EXPLANATORY MEMORANDUM TO

THE MUTUAL SOCIETIES (TRANSFERS) ORDER 2009

2009 No. 509

1. This explanatory memorandum has been prepared by Her Majesty's Treasury and is laid before Parliament by Command of Her Majesty.

2. Purpose of the instrument

2.1 The instrument modifies the legislation which applies to a transfer of a building society to a subsidiary of another mutual society, to facilitate such transfers. It also specifies mutual insurers as a type of EEA mutual society for the purposes of the Building Societies (Funding) and Mutual Societies (Transfers) Act 2007, so that the modified transfer provisions may apply to a transfer to a subsidiary of a mutual insurer.

3. Matters of special interest to the Joint Committee on Statutory Instruments

3.1 None

4. Legislative Context

4.1 The instrument is the first use of the Treasury's powers under sections 3 and 4 of the Building Societies (Funding) and Mutual Societies (Transfers) Act 2007 ("the Act"). It implements those sections in relation to building societies.

4.2 The instrument is being made to facilitate transfers of building societies to subsidiaries of other mutual societies. Under current law it is permissible to transfer the business of one mutual to another of the same kind. However, it is more difficult to transfer the business of a mutual to a company, even one owned by another mutual. This instrument will make it easier for a building society to transfer to the subsidiary of another mutual society, in recognition that the building society will be transferring into a mutual group and so will remain within the broader mutual sector.

4.3 The instrument will also enable mutual insurance undertakings to participate in such transfers, by designating mutual insurers as "EEA mutual societies" for the purposes of the Act and so making it easier for a building society to transfer to the subsidiary of a mutual insurer. This is in keeping with a commitment made by then Economic Secretary (Ed Balls) during debates in the House of Commons, to work to find a solution that would enable mutual insurance companies to be included in the transfer arrangements under the Act. [Column 1157 on 27 April 2007 of Hansard refers].

4.4 The Treasury will publish a subsequent draft Order implementing section 3 of the Act for industrial & provident societies at a later date. Following consultation the Treasury does not intend to implement the Act for friendly societies. Credit unions are outside the scope of the Act.

5. Territorial Extent and Application

5.1 This instrument applies to all of the United Kingdom.

6. European Convention on Human Rights

6.1 The Economic Secretary to the Treasury, Ian Pearson has made the following statement regarding Human Rights:

"In my view the provisions of the Mutual Societies (Transfers) Order 2009 are compatible with the Convention rights".

7. Policy background

7.1 Section 3 of the Act gives the Treasury the power to modify specified legislation to make it easier for a mutual society (building society, friendly society or industrial and provident society) to transfer its business to the subsidiary of another mutual society (building society, friendly society, industrial and provident society or EEA mutual society).

7.2 The Government's policy intention is therefore to facilitate transfers between the different mutual sectors, offering mutual societies an alternative route to transferring their business while remaining in the wider mutual sector.

7.3 The mutual sector in the UK is very diverse, comprising building societies, friendly societies, industrial & provident societies and credit unions. Together they have over 30 million members and combined total assets in excess of £400 billion. The sector is increasingly important in delivering on Government objectives in relation to financial inclusion and social cohesion.

7.4 The Government also welcomes the contribution the sector makes in providing for choice and diversity in the financial services sector as well as its overall contribution to the UK and global economies.

7.5 There is widespread interest in the mutual sector about the potential for cross fertilisation and consolidation within the sector. The instrument will make it easier for a building society to transfer to another mutual group; but it will not affect the legislation which applies to a transfer to a company or group outside the mutual sector. It will improve the opportunities for building societies to join up with other mutual societies.

8. Consultation outcome

8.1 The Treasury held a public consultation on its proposals to implement the Act from 1 September to 27 October 2008 and received twenty formal responses from a wide cross section of stakeholders ranging from trade associations and sector representative bodies to the general public, individual societies and other mutual societies.

8.2 The sector had requested urgent implementation of section 3 of the Act to facilitate transfers within the mutual sector in the current economic climate. Due to this urgency for implementation the Treasury considered that the shorter consultation period of 8 rather than the 12 weeks was justified in the light of the fact that some aspects of implementation of the Act had already been discussed in an earlier Treasury consultation[1] on "Financial stability and depositor protection[2]". In addition the implementing order would be debated in both Houses under the affirmative resolution procedure so there would be ample scope for discussion and scrutiny.

