



PROPOSED AMENDMENTS TO THE CREDIT UNIONS ACT 1979

A consultation Document by H M Treasury

October 2001

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- A. Allow credit unions to borrow money from external sources, other than authorised banks and other credit unions.**
- B. Allow credit unions to differentiate between certain accounts by paying dividends at different rates, and to pay dividends more than once each year.**
- C. Allow credit unions to provide additional basic services and charge fees (e.g. bill payments).**
- D. Make the common bond requirements more flexible.**
- E. Establish appropriate regulation on the use of the name Credit Union.**
- F. Change the minimum coverage requirements for fidelity bonds.**
- G. Allow credit unions to offer accounts that may be held in the name of more than one member.**

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CONSULTATION DOCUMENT

Foreword by Ruth Kelly MP

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FOREWORD BY RUTH KELLY MP, ECONOMIC SECRETARY TO THE TREASURY

The publication in 1999 of the reports of the Credit Unions Taskforce and Policy Action Team 14 – *Credit Unions of the Future*, and *Access to Financial Services* – turned the spotlight on credit unions, raising general awareness of the invaluable work that they have been doing for many years, without fanfare: encouraging people to save money by providing savings facilities, affordable credit, and financial education to the less well off.

Britain has one of the most competitive and sophisticated financial service sectors in the world, but for too many people, access to financial services still means cheque-cashing shops, and loan sharks. However, with their ethos of self-help and thrift, credit unions are in an excellent position to make a worthwhile contribution to increasing access to financial services, and not just among poorer communities, but as a competitive provider of basic services for the better off too. That is why the Government fully supports the work of credit unions, and is determined to encourage the sector wherever possible.

The Credit Union Taskforce and PAT 14 identified and promoted ways for the banks, building societies and others to assist credit unions expand their business, thereby assisting larger numbers of people on low incomes to gain access to basic financial services – particularly those who might otherwise have found it difficult to access main stream financial services. But there is still more that can be done.

This document contains a number of proposals that remove or reduce legislative constraints on credit unions' operational powers, many of which have been proposed by people from within the sector. The movement is known for its diversity, so I hope that as many credit unions as possible – large and small, community, associational and employee based – will respond, to enable us to take account of all the different perspectives and needs before we decide how to proceed.

RUTH KELLY MP

1. INTRODUCTION

This paper seeks views from interested parties on proposals to reform the Credit Unions Act 1979.

The proposals would only affect credit unions in Great Britain. Given the particular nature and origins of credit unions, separate legislation applies in Northern Ireland.

The proposals contained in this document are generally distinct from those changes that are due to be introduced when FSA commences its regulation of credit unions on 1 July 2002¹. They are, however, intended to complement the new regulatory regime.

FSA's new regime will strengthen the regulation of credit unions, while remaining proportionate to the risks that credit unions face. Importantly, it will bring the regulation of credit unions more closely into line with that of other deposit-takers, and give their members a similar level of protection to that afforded depositors with banks and building societies.

By contrast, the proposals contained in this document are designed to reduce some of the restrictions on credit unions' operational powers, which should help them to compete for deposits, and to develop their role as complementary financial institutions.

Structure and Nature of Credit Unions

Credit unions are societies registered under the Industrial & Provident Societies Act 1965, and which comply with the requirements referred to in section 1 of the Credit Unions Act 1979. Entities registered as credit unions have separate legal personality, and limited liability.

As self-help, democratic savings and loans institutions, credit unions have demonstrated that co-operative principles can offer an

¹ Responsibility for the regulation of credit unions will transfer from the Registrar of Friendly Societies to the Financial Services Authority (FSA) when the relevant sections of the Financial Services and Markets Act (Mutual Societies) Order 2001 are brought into force at midnight on 30 November 2001. However, the FSA's new regulatory regime will not be introduced until 1 July 2002.

effective way for many thousands of people to manage their financial affairs. Their basic philosophy and objectives appeal to a wide and diverse range of people, who benefit through greater self-sufficiency in the management of their financial affairs, and are protected from exorbitant interest charges by the statutory protection of a fixed maximum interest rate for borrowings by members.

Members save by subscribing for non-transferable shares deposited with a credit union. Members may take out loans, at a maximum rate of interest of 1% per month and, for the majority, up to £5,000 in excess of their shareholding.

The objects of credit unions, as defined by the 1979 Act, are:

- the promotion of thrift among the members by the accumulation of savings;
- the creation of sources of credit for the benefit of the members at a fair and reasonable rate of interest;
- the use and control of the members' savings for their mutual benefit; and
- the training and education of the members in the wise use of money and in the management of their financial affairs.

The main benefits to members are that they have a place to deposit savings, and may apply for loans at reasonable rates of interest.

Membership is restricted to those who meet the qualification ('the common bond'), for a particular credit union. The common bond may be one of four main types: residence in a particular locality; being a member of, or having an association with, an organisation; working for a common employer or in a particular locality; and following a particular occupation.

Most credit unions are largely run by unpaid volunteers, and provide basic savings and loan services of particular benefit to low income groups, who may well have no dealings with the mainstream financial services sector.

The value of each share in a credit union is fixed by statute at £1.00, and each member's savings are limited to a maximum of £5,000, or 1½% of the total shareholding of a credit union, whichever is the greater. A credit union may only accept deposits in the form of subscription for its shares. It may pay a dividend on shares, not exceeding 8%, after all expenses and taxes have been accounted for. The normal range of dividend payments is between 3 and 5%.

Most credit unions may only offer loans to their members up to a maximum of £5,000 more than the value of the borrowing member's share capital. So a member with the maximum of 5,000 shares may usually borrow up to £10,000, although certain credit unions are permitted to grant individual loans up to a maximum of 1½% of their aggregate shareholdings – with some constraints to limit its exposure to large loans, and provided it has adequate management and systems in place. In practice, though, the majority of loans are for less than £1,000.

Under the current regime, the rate of interest charged on loans may not exceed 1% per month on the reducing balance (12.68% APR maximum). Credit unions may borrow from authorised banks, and, in the short term, from other credit unions. They may hold surpluses on deposit subject to restrictions (broadly they are restricted to current and deposit accounts at authorised banks).

There are now just over 700 registered credit unions, with new registrations still averaging around 50 a year. Total assets have risen to over £200 million and continue to grow by about £20 million each year. In 2000, loans were made to a value of £160 million, and this year membership topped 300,000 – concentrated in the North of England and Scotland, although there is increasing presence in the South and West of England, and in Wales.

The Government strongly supports credit unions' ethos of self-help and wishes to encourage the movement's growth, thereby strengthening its capacity to provide financial services to the least well-off. The proposals in this consultation document are designed to help further that aim by removing or reducing legislative constraints on credit union's operational powers.

Regulatory Reform Orders

This document seeks views on proposed amendments to the Credit Unions Act 1979 (“the 1979 Act”) under section 1 of the Regulatory Reform Act 2001 (“the 2001 Act”).

There is a special Parliamentary procedure for making a Regulatory Reform Order, which is explained in more detail in **Annex A**. We hope it will be possible for the Order to be made in time that the changes under it may be brought into force on 1 July 2002 – the date the FSA are due to commence regulating credit unions – or as soon thereafter as practicably possible.

Each proposal for a Regulatory Reform Order must satisfy a number of legal tests. The questions in this document are designed to elicit the information that the Economic Secretary will need in order to satisfy the relevant Parliamentary Committees that, among other things, the proposal satisfies these tests. In particular, the Regulatory Reform Act requires information on, and assessment of:

- whether any of the proposals could remove any necessary protection;
- whether any of the proposals could prevent any person from continuing to exercise any right or freedom which he might reasonably expect to continue to exercise and, if so, how he is to be enabled to continue to exercise that right or freedom;
- whether any new burdens are being imposed on any person in the carrying out of an activity;
- whether any savings or increases in cost are estimated to result from the proposals and, if so,-
 - (i) the reasons why savings or increases in cost should be expected, and
 - (ii) if it is practicable to make an estimate of the amount, that amount and how it is calculated,
- any benefits (other than savings in cost) which are expected to flow from the implementation of the proposals.

For this reason, we would particularly welcome your views on how each aspect of the proposed changes in this consultation document meets the following tests:

- **Necessary protection:** the Minister making a Regulatory Reform Order must be of the opinion that it does not remove any necessary protection. Such protection relates to the checks and balances associated with a particular regulatory regime. The protection does not have to be statutory in nature and does not have to be for the purposes originally intended by Parliament. If the Minister considers a particular protection to be no longer necessary, he or she must provide the Parliamentary scrutiny committees with compelling evidence to support this view.
- **Rights and freedoms** - a Regulatory Reform Order cannot be made unless the Minister is satisfied that it does not prevent any person from continuing to exercise any right or freedom which they might reasonably expect to enjoy. This test recognises that there are certain rights that it would not be fair to take away from people under these procedures.

