

These notes refer to the Building Societies (Funding) and Mutual Societies (Transfers) Act 2007 (c.26) which received Royal Assent on 23rd October 2007

BUILDING SOCIETIES (FUNDING) AND MUTUAL SOCIETIES (TRANSFERS) ACT 2007

EXPLANATORY NOTES

COMMENTARY ON SECTIONS

Section 1: Funding limit for building societies

10. Subsection (1) amends section 7 of the Building Societies Act 1986 (“the 1986 Act”) to make it possible for the Treasury to change the funding limit for building societies.
11. New subsection (6A) enables the Treasury to make an order providing that the limit on non-member funding in section 7(1) has effect as if the current limit of 50% were a greater amount, up to a maximum of 75%, specified in the order. The order may also prohibit societies from applying the increased percentage unless they have passed a resolution of the kind specified in the order.
12. New subsection (6B) provides that an order under subsection (6A) is of no effect unless there is also an order in place under new section 90B, giving members equality with creditors in dissolution and winding up. This aims to protect the position of members: if no order were made under s.90B, an increase in wholesale (non-member) funding would put them at greater risk in the event of an insolvency, as funds would be used to satisfy a larger pool of creditors first.
13. New subsection (6C) provides that an order under subsection (6A) may not be amended or revoked if the effect is to reduce the percentage specified in the order. The purpose is to ensure that the funding limit, once increased, cannot be reduced. If the Treasury were able to raise the funding limit and later reduce it, that could deter building societies from taking advantage of the raised funding limit. There would be no certainty that they could continue to use that amount of wholesale funding in the future.
14. New subsection (8A) requires an order under subsection (6A) to be approved in draft by affirmative resolution in each House of Parliament before it is made.
15. Subsection (2) amends section 5 of the 1986 Act, which requires the purpose or principal purpose of a building society to be that of making loans secured on residential property which are funded substantially by its members.
16. New subsection (11) gives the Treasury a power to amend section 5(1)(a) of the 1986 Act so as to alter the extent to which loans are required to be funded by the society’s members. This will ensure that the requirement in section 5 is consistent with the revised funding limit, as that will allow societies to have less member funding.
17. New subsections (12) and (13) give the Treasury a power to make consequential, saving, supplementary or transitional provision. This includes provision amending specified provisions of the Act, concerning the functions of the Financial Services Authority, amalgamations and societies’ memoranda. This will ensure that those sections are consistent with section 5 as amended.

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18. New subsection (14) requires an order made under the section to be approved in draft by affirmative resolution in each House of Parliament before it is made.

Section 2: Power to alter priorities on dissolution and winding up

19. This section inserts new section 90B into the 1986 Act. Subsection (1) gives the Treasury the power to make an order to ensure that, on the winding up or dissolution by consent of a society, any assets available to satisfy the society's liabilities to creditors or to shareholders are applied in satisfying those liabilities *pari passu* (equally). This power may be exercised independently of the section 1 power. An order under this section may make amendments of the 1986 Act, as well as consequential, supplementary, transitional and saving provision (subsection (5)).
20. Subsection (2) provides that liabilities to creditors do not include liabilities in respect of subordinated deposits, preferential debts, and any other category of liability specified by the Treasury. Subsection (3) makes a similar provision in respect of deferred shares. The purpose is to ensure that only ordinary shareholding members are given equality with the general pool of unsecured creditors.
21. Subsection (6) requires an order under new section 90B to be approved in draft by affirmative resolution in each House of Parliament before it is made.