8.3 The Treasury also invited the main stakeholder respondents to the consultation to a follow-up meeting on 3 December 2008 and shared a draft of the Order with them. The Treasury also held discussions with the Financial Services Authority and Building Societies Association on the draft implementing Order.

8.4 Respondents were unanimous that the Treasury should use the powers granted in section 3 of this Act to facilitate transfers within the mutual sector.

8.5 The Government is not convinced of a need to implement section 1 of the Act in the current economic circumstances and will review the case for implementation in two years time. On section 2 the Government will implement at an appropriate time having regard to implementation of the Banking Bill, which will affect building societies insolvency law.

8.6 Detailed analysis of the consultation responses is available on the HM Treasury public website at www.hm-treasury.gov.uk/consultations.

9. Guidance

9.1 The Treasury will not be publishing guidance on the implementation of the Act. However, copies of the implementing Order will be mailed to all the respondents to the consultation and posted on the Treasury website.

10. Impact

10.1 An Impact Assessment is attached to this memorandum.

11. Regulating small business

11.1 Transfers under the Act are optional and will not have a disproportionate impact on small business. Societies will all have to apply the same procedures for a transfer.

[1] From 30 January 2008 to 23 April 2008.
[2] The consultation considered among other things whether the Treasury should act to make building society members' funds rank equally with liabilities to creditors in the event of an insolvency. Members' funds currently rank below liabilities to creditors in the event of an insolvency.

12. Monitoring & review

12.1 The FSA will need to be satisfied that a transfer is within the scope of the Act and the implementing Order, as it must approve transfers of business involving building societies. The Treasury, with the assistance of the FSA, will carry out a post implementation review in 3 years and if appropriate publish a report.

13. Contact

Sammy Amissah at HM Treasury Tel: 020 7270 5291 or email: sammy.amissah@hm-treasury.x.gsi.gov.uk can answer any queries regarding the instrument.

Summary: Intervention & Options		
Department /Agency:	Title: Impact Assessment of Building Societies (Funding) and Mutual Societies (Transfers) Act 2007	
Stage: Final	Version:	Date: 12 January 2009
Related Publications: Consultation on Building societies (Funding) and Mutual societies (Transfers) Act 2007 - September 2008		

Available to view or download at:

http://www.hm-treasury.gov.uk

Contact for enquiries: Sammy Amissah Telephone: 020 7270

What is the problem under consideration? Why is government intervention necessary?

Under current law it is straightforward for a mutual to transfer its engagements to another mutual of the same kind. However, it is more onerous for a mutual to transfer its engagements to a company, even if the company is owned by another mutual.

What are the policy objectives and the intended effects?

- Make it easier for a mutual society to transfer its business to a subsidiary of another UK mutual society or of an EEA mutual– by implementing sections 3 and 4 of the Act

What policy options have been considered? Please justify any preferred option.

(a) No intervention

(b) Partial Implementation to allow a UK mutual society to transfer its business to a subsidiary of another UK mutual or EEA mutual but not including mutual insurers.

(c) Full implementation to allow a UK mutual society to transfer its business to a subsidiary of another UK mutual or of an EEA mutual including mutual insurers

Option C is the preferred option. This would include mutual insurers within the scope of

When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects? 3 years

Ministerial Sign-off Partial Impact Assessments:

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options

Signed by the responsible Minister:

Summary: Analysis & Evidence

Policy Option:	Description:

COSTS		
	ANNUAL COSTS	Description and scale of **key monetised costs** by 'main affected groups: Authorities (Government and FSA) logistical costs of drafting policy and legal documents as shown (£0.1mn). The Act is an opt-in and mutual societies will only incur costs on implementation in relation to an actual transfer. Ranging from £0.45mn
	One-off Yrs	
	Approx	
	Average Annual Cost (excluding one-off)	
	£ N/A	Total Cost (PV) £ Not quantifiable
	Other **key non-monetised costs** by 'main affected groups' N/A	