As the changes we propose are intended to create additional options for credit unions without affecting their ability to operate within the existing parameters if they so choose, we do not believe that the proposals would deprive anyone of a necessary protection, or prevent anyone from exercising an existing right or freedom. We would welcome your views as to whether we are correct in thinking that this is the case.

Other Safeguards

In order to provide for the effective reform of regulatory regimes, Regulatory Reform Orders can re-state existing burdens and create new burdens. But where that is the case stringent additional safeguards apply:

- **Proportionality** - If a new legal burden is being imposed, or an existing burden retained or increased, then the Minister must ensure that it is proportionate to the benefit it brings. This means, for example, that imposing a burden of several thousand pounds on charities for some negligible benefit would not pass the test.

- **Fair balance** - before proposing any Regulatory Reform Order that has the effect of imposing legal burdens, the Minister must be of the opinion that a fair balance is being struck between the interests of the person affected by the Order and the interests of the wider public. In this context, fairness does not mean that everyone must benefit. What it does mean is that the benefit to society as a whole must be such as to justify the additional burden on a small group or the individual.
- **Desirability** - the Minister making the Regulatory Reform Order must be of the opinion that the extent to which it removes burdens or brings other benefits makes the Order as a whole desirable.

We do not consider that these reforms impose any new burdens, as they are entirely deregulatory in nature, and while some additional safeguards need to be introduced, we believe that in each case the overall effect is deregulatory. However, we would be interested in your views on this matter.

Consultation

The Act requires Departments to consult widely on regulatory reform proposals. It requires us to collect evidence on a number of issues from a wide range of consultees. The list of consultees, including the devolved administrations, to whom the document has been sent is at **Annex B**. It is also available on the internet at:

- <http://www.hm-treasury.gov.uk> (you should use the specific link that will take the reader straight to the condoc);
- <http://www.cabinet-office.gov.uk/regulation/act/condocs.htm>;
and
- <http://www.ukonline.gov.uk>

Comments are invited from all interested parties, and not just from those to whom this document has been sent. We should be particularly interested in any comments that respondents may have on that part of each proposal that deals with the preservation of necessary protections, rights and freedoms, and the observation of other safeguards, or any other comments or suggestions they may have.

The Parliamentary Committees who will deal with orders under the Regulatory Reform Act have requested that a note explaining the Parliamentary process for orders to be made under the Act be annexed to all consultation papers so that consultees understand when and to whom they are able to put their views, should they wish to do so. This is set out in **Annex A**.

This consultation document follows the format recommended by the Cabinet Office for such proposals. The criteria applicable to all UK public consultations under the Cabinet Office Code of Practice on Consultation are set out in **Annex C**.

Disclosure

Normal practice will be for details of representations received in response to this consultation document to be disclosed, or for respondents to be identified. While the Act provides for non-disclosure of representations in some cases, the Minister is at least required to include the names of all respondents in the list submitted to Parliament alongside the draft Order. You should note that:

- If you request that your representation not be disclosed, the Minister will not be able to disclose the contents of your representation without your express consent and, if the representation concerns a third party, their consent too. Alternatively, the Minister may disclose the content of your representation but only in such a way as to anonymise it.
- In all cases where your representation concerns information that may be damaging to the interests of a third party, the Minister is not obliged to pass it on to Parliament if she does not believe it to be true or she is unable to obtain the consent of the third party.

Please identify any information that you or any other person involved do not wish to be disclosed.

Finally, you should be aware that the scrutiny Committees would be able to request sight of your representation as originally submitted. This is a safeguard against attempts to bring improper influence to bear on the Minister. We envisage that, in the normal

course of events, this provision will only be used rarely and on an exceptional basis.

Comments should be sent by 18 January 2002 at the latest to: Michael Dynan-Oakley, HM Treasury, 2nd Floor, Allington Towers, Allington Street, London SW1E 5EB, from whom further copies of this document may also be obtained.

2. POLICY & LEGISLATIVE BACKGROUND

Credit unions are mutual savings and loan organisations, registered and regulated by the Registry of Friendly Societies (RFS). Staff at the Financial Services Authority (FSA) currently undertake regulatory tasks on behalf of RFS, in accordance with the terms of a service level agreement between RFS and the FSA. Registration and regulation are governed by the Industrial and Provident Societies Acts 1965 to 1968, and the Credit Unions Act 1979.

The registration and regulation of credit unions are due to transfer from RFS to FSA at midnight on 30 November 2001 (see footnote 1 above). Thereafter, on 1 July 2002, FSA will introduce their new regulatory regime, the details of which they have been consulting on for some time (the latest consultation document is at www.fsa.gov.uk/pubs/cp/107). The FSA's new structure will strengthen the regulation of credit unions, bringing it more into line with that of other deposit-takers. Credit union members will enjoy a similar level of protection to that afforded depositors with banks and building societies. The new regime is, however, intended to be proportionate to the nature and the scale of the risks that credit unions face.

Existing Regulatory Controls

Under the Credit Unions Act 1979, the Chief Registrar of Friendly Societies is responsible for:

- deciding whether to register a new credit union;
- requiring each credit union to produce an annual return including its accounts;
- requiring each credit union to satisfy him that it has in place a valid insurance policy covering its members against the loss of their savings through fraud by their officers or employees; and
- issuing a certificate (under section 11C of the Act) to any credit union that wishes to offer increased loans, provided it can demonstrate that it has adequate management and systems in place.

The Registrar has limited statutory powers to intervene in the affairs of a credit union after its registration. Under sections 17 and 18 of the Act, he has the power to require financial or other information and may appoint an inspector to investigate its affairs. If a credit union gets into financial difficulties or no longer meets the conditions for registration, the Registrar has the power under Sections 19 and 20 of the Act to: suspend its operations; suspend or cancel its registration; or to petition for it to be wound up.

Despite his restricted range of statutory powers, the Registrar has developed an informal system of supervision and guidance for credit unions. For example, before any credit union is registered, there are thorough discussions with the organisers of the project and the prospective "Committee of Management" (culminating in a pre-registration visit) to ensure that those involved have undertaken appropriate training and understand the responsibilities of managing a credit union. There is also a voluntary system of quarterly returns as a basis for monitoring the financial health of credit unions.

Under a service level agreement in operation since 1 January 1999, FSA staff have supported the Chief Registrar in the discharge of his responsibilities.

On 1 April 2001, some of the limits imposed by the Credit Unions Act 1979 were increased by Order of the Chief Registrar, with the consent of the Treasury (The Credit Unions (Increase in Limits on Deposits by persons too young to be members and of Periods for the Repayment of Loans) Order 2001 S.I. 2001/811). The limit on the deposits that a credit union may take from persons too young to be members was increased from £750 to £5,000. The maximum periods for which credit unions may make loans were increased from two to three years for unsecured loans, and from five to seven years for secured loans. For credit unions holding a certificate under section 11C of the Credit Unions Act 1979, the maximum periods were increased from four to five years for unsecured loans and from ten to twelve years for secured loans.

Forthcoming changes to regulatory controls

In December 2000, FSA issued CP77 through which it consulted on the approach it should adopt within the existing legislative

framework to the regulation of credit unions. The proposals covered the entire spectrum of regulatory oversight touching on standards, registration, approved persons, supervision, management systems, lending, capital liquidity, borrowing and investment, enforcement, consumer compensation, complaints, fees and transitional arrangements.

In the light of the responses to the consultation process, the FSA revised its proposals as set out in the Feedback Statement it issued in July 2001. Both FSA's consultation paper and the Feedback Statement can be downloaded from <http://www.fsa.gov.uk/pubs/cp/77/index.html>.

The reforms proposed in this consultation paper are intended to complement the regulatory system as proposed by the FSA, on which they are still consulting.

Previous deregulation order

A number of reforms to the Credit Unions Act 1979 were introduced in 1996 by way of the Deregulation (Credit Unions) Order 1996. In summary the main points were as follows. The Order:

- introduced a new membership qualification for credit unions: that of either living or working in a particular locality. It also allowed the appropriate registrar to register a credit union on the basis of a statutory declaration by three members and the secretary that a common bond exists among the members.
- permitted a member to hold shares of up to 1.5% of a credit union's total shareholdings, if that produces a higher figure than the £5,000 already permitted.
- allowed a loan which is equal to or less than a member's shareholding to be regarded as a secured loan (which can be repaid over a longer period than an unsecured one). It also amended section 7(5) of the Act to prevent a member from withdrawing the shares used to support such a loan.

- removed the restriction on borrowing which applied to non-qualifying members so that the same rules now apply to them as apply to other members.
- relaxed the limit on a member's borrowings for those credit unions which can demonstrate to the Registrar that they have satisfactory arrangements to deal with the increased risk. The maximum that may be lent by such an approved credit union, in excess of shareholding, became: (a) the greater of £10,000 and 1.5% of total shareholding or (b) 20% of the credit union's general reserve, whichever is the lesser amount. Approved credit unions may continue to make advances at the current statutory level of £5,000 in excess of shareholding. As a further safeguard the sum of those individual loans being greater than 10% of the general reserve may not exceed five times the value of the general reserve. For approved credit unions, the maximum periods within which a loan must be repaid, were increased to ten years for a secured loan and four years for an unsecured loan, provided that the credit union's general reserve at the time amounts to at least 10% of its assets. Procedures for the grant and withdrawal of certificates of approval for credit unions were also introduced.

