency in retained EU law, through statutory instruments. These contingency preparations for financial services legislation are sometimes referred to as 'onshoring'. These instruments are not intended to make policy changes, other than to reflect the UK's new position outside the EU, and to smooth the transition to this situation. The scope of the power is drafted to reflect this purpose and is subject to further restrictions, such as the inability to use the power to impose or increase taxation, or establish a public authority. The power is also time-limited and falls away two years after exit day.

7.5 Wherever practicable, the proposed approach is that the same laws and rules that are currently in place in the UK would continue to apply at the point of exit, providing continuity and certainty as we leave the EU. However, if the UK does not enter an implementation period, some changes would be required to reflect the UK's new positions outside the EU from 29 March 2019.

7.6 In the unlikely scenario that the UK leaves the EU without a deal, the UK would be outside the EU's framework for financial services. The UK's position in relation to the EU would be determined by the default Member State and EU rules that apply to third countries at the relevant time. The European Commission has confirmed that this would be the case.

7.7 In light of this, the approach in this scenario cannot and does not rely on any new, specific arrangements being in place between the UK and the EU. As a general principle, the UK would also need to default to treating EU Member States largely as it does other third countries, although there are cases where a different approach would be needed including to provide for a smooth transition to the new circumstances.

7.8 HM Treasury published a document on 27 June 2018, which sets out in more detail HM Treasury's approach to financial services legislation under the European Union (Withdrawal) Act. (https://www.gov.uk/government/publications/financial-services-legislation-under-the-eu-withdrawal-act)

7.9 This instrument amends the 2015 Order to address deficiencies arising from the UK's withdrawal from the EU. The key amendments mentioned in sections 2.8 – 2.9 are explained below.

Amending the territorial scope of regulated consumer buy-to-let lending

7.10 This instrument makes amendments to provide that the regulatory regime for buy-to-let mortgages and similar buy-to-let lending to consumers applies only in relation to land in the UK, and not the EEA. FCA supervisory responsibility for such lending entered into after the UK leaves the EU will be confined to loans secured on UK property, if there is no implementation period. However, lending relating to land in the EEA that is currently supervised under the buy-to-let lending regime will continue to be covered by FCA regulation. The regulatory status of post-exit lending to consumers relating to any property outside the UK will be decided under the

regulatory regime for consumer credit, as is currently the case for property outside the EEA.

Amending the rules for consumer buy-to-let foreign currency mortgages

7.11 The 2015 Order prescribes that for foreign currency buy-to-let loans, either (a) the consumer buy-to-let mortgage contract must give the borrower the option to convert to the currency in which he/she receives income/holds assets or of the EEA state where he/she lives, if certain conditions are met (for example, major exchange rate swings), or (b) the lender must put in place other arrangements to limit the exchange rate risk to which the borrower is exposed.

7.12 For borrowers who took out a foreign currency consumer buy-to-let mortgage pre-exit, if the currency conversion option has to be provided for in the initial contract, then those rights (which are contractual) should remain protected under the contract. However, after the UK leaves the EU, sterling will no longer be an EEA currency, and therefore, unless an amendment is made, a borrower resident in the UK whose main income is in sterling would not necessarily have the option of converting the consumer buy-to-let mortgage to pounds sterling.

7.13 This instrument will amend the 2015 Order to add the option of converting to pounds sterling in place of the currency of the EEA state in which the borrower was resident at the time they took out the consumer buy-to-let mortgage, or is currently resident.

7.14 This ensures that a UK-resident borrower who enters into a foreign currency consumer buy-to-let mortgage post-exit and is not otherwise protected by the lender from exchange rate risk would have the possibility of converting to sterling or the currency of their main income or assets (depending on the terms of the contract).

Amending the formula for the calculation of the annual percentage rate of charge for consumer buy-to-let mortgages

7.15 The Mortgage Credit Directive conferred a power on the European Commission to make subordinate legislation modifying the remarks and assumptions which accompany the formula for the calculation of the annual percentage rate of charge (APRC). The APRC is a standardised calculation of cost of credit. Its purpose is to provide the borrower with the total cost of the mortgage over its full term on a comparable annualised basis. This power enables the European Commission to ensure that the remarks and assumptions remain up to date and continue to create uniform results.