BENEFITS		
	ANNUAL BENEFITS	Description and scale of **key monetised benefits** by 'main affected groups. Benefits mainly accrue to societies in the flexibility and choice it will offer in their corporate restructuring
	One-off Yrs	
	Not quantifiable	
	Average Annual Benefit	
	£ Not	Total Benefit (PV) £ Not quantifiable
	Other **key non-monetised benefits** by 'main affected groups' Consolidation in the sector enhancing competition within the wider financial	

Key Assumptions/Sensitivities/Risks

Price Base	Time Period	**Net Benefit Range** (NPV) £	**NET BENEFIT** (NPV Best estimate)

What is the geographic coverage of the policy/option?	EEA
On what date will the policy be implemented?	April 2009
Which organisation(s) will enforce the policy?	FSA
What is the total annual cost of enforcement for these	£ To be confirmed
Does enforcement comply with Hampton principles?	Yes
Will implementation go beyond minimum EU	No
What is the value of the proposed offsetting measure	£ To be confirmed
What is the value of changes in greenhouse gas	£ N/A
Will the proposal have a significant impact on	No

Annual cost (£-£) per organisation (excluding one-off)	Micro	Small	Medium	Large
Are any of these organisations	No	No	No	No

Impact on Admin Burdens Baseline (2005 Prices)					(Increase – Decrease)
Increase	£ N/A	Decrease	£ N/A	Net	£ N/A

Key: Annual costs and benefits | (Net) Present Value

Evidence Base (for summary sheets)

1. PROPOSAL (Section 3 of the Act)

1.1 Current law provides for a mutual to transfer its engagements to another mutual of the same kind. There are also provisions governing a transfer of engagement (or business) of a mutual to a company.

1.2 However, it is more onerous for a mutual to transfer its engagements to a company, even if the company is owned by another mutual. This proposal is to facilitate a transfer of engagements to a company which is a subsidiary of another mutual.

2. OBJECTIVE

2.1The policy intention is to implement the provisions of the Act and make it easier for a UK mutual society to transfer its business to a subsidiary of another UK mutual or of an EEA mutual.

3. BACKGROUND

3.1 The Building Societies (Funding) and Mutual Societies (Transfers) Act 2007 received Royal Assent on 23 October 2007 and gives the Treasury power to make it easier for a mutual society to transfer its business to subsidiary of another mutual society. The Treasury subsequently sought stakeholders' views on the implementation of this Act, in a consultation that closed on 1 September 2008.

4. OPTIONS APPRAISAL

(a) No Intervention

(b) Partial Implementation to allow a UK mutual society to transfer its business to a subsidiary of another UK or EEA mutual

(c) Full implementation to allow a UK mutual society to transfer its business to a subsidiary of another UK mutual or of an EEA mutual (including mutual insurers).

Option C is the Government's preferred option.

Option	**Costs**		**Benefits**
(a) No intervention	No additional costs.		No benefits to mutual members.
(b) Partial Implementation– UK and EEA mutuals	Same as option c below but excludes mutual insurers.		Same as option c below but excludes mutual insurers.
(c) Full	<u>Authorities</u>	<u>Societies</u>	Benefits accruing,

implementation- Proposals implemented to allow UK mutual society to transfer its business to a subsidiary of another UK mutual or of an EEA mutual (including mutual insurers)	FSA Implementation costs: £20-£25K Costs per merger: £15K-£25K HM Treasury Policy and Legal £50K	Implementation costs- Not available Costs per merger Large: £1mn-£24 mn Medium £0.45mn-£1mn Small: £6K - £0.45mn	whilst substantial, are difficult to quantify. Primary benefits arise by allowing market consolidation beyond like-with-like merger or demutualisation. This in turn will allow mutuals to compete more effectively with other legal forms. As a result, the mutual sector will be placed on a more stable footing going forward.

5. RISKS, UNCERTAINTY AND UNINTENDED CONSEQUENCES

5.1 There are two primary areas where unintended consequences could occur- the need to prevent backdoor demutualisation and legal risk of disturbing contractual arrangements in relation to PIBS (permanent interest bearing shares) and charitable assignments.

5.2 The Treasury has consulted extensively on how to minimise the risk of demutualisation, but recognises that there is always the possibility that in future an innovative transaction structure could be constructed to avoid the safeguards which we have put in place to prevent this.

Charitable assignments

5.3 We do not propose to make any amendments to the existing contractual arrangements in relation to charitable assignments and consider that this is a matter for the parties to deal with, and it would be undesirable for Government to intervene.