Initial proposals for change in 1998 consultation document

The changes introduced in 1996 proved successful and were widely welcomed by the industry. Since then, there has grown up a broad consensus of opinion that there is scope for further reform, which would benefit credit unions and their members without any adverse effects.

During 1998, the Treasury established a Credit Union Taskforce chaired by Fred Goodwin, to consider ways in which the mainstream financial sector could help credit unions expand their business. The Taskforce's report, which can be found at: <http://www.hm-treasury.gov.uk/docs/1999/creditunion.html>.

In 1998, the Treasury issued a consultation document on proposed changes to the Credit Unions Act 1979 (available from <http://www.hm-treasury.gov.uk/pub/html/reg/cucon.html>). In the main, the proposals were well received, although the movement

was keen for Government to make changes to two of the key proposals. In the end, Government decided that it would be better to synchronise the introduction of any deregulatory changes with the introduction of FSA's new regulatory regime. In written answer to a Parliamentary Question on 7 December 1999 as at **Annex E**, the then Economic Secretary announced that a package of reforms would be brought forward in due course.

Current Proposals

The proposals in this document have been developed since 1998, as the Economic Secretary announced to Parliament on 18 July 2001. In brief, of the other proposals from 1998, two were brought into force on 1 April 2001, through an order made by the Chief Registrar, with the consent of Treasury, one other (removing the current maximum membership limit) will come into force when the Financial Services And Markets Act (Mutual Societies) Order 2001 is brought into force, while the timing of the one other change dealt with under the Financial Services & Markets Act 2000 (concerning the disposal of collateral) remains to be decided. In the interests of clarity, **Annex F** provides a comparison of the proposals in this consultation document with those from the 1998 consultation document.

The proposals in this consultation document, therefore, revise and build on the outstanding proposals from the 1998 consultation document. The following chapters provide detailed descriptions of each of the seven current proposals, and an assessment of each against the safeguards and tests as required by the Regulatory Reform Act 2001.

3. COSTS TO CREDIT UNIONS

These proposals are generally distinct from FSA's new regime for regulating credit unions. They are intended to reduce certain of the existing static restrictions on credit unions' operational powers.

The proposals covered in this document are due to be introduced at the same time FSA commences its regulation of credit unions, or as soon thereafter as is practicably possible.

The cost to credit unions of regulation by the Registrar of Friendly Societies is made according to a menu of individual charges. One change that regulation by FSA will introduce is that credit unions will pay a single annual charge, covering the cost of regulation, and their membership of the Financial Services Ombudsman and Compensation schemes.

On current plans, FSA's new charging regime will be in place long before any of changes proposed in this paper are introduced, which means that the cost to credit unions of securing any necessary rule changes or other permissions, will be nil. In other words, while credit unions will still be required to register any rule changes necessary for them to take advantage of some of the changes proposed in section 4, these changes will be covered by FSA's single annual charge, which means, unlike the current system, they will not face one-off additional charges for such registration services.

Where the adoption of an additional power requires authorisation under FSA Rules Version 2, credit unions will only need to make a single application to cover all the adopted powers listed. Where a credit union is already operating under Version 2 Rules, it will not be required to apply for further authorisation, but may be required to inform FSA that it proposes to adopt further powers.

Further comments about the anticipated costs and benefits of each proposal may be found in the partial Regulatory Impact Assessment included at **Annex D**.

The proposed amendments are intended to relieve credit unions from administrative burdens, so it would help if respondents could indicate the cost savings that might arise in each case. Equally, if

respondents do not think there will be savings they should explain why. If any additional cost burdens are envisaged, an estimate should also be given.

4. PROPOSED AMENDMENTS TO THE 1979 ACT

A: Allow credit unions to borrow money from external sources, other than authorised banks and other credit unions

Current Position:

Under section 8 of the 1979 Act, credit unions may only accept deposits in the form of share accounts. They may borrow only from authorised banks or, temporarily, from another credit union or association of credit unions under section 10 of the Act. However, they may, and do, receive grants.

As credit unions were new to Britain in 1979, caution was a significant factor behind the limitation of their borrowing powers to the most well established and closely regulated institutions i.e., banks. In 1979, it was also thought prudent to minimise credit unions' exposure to other credit unions, so inter-credit union borrowing was restricted to short-term loans.

Burden:

In their early years, it can be difficult for credit unions to acquire sufficient funds to make loans. Apart from members' savings, they are largely reliant on grants, usually from local authorities, to build-up resources. Independent research suggests that local authorities contribute around £15 million each year towards the cost of creating and developing credit unions, usually as part of wider community strengthening strategies, but always as a non-financial stakeholder. In addition, credit unions may only borrow from other credit unions for a limited period. While many banks do allow credit unions to borrow at sub-market rates, the current regime prevents credit unions from shopping around for the very best deals, or borrowing from local community based organisations that might have particular reasons to lend a credit union money at no or an extremely low rate of interest.

Regulatory reform amendment:

Amend section 10 to completely remove the restrictions that currently prevent credit unions from borrowing from anyone other than authorised banks and other credit unions, so that they may in future, borrow from whomever they choose.

Safeguards:

Necessary Protection

It might be argued that providing credit unions with greater freedom to decide from whom they may borrow could increase the risk to their members of poor borrowing decisions. However, we consider that such arguments must be viewed in light of the following points-

(1) The existing protection - that credit unions' borrowings may not exceed 50% of total paid up share capital - will be maintained, to ensure that they are not over committed to external sources of finance; and no one loan, or portfolio of loans from a single lender (other than from an institution authorised by FSA) may exceed 10% of a credit union's share capital.

(2) In addition, external borrowing will be reported to FSA as part of its prudential regulation of credit unions. FSA would therefore have the capacity to intervene if it became aware that poor or reckless borrowing decisions had led to a deterioration in a credit union's general financial position.

(3) Credit unions have operated in Britain for 22 years now, and we believe that the general development of expertise in their management, as well as their very ethos of prudence and thrift suggest that they would tend to maintain a responsible and cautious approach to borrowing. This would be reinforced by the additional experience of lenders to credit unions since 1979.

(4) Borrowing decisions by credit unions would remain subject to fiduciary duties owed to the credit union as a whole, which would also tend to promote prudent and cautious borrowing.

Overall, therefore, we do not believe that removing a limit on the range of players from whom a credit union may borrow constitutes the removal of a fundamental or necessary protection.

Rights and Freedoms

The effect of the proposal would be to expand the range of borrowing options available to credit unions. It would not prevent them from operating within the existing parameters if they so wished.

Burdens imposed

For the reasons given in the preceding paragraph, we take the view that this proposed change would not impose any additional burdens in relation to credit unions.

Costs, savings and other benefits

We believe the cost to credit unions of this proposed change would be nil. However, it would materially increase their range of potential sources of credit, enabling them to shop around for loans at more competitive rates and on more advantageous terms. Importantly, it would also enable credit unions to borrow from any local community based source with altruistic reasons for lending at a particularly low rate of interest – benefits that may be returned to members in the form of higher dividend payments.

In addition, FSA are separately consulting on draft rules governing the use of subordinated debt as capital – see page 53, paragraph 8.2.1(4) of CP107, Credit Unions Specialist Sourcebook Draft Rules, August 2001. Under the terms of these new rules, subordinated debt could be counted towards reserves, which would enable a credit union to grow more quickly than would otherwise be possible through conventional membership growth. It is likely that lenders would charge credit unions a premium for borrowing on subordinated terms, reflecting the additional risk associated with a loan that – depending on the exact terms – ranks below members' deposits in the unfortunate case of insolvency. However, the current regulatory reform proposal may assist credit unions to secure subordinated loans on favourable terms by increasing the range of potential lenders: for example, a local authority that is keen to see a local credit union develop and grow.

B: Allow credit unions to differentiate between certain accounts by paying dividends at different rates, and to pay dividends more than once each year

Current position:

Credit unions were originally designed as simple savings and loan institutions, to assist the least well off through the promotion of thrift and as a source of affordable credit. As such, credit unions may only accept deposits in return for their shares. They may pay a dividend on these shares, subject to the restrictions imposed by section 14 of the 1979 Act, which, among other things, limits the distribution of dividends to once a year, and to a single rate on all deposits.

Some credit unions already offer their members a range of accounts. However, they are unable to differentiate between these various accounts in a meaningful way, as the annual dividend must be paid at the same rate on each.

Burden:

The current position prevents credit unions from differentiating between members who save, save to borrow, or save and use ancillary services – such as making bill payments. This means that credit unions are less able to increase their capital base by rewarding members who invest but do not borrow. Also, they are unable to offset the cost of ancillary services by paying a lower or no dividend to those members that take advantage of such services. In addition, credit unions are restricted to paying an annual dividend.