7.16 This instrument confers an equivalent power on HM Treasury to ensure that the remarks and assumptions applicable in the UK can be updated as appropriate. This power is necessary because such changes made by the European Commission will not apply to the UK after exit.

8. European Union (Withdrawal) Act/Withdrawal of the United Kingdom from the European Union

8.1 This instrument is being made using powers in the European Union (Withdrawal) Act 2018 in order to address failures of retained EU law to operate effectively or other deficiencies arising from the withdrawal of the United Kingdom from the European Union. In accordance with the requirements of that Act the Minister has made the relevant statements as detailed in Part 2 of the Annex to this explanatory memorandum.

9. Consolidation

9.1 There are currently no plans to consolidate the relevant legislation.

10. Consultation outcome

10.1 HM Treasury has not undertaken a consultation on the instrument, but has engaged with relevant stakeholders on its approach to Financial Services legislation under the European Union (Withdrawal) Act 2018, including on this instrument, in order familiarise them with the legislation ahead of laying. The instrument was also published in draft, along with an explanatory policy note, on 12 December 2018, in order to maximise transparency ahead of laying. (https://www.gov.uk/government/publications/draft-mortgage-credit-amendment-eu-exit-regulations-2019)

11. Guidance

11.1 No further guidance is being published alongside this instrument.

12. Impact

12.1 The impact on business, charities or voluntary bodies is minimal. There is no, or no significant, impact on business, charities or voluntary bodies.

12.2 The impact on the public sector is minimal. There is no, or no significant, impact on the public sector. An Impact Assessment has not been prepared for this instrument because in line with Better Regulation guidance, HM Treasury considers that the net impact on businesses will be less than £5 million a year. Due to this limited impact, a de-minimis impact assessment has been carried out.

13. Regulating small business

13.1 The legislation applies to activities that are undertaken by small businesses. The impact will be minimal.

14. Monitoring & review

14.1 As this instrument is made under the EU Withdrawal Act 2018, no review clause is required.

15. Contact

15.1 Kezia Johnson at HM Treasury. Telephone: 020 7270 5366 or email: Kezia.Johnson@HMTreasury.gov.uk can be contacted with any queries regarding the instrument.

15.2 David Raw, Deputy Director for Banking and Credit, at HM Treasury, can confirm that this explanatory memorandum meets the required standard.

15.3 The Economic Secretary to the Treasury (John Glen MP) can confirm that this explanatory memorandum meets the required standard.

Annex A

Statements under the European Union (Withdrawal) Act 2018

Part 1

Table of Statements under the 2018 Act

This table sets out the statements that may be required under the 2018 Act.

Statement	Where the requirement sits	To whom it applies	What it requires
Sifting	Paragraphs 3(3), 3(7) and 17(3) and 17(7) of Schedule 7	Ministers of the Crown exercising sections 8(1), 9 and 23(1) to make a Negative SI	Explain why the instrument should be subject to the negative procedure and, if applicable, why they disagree with the recommendation(s) of the SLSC/Sifting Committees
Appropriate-ness	Sub-paragraph (2) of paragraph 28, Schedule 7	Ministers of the Crown exercising sections 8(1), 9 and 23(1) or jointly exercising powers in Schedule 2	A statement that the SI does no more than is appropriate.
Good Reasons	Sub-paragraph (3) of paragraph 28, Schedule 7	Ministers of the Crown exercising sections 8(1), 9 and 23(1) or jointly exercising powers in Schedule 2	Explain the good reasons for making the instrument and that what is being done is a reasonable course of action.
Equalities	Sub-paragraphs (4) and (5) of paragraph 28, Schedule 7	Ministers of the Crown exercising sections 8(1), 9 and 23(1) or jointly exercising powers in Schedule 2	Explain what, if any, amendment, repeals or revocations are being made to the Equalities Acts 2006 and 2010 and legislation made under them. State that the Minister has had due regard to the need to eliminate discrimination and other conduct prohibited under the Equality Act 2010.
Explanations	Sub-paragraph (6) of paragraph 28, Schedule 7	Ministers of the Crown exercising sections 8(1), 9 and 23(1) or jointly exercising powers in Schedule 2 In addition to the statutory obligation the Government has made a political commitment to include these statements alongside all EUWA SIs	Explain the instrument, identify the relevant law before exit day, explain the instrument's effect on retained EU law and give information about the purpose of the instrument, e.g., whether minor or technical changes only are intended to the EU retained law.
Criminal offences	Sub-paragraphs (3) and (7) of paragraph 28, Schedule 7	Ministers of the Crown exercising sections 8(1), 9, and	Set out the 'good reasons' for creating a criminal offence, and the penalty attached.