Permanent Interest Bearing Shares (PIBS)

5.4 PIBS are financial instruments, deferred shares issued by building societies to meet Tier 1 capital requirements: they are non-redeemable and rank after all other liabilities (including subordinated debt) in insolvency. Most PIBS include a term stating that if a building society transfers its undertaking to a company, the PIBS become subordinated debt of that company. By converting into subordinated bonds they would cease to qualify as Tier 1 capital in a transfer to a company or would at best be innovative Tier 1 capital.

Some respondents to the consultation had considered whether the Treasury could make explicit provision in the implementing Order so as to vary the terms of PIBS in a transfer to which the Order applied, converting them into a different instrument that would retain Tier 1 capital treatment. However, the Treasury considers that it would be outside the scope of the Act for it to interfere with contractual rights.

6. IMPLEMENTATION

6.1 The proposal will be implemented by Orders made under the Building Societies (Funding) and Mutual Societies (Transfers) Act 2007.

7. WHO WILL BE AFFECTED

7.1 The first order under the Act will make it easier for a building society to transfer its business to the subsidiary of another UK mutual or an EEA mutual (including a mutual insurer). Societies can decide whether or not to use the new procedure. A later order will implement the Act for industrial and provident societies.

8. EQUITY AND FAIRNESS

8.1 The Government considers that the changes proposed by this proposal will not bring disproportionate benefits or have disproportionate effects on particular groups.

9. CONSULTATION WITH SMALL BUSINESS

The Government sought respondents' views on the Government's proposals and implementation proposals.

- SMALL FIRMS IMPACT TEST

We do not expect the proposed changes to impose any costs on small firms. Use of the modified transfer procedures is optional.

- COMPETITION ASSESSMENT

We have carried out a simple competition assessment and are of the view that the proposals in the draft Order are not expected to lead to any barriers to entry.

10. CONSULTATION

10.1 HMT held a public consultation on these provisions in September 2008 and has held subsequent discussions with key stakeholders including the FSA, the BSA and a variety of mutuals. HMRC will hold a further consultation on the tax implications of the Act.

11. ENFORCEMENT AND SANCTIONS

11.1 The Financial Services Authority will need to be satisfied that parties to a transfer qualify to use the simplified procedures in the implementing Order.

12. SUMMARY AND RECOMMENDATIONS

12.1 Benefits cannot be quantified but are substantial, since they offer additional ways of ensuring financial stability within the mutual sector. The cost of each transaction will be high, so the process is unlikely to be utilised by small mutuals. However, since use of the mechanism will be a commercial decision by the merging entities and it is inevitable that this will only occur when the parties believe that benefits exceed costs. Because the benefits will far outweigh the costs we recommend that this proposal be adopted.

Costs annex and assumptions

Two categories: initial implementation costs and subsequent process costs incurred each time such a transfer is undertaken. Figures are merely indicative.

Implementation costs (estimated):

	FSA (say £20-25k) being:
Amend current Handbook	40 - 50 staff days (£17.2k to £21.5k)
Train supervisors etc	Regulatory/supervisory 5 man days (£2.15k)

Subsequent costs, each time a building society uses the procedure we estimate:

	FSA (Say £15k to £25k)	Transferee (£67k to £95k plus p&p)
Agreeing details of proposal and ensuring compliance with legislation	Nil	100 - 130 staff days (£43k to £55.9k)
Development of transfer statement	Nil	20 – 30 man days preparation (£8.6k to £12.9k)
Approval of transfer statement	10-15 man days review work (£4.3k to £6.45k)	10 – 15 man days redrafting (£4.3k to £6.45k)
Printing and postage of transfer statement (Say £5 per member)	Nil	Large: £2.5m - £60m Medium: £1.125m - £2.5m Small: £15k - £1.125m

General meeting and vote	Nil	May not need a separate meeting if it can be coordinated to take place alongside AGM.
Confirmation hearing	25 – 40 man days (£10.75k to £17.2k)	25 – 40 man days (£10.75k to £17.2k)

Note:

FSA average mean daily costs £430 (include overhead allocations).

Transferee average mean daily costs taken as similar to FSA.

Split based on Companies Act Balance Sheet definition of company size.