Regulatory reform amendment:

Amend section 14 to enable certain credit unions to offer different dividends on different accounts, and to declare such dividends more than once each year.

Safeguards:

Necessary Protection

It may be argued that, in allowing credit unions to offer different dividends on different accounts, those people with only modest levels of savings, but who do take advantage of ancillary services, could be materially worse off under this proposal. However, there is no reason why members with modest means should be expected to hold all their savings in an account on which there may be a record of no or low dividend payments. This also needs to be seen in the light that – in line with their general ethos of promoting thrift – we would expect credit unions to advise their members on beneficial ways to allocate their resources.

In addition, we propose that the amendment described above will be circumscribed, by restricting the range of credit unions that may take advantage of it. The ability to differentiate between dividend payments will be limited to a restricted group of credit unions – to be defined by a similar set of criteria to those which define version 2 credit unions under FSA rules. (This will ensure that this considerably greater flexibility and freedom is only available to larger credit unions which are subject to greater capital and liquidity requirements than are standard – and which will also generally operate more sophisticated systems and controls.) Details of the criteria used by FSA can be found in CP107, Credit Unions Specialist Sourcebook Draft Rules, August 2001, available through:

<http://www.fsa.gov.uk/pubs/cp/77/index.html>

Importantly, dividends may only be paid from past or present profits, which means that the distribution of accumulated profits more than once a year, or in a way that differentiates between accounts, would not expose a credit union or its members to any additional risks, financial or otherwise. In addition, credit unions would still be free to pay a single rate dividend once a year. It should be noted that compliance with the draft capital requirements in the Credit Unions Specialist Sourcebook might restrict the amount of profit available for distribution to members.

In the circumstances, we do not believe that this proposal entails the removal of any necessary protections.

Rights and Freedoms

It remains for members to allocate their funds in a way that maximises the returns they are able to make, and they should be better able to do this with the broader range of options that are likely to be available were this proposal to be introduced in its current form. In the circumstances, we do not believe that the proposal would prevent any person from continuing to exercise any right or freedom he might reasonably expect to continue to exercise. Credit unions would still be able to pay a single dividend if they so chose, and while members may receive lower dividends on deposits held in, for example, transaction accounts, there would be no restriction on their ability to transfer such of their deposits not needed for transactions to an account on which a credit union has a record of paying a higher dividend.

Burdens imposed

Under the proposal in its current form, additional options would be available to certain credit unions, some of which may be more expensive than others to operate. However, the adoption of such options would remain a commercial decision for individual credit unions to take. Ultimately, this proposal is permissive only, and as such, we do not believe it imposes additional burdens.

Costs, savings and other benefits

Although the operation of different options made possible by this proposal may be more costly, we do not think that the introduction of this permissive change would in itself result in additional costs for credit unions.

To the extent that credit unions would need to register a rule change in order to take advantage of the ability to set dividends in accordance with this proposal they would not be subject to any additional charge for so doing (see section 3).

An important benefit will be that credit unions will be able to compete for deposits on a more level playing field with other deposit takers. In other words, by offering to pay higher returns on savings-only accounts, they should be able to attract a higher number of investors that only wish to benefit from the savings side

of a credit union's business, while providing a larger pool of money for the credit union to turn into loans for those who wish to borrow.

C: Allow credit unions to provide additional basic services and charge fees (e.g. bill payments)

Current Position:

Under section 1(2) of the 1979 Act, a credit union may only pursue the objectives set out in section 1(3) – described at paragraph 9 of the Introduction. As simple savings and loan institutions, credit unions were given relatively limited objectives when they were introduced to Britain in 1979, and while the legislation does not prevent a credit union from offering ancillary services to its members, its effect is to prohibit them from charging for any service other than the provision of loans.

Burden:

Some credit unions pay bills on members' behalf by making out a cheque drawn against each member's account. However, many are deterred from offering such services, as they are unable to pass on the cost of processing the transactions. In addition, as mutual organisations, those credit unions that provide bill payment services have no option but to spread the associated costs across the total membership, as there is no way for them to limit charges to those members that take advantage of ancillary services.

Regulatory reform amendment:

Derogate from section 1 (2)(a) to allow credit unions to charge for the provision of ancillary services – money transmission, issuing and administering means of payment, and bill payments – on a cost recovery basis.

Safeguards:

Necessary Protection

Some credit unions already provide bill payment and money transmission services. This change simply permits credit unions to undertake this work on a more commercial basis, and we incline to the view that permitting them to charge does not entail the removal of any necessary protection.

Rights and Freedoms

Allowing credit unions to recover the cost of ancillary services is expected to increase the availability of such services throughout the movement, thereby extending the rights and freedoms currently enjoyed by the members of only a handful of credit unions, to others in the movement.

Burdens imposed

Those members who have so far enjoyed the privilege of free ancillary services may – should credit unions start to recover the cost of providing such services – face the burden of new charges. However, we incline to the view that in enabling credit unions to charge only those members that take advantage of ancillary services, rather than the membership as a whole (which would certainly include non-user members), this proposal strikes a fair balance between users and non-users in terms of apportioning any new burden. We also believe that in restricting charges to cost recovery only, this proposal ensures that charges remain proportional to the value of any service provided. In addition, it would still remain for individual members to decide whether to take advantage of any services on offer.

Costs, savings and other benefits

The cost to credit unions will be neutral i.e., they will be able to move from the current position of charging the whole membership for any services they offer a limited number of their members, to simply charging those members that take advantage of such services.

There are savings that individuals can make by paying their utility bills by automatic credit transfer. Allowing credit unions to recover the cost of ancillary services is likely to increase the number of credit unions that actually offer bill payment services, thus increasing the number of people with access to the benefit of cheaper utility services. In addition, we would expect the benefits of cheaper utility bills to outweigh any payments to a credit union for providing a bill payment service, but would be particularly interested in any comments on this from consultees.

D: Make the common bond requirements more flexible.

Current Position:

Section 1 (2)(b) requires a credit union's membership to be "restricted to persons all of whom fulfil a specific qualification which is appropriate to a credit union... and that in consequence a common bond exists between the members..." rationale for common bonds includes the building of confidence among members, and their ability to exert moral pressure on one another to repay loans. Section 1(4) as amended lists some common bond qualifications that are deemed to be appropriate; others have subsequently been added by the Chief Registrar in exercise of the powers vested in him by that section. The 1996 deregulation order added paragraph (f), in which the qualification rests on a combination of criteria: a member may either reside, or work, in a particular locality.

Burden:

As credit unions grow, they find that the common bond qualifications act as a restriction on whom they can attract as members, particularly where workplace and community based credit unions wish to merge. The "living or working" common bond does not always address the problem. For example, a residential credit union may wish to join with one based on worship at a particular church in the area (this would be under an associational common bond - category (e)), whose congregants do not necessarily live in the common bond area. This applies to groups wanting to register as well as credit unions wishing to merge.

Regulatory reform amendment:

To further extend Section 1(4) to permit the combination of category (e) - the associational common bond, which enables those people who have an association with a particular organisation to form a credit union - with all other types.

Safeguards:

Necessary Protection

The existing safeguard contained in section 1(5) would continue to operate, i.e. that “in ascertaining that a common bond exists . . . the appropriate registrar shall have regard to the nature of the qualification for admission to membership of the society”. Experience in other countries (USA, Canada and the Irish Republic) does not suggest that widening the common bond weakens credit unions. Indeed, credit unions already merge using the large number of existing options. We do not, therefore, believe that increasing the number of options affects the existing protection afforded to credit unions or their members. In any event, it is not possible for one credit union to takeover another by hostile means, and this proposal would not alter that position. Mergers between credit unions are regulated by FSA, which would not permit one credit union to takeover the common bond of another credit union unless the all parties were in favour of such a development.

Rights and Freedoms

We do not believe that increasing the permutations under which credit unions may merge affects the rights or freedoms of these organisations or their members.

Burdens imposed

In our opinion, this proposed change would increase the options for the combinations of credit unions that may be formed without imposing any new burdens on credit unions or their members.

Costs, savings and other benefits

As is currently the case, credit unions would still need to obtain permission from FSA should they wish to extend or amend their common bond, but they will not be incur any additional charges for so doing (see section 3).

E: Establish appropriate regulation on the use of the name Credit Union

Current Position:

Section 3 of the 1979 Act sets out the rules governing the use of the name “credit union”, which have never been brought into force. One reason for this is that the provisions would have had unintended consequences, e.g. they would prevent American military personnel on bases in Britain from using the name “credit union” in connection with activities relating to a credit union based outside Britain, and which are not subject to regulation by FSA.

Burden:

The use of the name “credit union” is not controlled or protected in any way, which means there is no legal recourse should the name be used inappropriately or in a way deliberately designed to mislead, where misuse could damage the reputation of the movement.

