

Clients & Friends Memo

Finally Certainty About Licensing SPVs Under the FCA Consumer Credit Regime

20 August 2014

From 1 April 2014, responsibility for the regulation of consumer credit in the UK was transferred from the Office of Fair Trading (“OFT”) to the Financial Conduct Authority (“FCA”), drawing certain activities relating to consumer credit within the authorisation and regulated activity provisions of the Financial Services and Markets Act 2000 (“FSMA”). As the FSMA regime is regarded as more onerous than the previous Consumer Credit Act 1974 (“CCA”) licencing regime and due to the timing implications of obtaining full authorisation, the applicability of an exemption¹ (the “SPV Exemption”) for SPVs introduced by statutory instrument² to entities holding the benefit of consumer credit agreements will be of interest to market participants.

The transfer from the CCA regime to the FSMA regime

The Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) (No. 2) Order 2013³ came into full force and effect on 1 April 2014 (the “Effective Date”)⁴. This order, among other things, repealed the licensing regime under the CCA and amended FSMA and the Regulated Activities Order⁵ to govern certain activities relating to consumer credit agreements.

Following the Effective Date, entering into a regulated credit agreement as a lender or exercising the rights and duties of a lender under a regulated credit agreement is a specified

¹ Paragraphs 55 and 56 of the Financial Services and Markets Act 2000 (Exemption) Order 2001 (SI 2001/1201), as amended. This memo analyses the applicability of paragraph 55 to securitisation SPVs and therefore uses the terminology of “lender” and “regulated consumer credit agreements”. However, paragraph 56 mirrors this exemption in relation to consumer hire agreements such that a similar analysis may be undertaken. Please feel free to contact the lawyers listed at the end of this memo if you would like to discuss the applicability of paragraph 56 to consumer hire agreements.

² The Financial Services and Markets Act 2000 (Consumer Credit) (Miscellaneous Provisions) (No. 2) Order 2014 (SI 2014/506)

³ SI 2013/1881

⁴ Certain provisions came into force on 26 July 2013 and the interim permissions regime came into force on 2 September 2013

⁵ Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (SI 2001/544)

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activity regulated under FSMA.⁶ Various other activities that may be relevant to securitisation SPVs have also become specified activities following the Effective Date (including debt-collecting⁷ and debt administration⁸).

Since consumer credit agreements have been made specified investments⁹, the above activities are also now regarded as regulated activities. To carry on a regulated activity, an entity must either be authorised (which, in the case of consumer credit authorisation, is currently under an interim permission scheme) or exempt. If a regulated activity is carried on by an entity that is neither authorised nor exempt, the underlying agreements relating to that activity may be unenforceable and that entity will commit an offence. Given these consequences, it is important that any interpretation or exemption relied upon by a securitisation SPV is both clear and unambiguous.

Does a securitisation SPV conduct these regulated activities?

Under the old CCA regime there was some uncertainty as to whether an SPV that held the benefit of consumer loans (especially when such loans were assigned equitably, as is the market standard) would be required to hold a licence. This uncertainty (insofar as it remained after the coming into force of the Consumer Credit Act 2006¹⁰) arose as a result of the definition of creditor, being “the person providing credit under a consumer credit agreement or the person to whom his rights and duties under the agreement have passed by assignment or operation of law, and in relation to a prospective consumer credit agreement, includes the prospective creditor”¹¹. In the case of an SPV taking an interest in consumer loans under an equitable assignment this definition (read strictly) would not apply, since such an SPV would not take both “rights and duties” of the original creditor as a result of such assignment. However, since no assignment could result in the passing of duties and due to the approach taken in similar legislation¹², some commentators¹³ were of the opinion that this definition would be construed by a court as only requiring “rights or duties” to pass. Accordingly, and in what was viewed by some practitioners as a precautionary rather than necessary measure, most SPVs took the steps required to obtain a licence under the CCA.

⁶ Article 60B, Regulated Activities Order, as amended

⁷ Article 39F, Regulated Activities Order, as amended

⁸ Article 39G, Regulated Activities Order, as amended

⁹ Article 88D, Regulated Activities Order, as amended

¹⁰ This Act amended the definition of “consumer credit business”, which was previously seen as the primary source of uncertainty in the CCA. The amended definition extended consumer credit business to include persons that otherwise become “creditors”. Some commentators considered that this fixed the ambiguity in the application of the CCA, though such an argument still relied on a less strict reading of the term “creditor”.

