

**EXPLANATORY MEMORANDUM TO THE
FINANCIAL SERVICES AND MARKETS ACT 2000 (COLLECTIVE INVESTMENT
SCHEMES) (AMENDMENT) ORDER 2005**

2005 No. 57

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

2. Description

2.1 This instrument amends the Schedule to the Financial Services and Markets Act 2000 (Collective Investment Schemes) Order 2001 (“**the Principal Order**”) which sets out the arrangements that are not to be regarded as collective investment schemes for the purposes of the Financial Services and Markets Act 2000 (“**FSMA**”).

2.2 Paragraph 7 of that Schedule excludes certain funds relating to leasehold property. The purpose of the amendment to be made by this instrument is to extend this exclusion to arrangements where the rights or interests of the participants are not rights or interests in a “trust fund” (as defined in section 42(1) of the Landlord and Tenant Act 1987 (“**LTA**”)), only because the landlord is an “exempt landlord” (as defined in section 58(1) of the LTA).

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

None.

4. Legislative Background

4.1 FSMA makes provision for the regulation of financial services and markets, including regulation by the Financial Services Authority (“**FSA**”) of certain types of arrangements with respect to property known as “collective investment schemes”.

4.2 Collective investment schemes are defined in section 235 of FSMA.

4.3 Section 235(5) of FSMA empowers the Treasury to provide that arrangements do not amount to collective investment schemes if, for example, they fall within a specified category of arrangement. The Treasury made the Principal Order under these powers.

4.4 The Principal Order provides that arrangements of the kind specified in its Schedule do not amount to collective investment schemes. Paragraph 7 of the Schedule specifies arrangements where “the rights or interests of the participants are rights or interests in a fund which is a trust fund within the meaning of section 42(1) of the Landlord and Tenant Act 1987”.

4.5 Section 42 of the LTA requires that certain sums relating to service charges to which tenants of leasehold property have contributed be held in a trust fund

(within the meaning of section 42(1)) by the landlord or other person to whom any such charges are payable. However, that section does not apply in the case of any tenants of an “exempt landlord” within the meaning of section 58(1) of the LTA. An “exempt landlord” within the meaning of section 58(1) includes a landlord who is a local authority or one of the other bodies specified in that subsection.

4.6 As a result of the combined operation of sections 42 and 58(1) of the LTA, arrangements where the rights or interests of the participants are not rights or interests in a fund which is a “trust fund” (within the meaning of section 42(1)) because the landlord is an “exempt landlord” (within the meaning of section 58(1)) do not fall within paragraph 7 of the Schedule to the Principal Order.

4.7 This instrument has been made to rectify this unintended effect of the legislation.

5. Extent

This instrument applies to all of the United Kingdom.

6. European Convention on Human Rights

Not applicable.

7. Policy background

7.1 The purpose of the Principal Order is to specify arrangements that the Government does not intend the FSA to regulate under FSMA.

7.2 Paragraph 7 of the Schedule to the Principal Order is intended to exclude arrangements where the rights or interests of the participants are rights or interests in a “trust fund” within the meaning of section 42(1) of the LTA. This reflects the policy objective of not subjecting such funds, or those who operate them, to regulation by the FSA.

7.3 Certain categories of landlord are exempt, under section 58(1) of the LTA, from the requirement in section 42 to hold on trust certain funds to which tenants have contributed. However, some “exempt landlords”, such as housing associations regulated in England, do hold such funds on trust in compliance with the regulatory code that applies to them, and, in some cases, the terms of their lease agreements. It is also possible that other “exempt landlords” under section 58(1) operate such funds, notwithstanding the fact that they are not legally required to do so under section 42 of the LTA.

7.4 At present, the policy objective of not subjecting such funds to regulation by the FSA is not borne out by the operation of the legislation. Paragraph 7 of the Schedule to the Principal Order appears to have been drafted on the basis that if “exempt landlords” under section 58(1) of the LTA are not statutorily required to hold tenants’ funds on trust, they would not for any other reason do so.

7.5 However, with particular regard to registered social landlords, the existence of the regulatory code, and (in some cases) the terms of their lease agreements, has created a situation in which arrangements that are not intended to be collective investment schemes for the purposes of FSMA could nevertheless be so. More

generally, if any of the other categories of “exempt landlord” set out in section 58(1) of the LTA were, for any reason, to operate such arrangements notwithstanding their exemption from the section 42 LTA legal requirement to do so, they too could be operating collective investment schemes.

7.6 The impact on registered social landlords, as well as any other category of “exempt landlord” that holds funds to which tenants have contributed on trust (either presently or at some point in future), is potentially serious. Such bodies could be inadvertently and unlawfully operating collective investment schemes and subject to regulatory action by the FSA. An additional concern is that as a result of this uncertainty, courts find lease agreements between “exempt landlords” and their tenants to be unlawful and unenforceable.

7.7 Therefore, in order to ensure the Government’s policy not to subject to regulation by the FSA under FSMA arrangements (or the operators of arrangements) which would be arrangements of the type described in section 42(1) of the LTA but for the fact that the landlord is an “exempt landlord” within the meaning of section 58(1), the Government is proposing this amendment to the Principal Order.

7.8 In preparing this proposal we have consulted the Office of the Deputy Prime Minister and the FSA, and they agree with this approach.

8. Impact

8.1 A Regulatory Impact Assessment has not been prepared for this instrument as it has no impact on business, charities or voluntary bodies.

8.2 The impact on the public sector is to ensure that local authorities and certain other bodies (as set out in section 58(1) of the LTA) that act as landlords and operate trust funds equivalent to those described in section 42 of the LTA, notwithstanding no legal requirement to hold such funds on trust, are not operating “collective investment schemes” for the purpose of FSMA, so are not subject to regulation by the FSA.

9. Contact

Alexandra Hale at HM Treasury Tel: 020 7270 5079 or e-mail: Alexandra.Hale@hm-treasury.gov.uk can answer any queries regarding the instrument.