Regulatory reform amendment:

Retain the general prohibition in section 3(2) of the 1979 Act, but add to the exceptions in subsection (3) by allowing certain persons based overseas to use the term “credit union” (or related expressions) in reference to themselves, or to represent themselves as being credit unions. The new exception would be for institutions with their head offices outside the United Kingdom and recognised under the law of a state other than the United Kingdom as credit unions, or institutions equivalent to credit unions as they exist in the United Kingdom. The test for equivalence would relate to the central features of credit unions’ as they exist in the UK, and would include objects, membership, restrictions on forms of deposit-taking, share value and monetary limits on borrowing.

Although sections 3(2) and (3) of the 1979 Act have not been brought into force, it is clear from section 1(2)(a) of the Regulatory

Reform Act that orders under that Act may amend uncommenced statutory provisions.

Safeguards:

Necessary Protection

This change would introduce a valuable protection that was always envisaged, but has never been brought into force.

Rights and Freedoms

The introduction of this change would not remove existing rights and freedoms. It would only operate in relation to rights and freedoms already curtailed by Act of Parliament (i.e. the ability to use the term "credit union"), by relaxing that curtailment by the introduction of a further exception. In other words, the prohibition imposed by Parliament would become less restrictive by the removal from its scope of the overseas persons referred to above.

Burdens imposed

The introduction of this change would enable FSA to challenge through the courts any individual or organisation that it came to notice was, in its opinion, illegally using the name "credit union". However, while this change would place a burden on FSA, we do not believe the incidence of misuse is likely to be such that large volumes of additional activity would be required, and believe that the value of being able to seek redress through the courts, to protect the good name of the movement, would be worthwhile. In that light, we believe this proposal is proportionate in as much as it introduces a desirable protection for the movement that we feel strikes a fair balance between the rights of individuals and the public interest. However, we should be interested to receive any views consultees may have about whether they feel this proposal meets these tests.

Costs, savings and other benefits

In seeking legal remedy, FSA may incur costs. However, we believe that simply having the power to seek legal recourse will have a positive effect in minimising the incidence of misuse of the

name “credit union”, and that any actual cost incurred would be worth paying, where it provided greater consumer confidence in credit unions.

F: Change the minimum coverage requirements for fidelity bonds

Current Position:

Section 15 requires credit unions to maintain insurance against losses incurred by reason of the fraud or dishonesty of their officers and employees. The Credit Unions (Insurance against Fraud etc.) Regulations 1980, made by the Chief Registrar, with the consent of Treasury, established the minimum coverage amounts now prescribed by that section, which reflect the size of credit unions at that time.

Total share value	Minimum cover requirements (percentage of total share value)	
	Single claim	Total claims per annum
Up to £10,000	50 %	100 %
From £10,000 to £100,000	20 %	100 %
Over £100,000	15 %	75 %

For example: a credit union with share capital of £92,000 would require single claim cover of at least £21,400 and total claim cover of £92,000. Similarly, a credit union with share capital of £175,000 would require single claim cover of at least £34,250 and total claim cover of £156,250.

Burden:

The 1980 regulations allow the minimum levels of insurance against fidelity losses to reduce as a percentage of a credit union's share capital. However, these regulations have not been updated to take account of the considerable growth in the size of Britain's largest credit unions since that time. Consequently, a growing number of British credit unions find themselves having to purchase bonds that provide levels of cover that are substantially above that purchased by credit unions overseas, which have asset bases many times the size of the largest British credit unions. This comparative over-insurance leads to higher premium costs, and is a situation that will only become more acute as the asset bases of British credit unions continue to grow.

Regulatory reform amendment:

A new threshold, together with ceilings for bond minimum limits are proposed, as amendments to Section 15(2)(b), which prescribes the current levels of cover required. The new threshold and ceilings would be:

Total share value	Minimum cover requirements (percentage of total share value)	
	Single claim	Total claims per annum
Over £1,000,000	<ul style="list-style-type: none">£150,000 plus5 % of value over £1,000,000	<ul style="list-style-type: none">£750,000 plus5 % of value over £1,000,000
Minimum limits are not required to exceed:	£ 2,000,000	£4,000,000

For example: under the new system, a credit union with share capital of £14,000,000 would be required to take-out single claim cover of £850,000 while under the existing system, a bond of £2,108,000 would be required.

It would not be possible to simply re-make the 1980 regulations to take account of the changes suggested here, as the existing legislation only provides for three thresholds, and the purpose of this amendment is to add a fourth threshold. We envisage that necessary effect would be achieved by designating the relevant provisions of the RRO as "subordinate provisions" under section 4(3) of the Regulatory Reform Act. This would allow them to be modified in the future by negative resolution procedure. Given that the existing regulation-making power is not subject to any Parliamentary procedure, we consider that the use of "subordinate provisions" in this instance would be appropriate - it would in fact lead to a greater degree of Parliamentary scrutiny than exists now.

The current regulation-making power is exercisable by the Chief Registrar with the consent of the Treasury. We propose that the new power to adjust the limits would be exercisable by the Treasury.

Safeguards:

Necessary Protection

Bond cover minima for small and medium sized credit unions will remain unaffected, so the basic necessary protection will remain in place. In addition, new FSA regulatory regime will provide additional safeguards against fidelity losses by encouraging the development of stronger management systems and internal controls, particularly at larger credit unions.

Rights and Freedoms

To the extent that the rights and freedoms of credit unions or their members may be affected, the rights and freedoms concerned would have to be the right to manage or participate in a credit union at a certain level of fidelity cover. In the circumstances, we do not believe that a reduction in the level of cover for the very largest credit unions – in order to bring the levels of bond cover they require into line with bond ratios for equivalent credit unions overseas – represents the removal of a right or freedom that a credit union or its members could reasonably expect to continue.

Burdens imposed

In practice, the only impact of this proposal would be to reduce the level of insurance cover that a large credit union would be required to purchase, thus reducing an existing burden.

Costs, savings and other benefits

None, although credit unions with share capital above £1 million should benefit from lower cost bond premiums. In the circumstances, it would be helpful if consultees were able to indicate what, if any, bond price savings they feel could be achieved by the introduction of the suggested new threshold, or whether another threshold might be more appropriate.

G: Allow credit unions to offer accounts that may be held in the name of more than one member

Current Position:

All accounts operated by credit unions are held in the name of individual members. The legislation does not include a specific prohibition on joint accounts but the wording of section 5(3) creates what in our view are unwarranted limitations on the utility of joint accounts with credit unions. That subsection says that any one member of a credit union cannot have any claim or interest in the shares of the credit union exceeding £5,000 or 1.5% of the total shareholding, whichever is the greater. For shares held jointly (for which each joint holder has an entire claim), this means that the effective limit for each shareholder is half the prescribed upper limits.

Burden:

Many families, couples in particular, would choose to operate joint accounts rather than individual ones. The above limitations restrict the options which credit unions are currently able to offer to their members.

Regulatory reform amendment:

Amend section 5(3) so that the upper limits are doubled for joint holders of shares.

Safeguards:

Necessary Protection

The legislation will be amended to make clear that for any liabilities associated with a joint account i.e., loans, the holders will be jointly and severally liable.

Rights and Freedoms

We do not believe that any rights or freedoms are affected by this proposed change. Individual members would still be entitled to establish a new or maintain an existing account or accounts in their own name. The opening of a joint account would simply be an additional option.

Burdens imposed

It is possible that an individual could face the additional burden of responsibility for the liabilities of the other party with whom they hold a joint account. However, we would expect credit unions to alert those members that sought to open accounts in joint names, to the key implications of entering into joint financial agreements, which means that any liability would be proportionate to the member's own behaviour and risk profile. In addition, as joint liability is a relatively standard practice in the provision of financial services, we believe this proposal strikes a fair balance between the rights of the individual and the public interest, as it would seem unreasonable for members more generally to bear any risks associated with joint members. Finally, the opening of a joint account would increase the available options for members, and while it would still be up to couples to decide whether they wanted to open a joint account, we see this as a desirable change, which brings families and de facto partnerships within credit union membership. We should be interested to receive any views consultees may have about whether they feel this proposal meets these tests.

Costs, savings and other benefits

As is currently the case, credit unions would still need to register a rule change with FSA should they wish to offer joint accounts, but they will not be charged for so doing (see section 3).

ANNEX A

REGULATORY REFORM PROPOSALS AND ORDERS - PARLIAMENTARY CONSIDERATION

Introduction

1. These reform proposals in relation to the Credit Unions Act 1979 as amended will require changes to primary legislation in order to give effect to them. The Minister could achieve these changes by introducing a Regulatory Reform Order under the Regulatory Reform Act 2001. Regulatory Reform Orders are subject to preliminary consultation and an extended Parliamentary scrutiny (by Committees in each House of Parliament) of any subsequently proposed Order. On that basis, the Minister invites comments on these reform proposals in relation to the Credit Unions Act 1979 as measures that might be carried forward by a Regulatory Reform Order.