¹¹ s.189 of the CCA

¹² A common contrast was made between the definition of “owner” in the CCA that corresponds to the definition of “creditor” in that Act and the definition of “owner” in the Hire Purchase Act that referred to the “rights or duties” but otherwise closely mirrored the language.

¹³ See e.g. Goode on Consumer Credit Law

The new regulated activities in FSMA relating to credit agreements hinge on whether the relevant party is regarded as a lender in much the same way that the CCA regime was premised on the concept of creditor. The definition of lender is “(a) the person providing credit under a credit agreement, or (b) a person who exercises or has the right to exercise the rights and duties of a person who provided credit under such an agreement”. This language differs from the previously applicable definition of creditor insofar as it makes no reference to an assignment. However, the use of the term “rights and duties” remains and this continues to cast doubt as to whether the definition would apply to an SPV assignee of a credit agreement. While the altered formulation removes the inconsistency of referring to an assignee of duties, if it was intended that assignees of credit agreements were to be treated as lenders, “rights or duties” would be a more natural choice of language. Though the definition of lender still does not clearly apply to an SPV on its face, it is clear from the SPV Exemption that HM Treasury anticipated that it would and (in any case) the SPV Exemption should lead to a more certain position for an SPV.¹⁴

Conditions to the application of the SPV Exemption

The explanatory note published by HM Treasury¹⁵ makes clear that the justification for the SPV Exemption is that “relevant consumer protections will be maintained because of the requirement that the servicer is authorised”. Accordingly, a number of conditions must be satisfied to benefit from the SPV Exemption, though these arguably go beyond the stated objective.

The most notable conditions are that the SPV seeking the benefit of the exemption:

- is not the original lender and does not grant (nor is required to or promises to grant) credit under the relevant consumer credit agreement;
- does not undertake debt adjusting, debt counselling or debt collecting (as those terms are understood in the Regulated Activities Order);
- has entered into a servicing arrangement in relation to the relevant consumer credit agreement with a servicer that is authorised to carry on specific regulated activities relating to consumer credit¹⁶; and
- has arranged for the servicer to comply (or, where it acts without the servicer, it complies) with relevant provisions of FSMA and the CCA in relation to the variance of terms and conditions of the credit agreement.

¹⁴ For example, article 39H of the Regulated Activities Order, as amended, provides that activities conducted by a lender are excluded from the scope of the regulated activities at articles 39D(1), 39E(1), 39F(1) and 39G(1). In addition, any argument around the use of “rights and duties” would have to be repeated in the interpretation of article 60B(2), where this language is repeated again. The use of the SPV Exemption thus gives greater certainty.

¹⁵ The Explanatory Note to the Financial Services and Markets Act 2000 (Consumer Credit) (Miscellaneous Provisions) (No. 2) Order 2014

¹⁶ The activities specified under article 39F, 39(G) or 60(B) of the Regulated Activities Order, as amended.

There is also a concept of an exempt period, being the 30 day period after a servicing arrangement comes to an end. During an exempt period an SPV may carry on the relevant regulated activities itself and will remain exempt.

While these conditions are likely to be satisfied in respect of most consumer loan securitisations without amendment, there are prudent modifications that may be made to transaction documents to ensure that the conditions are satisfied. For example, while servicing agreements as a matter of course require servicers to maintain all authorisations required to conduct the servicing activities, it would be prudent to specifically require them to maintain the authorisations referred to in the SPV Exemption.

In addition, the short length of the exempt period means that attention should be paid to the replacement mechanics of any servicer. It is better to address the possible issues that may arise in this respect at the outset of a transaction, rather than when the servicer is being replaced (which is likely to be a high stress scenario).

Conclusions

The SPV Exemption provides a useful exemption to registration under the new FCA consumer credit regime. If registration were to be required under the new regime, this would involve both significant timeline implications (with registrations for authorisation under the full regime anticipated to take up to 6 months) and costs for the transaction (both up front and on-going). As such, it is beneficial that under the SPV Exemption most securitisation SPVs will now be able to fall outside the scope of the FCA regime. Furthermore, the SPV Exemption provides the benefit of certainty to what was previously an uncertain area of law, although in this regard it is unfortunate that the underlying regulated activities remain unclear in their drafting.

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