		23(1) or jointly exercising powers in Schedule 2 to create a criminal offence	
Sub-delegation	Paragraph 30, Schedule 7	Ministers of the Crown exercising sections 10(1), 12 and part 1 of Schedule 4 to create a legislative power exercisable not by a Minister of the Crown or a Devolved Authority by Statutory Instrument.	State why it is appropriate to create such a sub-delegated power.
Urgency	Paragraph 34, Schedule 7	Ministers of the Crown using the urgent procedure in paragraphs 4 or 14, Schedule 7.	Statement of the reasons for the Minister's opinion that the SI is urgent.
Explanations where amending regulations under 2(2) ECA 1972	Paragraph 13, Schedule 8	Anybody making an SI after exit day under powers outside the European Union (Withdrawal) Act 2018 which modifies subordinate legislation made under s. 2(2) ECA	Statement explaining the good reasons for modifying the instrument made under s. 2(2) ECA, identifying the relevant law before exit day, and explaining the instrument's effect on retained EU law.
Scrutiny statement where amending regulations under 2(2) ECA 1972	Paragraph 16, Schedule 8	Anybody making an SI after exit day under powers outside the European Union (Withdrawal) Act 2018 which modifies subordinate legislation made under s. 2(2) ECA	Statement setting out: a) the steps which the relevant authority has taken to make the draft instrument published in accordance with paragraph 16(2), Schedule 8 available to each House of Parliament, b) containing information about the relevant authority's response to— (i) any recommendations made by a committee of either House of Parliament about the published draft instrument, and (ii) any other representations made to the relevant authority about the published draft instrument, and, c) containing any other information that the relevant authority considers appropriate in relation to the scrutiny of the instrument or draft instrument which is to be laid.

Part 2

Statements required when using enabling powers under the European Union (Withdrawal) 2018 Act

1. Appropriateness statement

1.1 The Economic Secretary to the Treasury (John Glen MP) has made the following statement regarding use of legislative powers in the European Union (Withdrawal) Act 2018:

"In my view the Mortgage Credit (Amendment) (EU Exit) Regulations 2019 does no more than is appropriate."

1.2 The changes to the law made by these Regulations are limited to those that fix deficiencies arising out of EU Exit, or those that provide for the revocation of otiose legal provisions."

2. Good reasons

2.1 The Economic Secretary to the Treasury (John Glen MP) has made the following statement regarding use of legislative powers in the European Union (Withdrawal) Act 2018:

"In my view there are good reasons for the provisions in this instrument, and I have concluded they are a reasonable course of action."

2.2 This is because the instrument is necessary to ensure the UK mortgages regulation regime can continue to operate effectively from exit day.

3. Equalities

3.1 The Economic Secretary to the Treasury (John Glen MP) has made the following statement(s):

"The instrument does not amend, repeal or revoke a provision or provisions in the Equality Act 2006 or the Equality Act 2010 or subordinate legislation made under those Acts.

3.2 The Economic Secretary to the Treasury (John Glen) has made the following statement regarding use of legislative powers in the European Union (Withdrawal) Act 2018:

"In relation to the instrument, I, Economic Secretary to the Treasury (John Glen MP) have had due regard to the need to eliminate discrimination, harassment, victimisation and any other conduct that is prohibited by or under the Equality Act 2010."

4. Explanations

4.1 The explanations statement has been made in section 2 of the main body of this explanatory memorandum.