Regulatory Reform Proposals

2. This consultation document on the Credit Union Act 1979 has been produced because the starting point for regulatory reform proposals is thorough and effective consultation with interested parties. In undertaking this preliminary consultation, the Minister is expected to seek out actively the views of those concerned, including those who may be adversely affected, and then to demonstrate to the Scrutiny Committees that he or she has addressed those concerns.
3. Following the consultation exercise, when the Minister lays proposals before Parliament under the Regulatory Reform Act, he or she must also lay a report for consideration by the Scrutiny Committees setting out a summary of:
 - the burden imposed by the existing law;
 - whether any of those burdens are proposed to be removed or reduced;
 - how the proposals otherwise further the other objects of the Regulatory Reform Act (re-enacting proportionate burdens, introducing new but proportionate burdens, removing inconsistencies and anomalies);
 - whether there is 'necessary protection' and how it is to be continued;

- how any reasonable expectation of the exercise of rights or freedoms is affected (if at all) and how the exercise can be continued;
 - how new burdens (if any) are both proportionate and, taking the proposals as a whole, strike a fair balance between the public interest and the interests of the persons affected by the new burdens;
 - whether an Order that imposes burdens is desirable in terms either of the burdens it removes or the other benefits it brings;
 - whether any parts of the proposed Order are being designated as 'subordinate provisions', allowing them to be changed by less elaborate Parliamentary procedures in the future;
 - what cost savings or increases are expected, and why;
 - what other benefits there will be from the proposals;
 - details of the consultation process;
 - any representations received as a result of that consultation; and
 - the changes made as a result.
4. On the day the Minister lays the proposals and report, the period for Parliamentary consideration begins. It lasts for 60 days, excluding Parliamentary recesses of more than four days. If you want a copy of the proposals and the Minister's report, you will be able to get them either from the Government department concerned or by visiting the Cabinet Office's website at <http://www.cabinet-office.gov.uk/regulation/act/index.htm>.

Parliamentary Scrutiny

5. Both Houses of Parliament scrutinise regulatory reform proposals and draft orders. This is done by the Scrutiny Committees.
6. Standing Orders in the Commons stipulate that the Committee there considers whether proposals:
- (a) appear to make an inappropriate use of delegated legislation;
 - (b) remove or reduce a burden or the authorisation or requirement of a burden;
 - (c) continue any necessary protection;

- (d) have been the subject of, and take appropriate account of, adequate consultation;
 - (e) impose a charge on the public revenues or contain provisions requiring payments to be made to the Exchequer or any government department or to any local or public authority in consideration of any licence or consent or of any services to be rendered, or prescribe the amount of any such charge or payment;
 - (f) purport to have retrospective effect;
 - (g) give rise to doubts whether they are *intra vires*;
 - (h) require elucidation, are not written in plain English, or appear to be defectively drafted; or
 - (i) appear to be incompatible with any obligation resulting from membership of the European Union;
 - (j) prevent any person from continuing to exercise any right or freedom which he might reasonably expect to continue to exercise;
 - (k) satisfy the conditions of proportionality between burdens and benefits set out in sections 1 and 3 of the Act;
 - (l) satisfy the test of desirability set out in section 3(2)(b) of the Act;
 - (m) have been the subject of, and take appropriate account of, estimates of increases or reductions in costs or other benefits which may result from their implementation; or
 - (n) include provisions to be designated in the draft order as subordinate provisions; and in the case of the latter consideration the committee shall report its opinion whether such a designation should be made, and to what parliamentary proceedings any subordinate provisions orders should be subject.
7. The Committee in the House of Lords will consider each proposal in terms of similar criteria, although these are not laid down in Standing Orders.
8. Each Committee might take oral or written evidence to help it decide these matters, and each Committee could then be expected to report:
- whether the Minister should proceed to lay a draft order in the same terms as the original proposal, or
 - whether amendment is necessary, or
 - whether the order-making power should not be used (for example, because of the significance or sensitivity of the proposal).

Copies of Committee Reports, as Parliamentary papers, can be obtained through HMSO. They are also made available on the Parliament website at

- <http://www.parliament.uk/commons/selcom/drghome.htm> for the Deregulation and Regulatory Reform Committee in the Commons; and
 - <http://www.parliament.the-stationery-office.co.uk/pa/ld/lddereg.htm> for the Delegated Powers and Regulatory Reform Committee in the Lords.
9. After the 60 days for Parliamentary consideration, the Minister can lay a draft order before both Houses, this time for the approval of Parliament.
 10. Each of the Scrutiny Committees examines the draft order to see how far its views have been taken into account. They report, within 15 sitting days, whether the draft order should be approved or not, and it would then be for the relevant House itself to take its final decision.
 11. The final draft order then has to be approved by both Houses of Parliament before becoming law.

How To Make Your Views Known

12. Responding to this consultation document is your first and main opportunity to make your views known to the relevant department as part of the consultation process. You should send your views to the person named in the consultation document, in this case Michael Lines, Maritime and Coastguard Agency, Bay 2/1, Spring Place, 105 Commercial Road, Southampton, SO15 1EG. When the Minister lays proposals before Parliament you are welcome to put your views before either or both of the Scrutiny Committees.
13. In the first instance, this should be in writing. The Committees will normally decide on the basis of written submissions whether to take oral evidence.
14. Your submission should be as concise as possible, and should focus on one or more of the criteria listed in paragraph 6 above.
15. The Scrutiny Committees appointed to scrutinise Regulatory Reform Orders can be contacted at:

Delegated Powers and
Regulatory Reform Committee
House of Lords

Deregulation and Regulatory
Reform Committee
House of Commons

London
SW1A 0PW
Tel: 0207 219 3103
Fax: 0207 219 2571
email: DPDC@parliament.uk

7 Millbank
London
SW1P 3JA
Tel: 020 7219 2830/2833/2837
Fax: 020 7219 2509
email: deregcom@parliament.uk

Non-disclosure of responses

16. Section 7 of the Act provides what should happen when someone responding to the consultation exercise on a proposed order requests that their response should not be disclosed.
17. The name of the person who has made representations will always be disclosed to Parliament. If you ask for your representation not to be disclosed, the Minister should not disclose the content of that representation without your express consent and, if the representation relates to a third party, their consent too. Alternatively, the Minister may disclose the content of the representation in such a way as to preserve your anonymity and that of any third party involved.

Information about Third Parties

18. If you give information about a third party which the Minister believes may be damaging to the interests of that third party, the Minister does not have to pass on such information to Parliament if he does not believe it is true or he is unable to obtain the consent of the third party to disclosure. This applies whether or not you ask for your representation not to be disclosed.
19. The Scrutiny Committees may, however, be given access on request to all representations as originally submitted, as a safeguard against improper influence being brought to bear on Ministers in their formulation of regulatory reform orders.

ANNEX B

List of Consultees

All registered credit unions (circa 700)

ACE Credit Union Services
Adams and Co
Aird Sakol, Chartered Accountants
Alexander Sloan & Co.
Appleby and Wood
Association of British Credit Unions Ltd
Association of British Credit Unions Ltd (Scotland)
Association of Friendly Societies
Association of Independent Credit Unions Ltd
Bailey Page & Roper
Bar Council
Beever & Struthers Chartered Accountants
Birmingham Credit Union Development Agency
Blythe Valley Credit Union Development Group
Bolton Neighbourhood Economic Development
Bradford Credit Union Development Agency
Braintree Credit Union Development Agency
Bridgwater Credit Union Ltd
Bristol and Avon Community Enterprise Network
British Bankers Association
Building Societies Association
Carlisle City CU Study Group
Chown Hugh
Clarks Louis Pearlman
Coalfield Community Economy Project
Confederation of British Industry
Consumers Association
Co-operative Bank Plc
Co-operative Union
Cornish Credit Union Development Project
Coventry & Warwickshire CUDA
Cranhill Credit Union Ltd
Credit Union Development Initiative Middlesborough
Credit Union Enterprise Services
Dacorum Borough Council Community Department
Derby Credit Union Development Agency
Derwentside Credit Union Development Agency

Devon Co-active Development Agency Limited
Doncaster Community Liason Department
Dudley Credit Union Development Agency
Dumfries Credit Union Development Agency
Durham Co-operative Development Association Limited
East Midlands CU Development Agency
Ernst & Young
Federation of Small Business
Financial Services Authority
GMB (Lancs Region) Credit Union Ltd
Greenwich Credit Union Development Agency
Hackney Credit Union Development Agency
Hallidays
Harlow Credit Union Development Agency
Harrison Jones & Co
Hartlepool Credit Union Project
Haslingden & Helmshore Credit Union Ltd
Heaton, Lumb Lisle
Herefordshire and Worcestershire Credit Union
Home Housing Association
Hull Credit Union Development Project
Isle of Wight Rural Community Council
Institute of Directors
Lancashire Co-operative Development Agency Ltd
Law Department, Leicester University
Law Society
Leeds Credit Union Development Agency
Leicester & County Co-operative Development Agency
Leicester University Law Department
Liverpool Credit Union Development Team
Llanrumney Credit Union Development Project
Local Government Association
Lothian Region Credit Union Development Agency Ltd
Mark Donovan
Milton Avis
National Assembly for Wales
National Association of Citizen's Advice Bureau
National Association of Credit Union Workers
NCVO
Newcastle Credit Union Development Agency
Newcastle Credit Union Project
Norman Gray & Co
Northern Ireland Assembly

North Tyneside Council Community Services
Nottingham Credit Union Development Agency
Nottinghamshire CC Centre for Economic Development
Nottinghamshire Credit Union Development Network
Oxfordshire Credit Union Development Agency
Pannell Kerr Forster
Patricia Bradley
Paul Jones, Liverpool John Moores University
People for Action
Performance and Innovation Unit, Cabinet Office
Ralph Swoboda
Raymond McKeag, Registrar, Northern Ireland
Redditch Credit Union Development Agency
Registry of Friendly Societies
Renfrewshire Credit Union Development Agency
Rhodes Clark & Co
Rotherham Credit Union Development Agency
Royal Bank of Scotland
St Columbas Credit Union Ltd
Sally Anderson
Sandwell Credit Union Development Agency Limited
Scottish Executive
Scottish League of Credit Unions
Scottish Transport Workers Credit Union Ltd
Scotwest Credit Union Ltd
Sefton Credit Union Development Agency
Sheffield Credit Union Development Agency
Social Enterprise London
Social Enterprise Unit, DTI
Social Exclusion Unit, Cabinet Office
Southampton Area Co-operative Development Agency
Southwark Credit Union Development Agency
St Helens Credit Union Development Agency
Stanley V Bye and Co
Stockton Credit Union Development Agency
Strathclyde Credit Union Development Agency
Swansea City Credit Union Project
The Kelvin Partnership
Trade Union Congress
UK Co-operative Council
Unity Trust Bank
VOSE
W. P. Johnston, Chartered Accountant & Registered Auditor

Wales Co-operative Development and Training Centre
Walsall Credit Union Development Agency Limited
West Cumbria Credit Union Development Project
Wigan Community Credit Union Development Agency
Wirral Credit Union Resource Centre
Wolverhampton Credit Union Development Agency
Wrekin Credit Union Development Agency
Yvonne Gallacher

ANNEX C

THE CABINET OFFICE CODE OF PRACTICE ON CONSULTATION

The criteria in the Code of Practice on Consultation apply to all UK national public consultations on the basis of a document in electronic or printed form. These are reproduced below:

1. Timing of consultation should be built into the planning process for a policy (including legislation) or service from the start, so that it has the best prospect of improving the proposals concerned, and so that sufficient time is left for it at each stage.
2. It should be clear who is being consulted, about what questions, in what timescale, and for what purpose.
3. A consultation document should be as simple and concise as possible. It should include a summary, in two pages at most, of the main questions it seeks views on. It should make it as easy as possible for readers to respond, make contact or complain.
4. Documents should be made widely available, with the fullest use of electronic means (though not to the exclusion of others), and effectively drawn to the attention of all interested groups and individuals.
5. Sufficient time should be allowed for responses from all groups with an interest. Twelve weeks should be the standard minimum period for a consultation.
6. Responses should be carefully and open-mindedly analysed, and the results made widely available, with an account of the views expressed, and reasons for decisions taken.

Departments should monitor and evaluate consultations, designating a consultation co-ordinator who will ensure that the lessons learned are disseminated.

Annex D

Partial Regulatory Impact Assessment

CREDIT UNIONS

PUBLIC CONSULTATION

Proposed amendments to the Credit Union Act 1979 – Regulatory Impact Assessment

Overview

1. The Government strongly supports credit unions' ethos of thrift and self-help, and has been involved in a number of initiatives to help the sector to grow, thereby increasing their ability to widen access to financial services, particularly among the least well-off.

2. In April 2001, Government introduced two deregulatory changes to assist credit unions to develop their businesses. This RIA concerns Government's proposals for seven further changes to the Credit Unions Act 1979, which are designed to help credit unions to compete for deposits, and to develop their role as complementary financial institutions. The changes are:

Proposal	Change
A	Allow credit unions to borrow money from external sources, other than authorised banks and other credit unions.
B	Allow credit unions to differentiate between certain accounts by paying dividends at different rates, and to pay dividends more than once each year.
C	Allow credit unions to provide additional basic services and charge fees (e.g. bill payments).
D	Make the common bond requirements more flexible.
E	Establish appropriate regulation on the use of the name Credit Union.
F	Change the minimum coverage requirements for fidelity bonds.
G	Allow credit unions to offer accounts that may be held in the name of more than one member.

3. These proposals are generally distinct from those changes that are due to be introduced when Financial Services Authority (FSA) commences its regulation of credit unions on 1 July 2002. They are, however, intended to complement the new regulatory regime.

The purpose and benefit of the Regulations

4. These regulations are designed to reduce certain restrictions on credit unions' operational powers. The changes bring the regulation of credit unions more into line with that for other deposit-takers, and are intended to help credit unions develop into more competitive providers of financial services, and to help the movement grow.

CHANGE PROPOSED		BENEFIT
A	Remove the restrictions that currently prevent credit unions from borrowing money from external sources, other than authorised banks and other credit unions, so they may borrow from whomever they choose.	A material increase in the range of potential sources of credit, which would enable credit unions to shop around for loans at more competitive rates and on more advantageous terms. It would also enable credit unions to borrow from any local community based source with altruistic reasons for lending at a particularly low rate of interest.
B	Allow credit unions to differentiate between the accounts they offer, by paying dividends at different rates, and to pay dividends more than once each year.	This change levels the playing field between credit unions and other deposit takers. By giving higher returns on certain accounts, credit unions should be able to attract a larger number of investors that only wish to benefit from the savings side of a credit union's business, while simultaneously securing a larger pool of money to support loans for those who wish to borrow.
C	Allow credit unions to charge for the provision of ancillary services – money transmission, issuing and administering means of payment, and bill payments – on a cost recovery basis.	Individuals can save by paying utility bills by automatic credit transfer. Allowing credit unions to recover the cost of ancillary services is likely to increase the number of credit unions that actually offer bill payment services, thus increasing the number of people with access to the benefit of cheaper utility services.

D	Make the common bond requirements more flexible, by permitting the combination of the associational common bond – which enables those people who have an association with a particular organisation to form a credit union – with all other types.	This change would increase the number of permutations that are available to credit unions that wish to merge.
E	Establish appropriate regulation on the use of the name Credit Union.	Controlling the use of the name “credit union” should enable FSA to ensure it is not used inappropriately or in a way deliberately designed to mislead, particularly where misuse could damage the reputation of the movement.
F	Change the minimum coverage requirements for fidelity bonds.	This change would add a new upper threshold to the minimum fidelity bond cover calculation, which should benefit all credit unions with share capital above £1 million through lower cost bond premia.
G	Remove any doubt that credit unions may offer accounts held in the name of more than one member i.e., joint accounts.	This change would enable credit unions to offer a savings vehicle for use by couples, which may be of particular value for those people who find the additional discipline of joint savings helpful.

Businesses Affected

5. British credit unions, registered under the Industrial & Provident Societies Act 1965, and which comply with the requirements referred to in section 1 of the Credit Unions Act 1979. Given the particular nature and origins of credit unions, separate legislation applies in Northern Ireland. There are currently around 700 credit unions registered in Britain, with new registrations averaging around 50 a year. Total assets are now over £200 million and are continuing to grow by about £20 million each year. In 2000, credit unions made loans to a value of £160 million, and in 2001 membership topped 300,000.

6. All credit unions would be able to take advantage of proposals A, C, D, E, F & G to the extent that they may wish to do so. However, the ability to take advantage of the changes under proposal B will be limited to a similar group of credit unions to

those that are subject to FSA Rules Version 2 (under which FSA need to be satisfied that there are appropriate policy manuals documenting the systems, and committees in place to manage the functions - in loans and internal audit/supervisory committees).

Compliance Costs

7. Government plans to introduce the new regulations on 1 July 2002, or as soon thereafter as is practicably possible, to coincide with the commencement of Financial Services Authority's (FSA) new regulatory regime.

8. Credit unions are currently registered by the Registry of Friendly Societies (RFS), and regulated on behalf of RFS by FSA, under the terms of a service level agreement. The cost of regulation is met through a menu of individual charges for different services, levied according to use.

9. An important change that regulation by FSA will introduce is that credit unions will pay a single annual charge, covering the cost of regulation, and their membership of the Financial Services Ombudsman and Compensation schemes.

10. FSA's new single annual charge regime will be in place by the time these changes are introduced, which means that the cost to credit unions of securing any necessary rule changes or other permissions, will be nil.

11. While credit unions may still be required to register certain rule changes, necessary if they are to take advantage of some of these proposals, FSA's single annual charge will cover the cost of registering such changes, which means they will no longer face one-off additional charges for such registration services.

12. For proposal B, which require authorisation under FSA Rules Version 2, credit unions will only need to make a single application to cover these new powers. Where a credit union is already operating under Version 2 Rules, it will not be required to apply for further authorisation, but may be required to inform FSA that it proposes to adopt further powers.

PROPOSAL	COMPLIANCE COST
A	Nil.
B	None, although required to be regulated subject to FSA Rules Version 2. One-off registration of a rule change may also be required.
C	None, although the one-off registration of a rule change may be required.
D	None. However, still need to obtain permission from FSA to extend or amend a common bond.
E	Nil.
F	Nil.
G	None, although the one-off registration of a rule change may be required.

Benefits

PROPOSAL	BENEFIT
A	Material increase in credit unions' range of potential sources of credit, including local community based source with altruistic reasons for lending at a particularly low rate of interest, enabling them to shop around for loans at more competitive rates and on more advantageous terms the benefits of which may be returned to members in the form of higher dividend payments.
B	Ability to compete for deposits by offering to pay higher returns on savings-only accounts, thereby attracting a higher number of saver-only investors, whose deposits may in turn be loaned to those members who wish to borrow.
C	Allowing credit unions to recover the cost of ancillary services should increase the number of credit unions that actually offer bill payment services, thus increasing the number of people with access to the benefit of cheaper utility services through ACT.
D	This change would increase the number of permissible types of credit unions that may merge.
E	Protection against inappropriate or deliberate misuse of the name "credit union", which might damage the reputation of the movement.
F	Credit unions with share capital above £1 million should benefit through lower cost bond premia.
G	Provision of a distinct savings vehicle for those people who find the additional discipline of joint savings helpful.

Impact on small businesses

PROPOSAL	SMALL CREDIT UNIONS	LARGE CREDIT UNIONS
A	Equal impact on both large and small credit unions.	
B	None – only open to a similar group of credit unions to those that are subject to FSA Rules Version 2.	Ability to compete for deposits by offering higher returns on savings-only accounts.
C	Equal impact on both large and small credit unions.	
D		
E		
F	None.	Credit unions with share capital above £1 million should benefit through lower cost bond premia.
G	Equal impact on both large and small credit unions.	

Consultation with the industry

13. These changes were set out in the Treasury's consultation paper Proposed Amendments to the Credit Unions Act 1979, which was published in October 2001.

Compliance, Enforcement and Monitoring

PROPOSAL	COMPLIANCE
A	Permissive only. However, external borrowing will be monitored by FSA as part of their prudential regulation of credit unions, both in terms of cost and exposure. FSA would therefore have the capacity to intervene should poor or reckless borrowing decisions by a credit union give rise to any concern about its general financial position.
B	Permissive only, and limited to a similar group of credit unions to those that are subject to FSA Rules Version 2. Also likely to require a rule change before such credit unions may take advantage of this proposed change. Furthermore, dividend payments will be monitored by FSA as part of their prudential regulation of credit unions.
C	Permissive only, and likely to require a rule change before such credit unions may take advantage of this proposed change. In addition, charges for ancillary services are likely to be monitored by FSA as part of their prudential regulation of credit unions.
D	Credit unions will need to obtain permission from FSA should they wish to extend or amend their common bond.
E	This change would enable FSA to challenge through the courts any individual or organisation that it came to notice was, in its opinion, illegally using the name "credit union".
F	None required.
G	Permissive only, and likely to require a rule change before such credit unions may offer joint accounts.

ANNEX E: Parliamentary Answers and Statements

7 Dec 1999: Column: 522W

Credit Unions

Mr. Gordon Prentice: To ask the Chancellor of the Exchequer what steps he is taking to encourage the establishment and development of credit unions. [101727]

Miss Melanie Johnson: Two reports were published on 16 November which include moves to boost credit unions. The report by the Credit Unions Taskforce, under the chairmanship of Fred Goodwin, investigated ways in which banks and building societies could help credit unions, and the report by the Policy Action Team looked at ways to improve individual access to financial services.

There will be a new central services organisation for credit unions to help them to deliver a more consistent and flexible service to members. Improved regulation by the Financial Services Authority will ensure that credit union members enjoy similar protection to savers in banks and building societies. A number of deregulatory measures, including increasing the maximum repayment periods for loans, removing the maximum membership limit and allowing credit unions to charge for ancillary services will also be implemented.

Westminster Hall

Wednesday 18 July 2001

Credit Unions

Ruth Kelly: The Treasury's role is to help create the right conditions for credit unions to expand. Earlier this year, we introduced two changes to give credit unions greater freedom. We increased the maximum loan repayment periods that credit unions may offer borrowing members, and we increased the amount that junior members may save with a credit union, bringing it into line with the amount that adults may save. *(two of the original 1998 proposals)*

We shall also be introducing a further package of three deregulatory changes, when the relevant sections of the Financial Services and Markets Act 2000 are brought into effect on 1 July 2002. The forthcoming changes will abolish the maximum limit on the number of members a credit union may have, and abolish the statutory distinction between the large credit unions that are able to take advantage of the additional powers conferred by a section 11C certificate, and other credit unions. They will also abolish the requirement on credit unions to dispose of repossessed collateral as soon as possible. *(the latter is the third 1998 proposals to already have been done.)*

We also plan to consult on a range of further measures aimed at relaxing some of the restrictions on credit unions' operational powers. This exercise will include a number of proposals that have been put forward by the sector, many of which remove or reduce legislative constraints, and which will also include some of the proposals that my hon. Friend the Member for Harrow, West made today.

I know that these measures are eagerly awaited in the movement, and I am keen that we make progress with the assembly of a package of measures for public consultation as soon as possible. I am also aware that it would be helpful to introduce those deregulatory changes that consultees consider desirable at the same time as the Financial Services Authority commences its regulation of credit unions, next year. A great deal of work still needs to be done before we can release the consultation document, but I hope that we shall be in a position to start the consultation process before the end of the summer.

ANNEX F

1998 consultation document proposals.	2001 consultation document proposals
Amend section 10 to allow credit unions to borrow from authorised institutions (building societies, insurance companies, friendly societies), Local Authorities, and organisations that fall within the common bond, in addition to their existing powers to borrow from banks and other credit unions.	Amend section 10 to completely remove the restrictions that currently prevent credit unions borrowing from whomever they choose.
Amend section 8(1) to specify that shares may be held in either interest bearing or dividend accounts. Amend section 14 to permit the payment of interest, which may not exceed three-quarters of the current maximum rate set in section 14(4) - currently 8% - which applies to dividend share accounts.	Amend section 14 to allow credit unions to pay dividends at different rates, and to offer different dividends on different accounts, and to declare such dividends more than once each year.
Derogate from section 1(2)(a) to allow credit unions to add, as an object, the provision of chargeable ancillary services: money transmission, issuing and administering means of payment, and bill payments.	Derogate from section 1 (2)(a) to allow credit unions to charge for the provision of ancillary services – money transmission, issuing and administering means of payment, and bill payments – on a cost recovery basis.
Abolish the limit on the maximum amount that can be held in youth accounts (currently £750) and lower the minimum age for joining a credit union, (without conferring voting rights).	Achieved through secondary legislation.
To add to the list in Section 1(4) common bonds combining category (e) – the associational common bond - with the other four types: (a) following a particular occupation; (b) residing in a locality; (c) being employed in a particular locality; and (d) working for a particular employer	To further extend Section 1(4) to permit the combination of category (e) - the associational common bond - with all other types.

<p>Remove the current 5,000 maximum membership limit: Repeal sub-sections (3), (4) and (6) of section 6, and amend subsection (5) so that obtaining a Section 11C certificate meets the requirement for exemption from the 5000 limit.</p>	<p>Dealt with under Financial Services & Markets Act 2000, and due to come into force on 1 July 2002.</p>
<p>Require credit unions to dispose of any land in which they acquire an interest within three months or in such other period as may be approved –for individual credit unions or case-by-case - by the registrar.</p>	<p>Dealt with under Financial Services & Markets Act 2000. However, the timing of this repeal has not yet been finalised.</p>
<p>Proposal: To increase the re-payment period for loans: secured lending to twelve years for credit unions holding Section 11C certificates, and seven years otherwise. unsecured lending to five and three years respectively</p>	<p>Achieved through secondary legislation.</p>
<p>No equivalent proposal.</p>	<p>Replace Sections 3(2) and 3(3) with form of words that would give the name “credit union” protection in law, while offering sufficient flexibility to enable the members of credit unions based outside Britain to use the name when operating in Britain</p>
<p>No equivalent proposal.</p>	<p>Amend wording of sections 5 and 7 to remove any doubt that credit unions may offer joint accounts.</p>
<p>No equivalent proposal.</p>	<p>A new threshold, together with ceilings for bond minimum limits are proposed, as amendments to Section 15(2)(b), which prescribes the current levels of cover required.</p>