Section 3: Transfers to subsidiaries of other mutuals

22. Subsection (1) gives the Treasury the power to modify provisions in the legislation identified in subsection (11), to facilitate, or in consequence of, a transfer of business from a mutual society to the subsidiary of another mutual society.
23. The legislation which may be modified under this section specifies the procedures for transfers of business of building societies, friendly societies and industrial and provident societies (subsection (11)). So any modifications will only affect transfers made by one of those types of society.
24. A transfer under the modified procedures may be made to a subsidiary of a building society, friendly society or industrial and provident society, or to a subsidiary of an EEA mutual society (subsections (1) and (10)). An EEA mutual society is a European Cooperative Society, a cooperative under the law of an EEA (European Economic Area) state, or a cooperative or mutual undertaking of such description as the Treasury specify by order (subsection (12)).
25. A subsidiary of a mutual society is a relevant company in which the society holds or controls a majority of the voting rights and in relation to which the society can appoint or remove a majority of the board of directors (subsection (13)). A relevant company is a UK company or a body incorporated in another EEA state (subsection (14)).
26. The inclusion of EEA mutual societies in section 3 ensures that any changes made under the Act to the legislation specified in subsection (11) apply where the transfer is to a subsidiary of an EEA mutual as well as where the transfer is to a subsidiary of a UK building society, friendly society or industrial and provident society. Mutual insurers, and other UK mutual undertakings, could come within the scope of "EEA mutual society".
27. Subsection (2) specifies that the order may make provision concerning certain rights, including membership rights, in the mutual society controlling the subsidiary. This will enable the Treasury to require that members of the transferring mutual society, and new customers of the subsidiary, are given equivalent rights to those they would have enjoyed as members of the transferring mutual.
28. Subsection (3) provides that the order may confer functions on the Financial Services Authority. Those functions might for example include a power to direct that, in certain circumstances, restrictions on transfers of shares in the new subsidiary, or transfers of

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its business, will not apply. The Authority has a similar power under s.101(4) of the Building Societies Act 1986.

29. Subsections (6) and (7) provide that an order which modifies the primary legislation identified in subsection (11), or which modifies subsection (13), must be approved in draft by affirmative resolution of each House of Parliament before it is made. An order which does not modify those provisions will be subject to annulment by a resolution of either House. This allows an order which modifies subordinate legislation only to be made under the negative resolution procedure. An order specifying a new kind of EEA mutual may also be made under the negative resolution procedure.
30. Subsection (8) ensures that any order made under section 3 which may have effects peculiar to a particular mutual will not be dealt with under the hybrid instrument procedure in the House of Lords. As EEA mutual societies are included in subsection (10), it is possible that an order under section 3 could require an EEA mutual society acquiring a UK mutual society to give transferring members full membership rights in the EEA mutual. If the EEA mutual has a unique legal form, for example if it is established by a private Act of Parliament, that might raise a question of hybridity. This provision ensures that the hybrid instrument procedure will not apply, should such a situation arise.
31. Subsection (15) enables the Financial Services Authority to charge fees in respect of any functions conferred on it under the Act. It extends the FSA's existing powers to charge fees under the Financial Services and Markets Act 2000. The inclusion in section 3 of EEA mutual societies will require certain safeguards to be in place, equivalent to those applicable to domestic mutuals, regarding membership rights in the holding mutual and further demutualization. The FSA, which in most cases must approve transfers of UK mutual societies' business, will have to be satisfied that these safeguards are in place. If additional functions are conferred on the FSA in the order implementing the Act, it may need to charge fees in connection with those functions.

Section 4: transfers to subsidiaries: distribution of funds

32. This section has effect only if an order made under section 3 so provides (subsection (1)), and applies only to transfers to which the order applies (subsection (2)).
33. Subsection (3) provides that a distribution of funds which exceeds limits prescribed by the Treasury must be approved by the transfer resolution of the mutual society making the transfer, and by a resolution of the holding mutual of a kind specified by the Treasury. A distribution which does not exceed the prescribed limit must only be approved by the transfer resolution or by the resolution of the holding mutual.
34. A distribution of funds is a distribution of part of the funds of the transferring society, or of the holding mutual, in consideration of the transfer, among the members of the transferor, the holding mutual or both of them (subsection (2)). The transfer resolution is the resolution specified in subsection (5) which approves the transfer. The holding mutual is the mutual society of which the transferee is a subsidiary (subsection (2)).
35. Subsection (4) requires the Treasury to authorise such distributions and to prescribe limits. If an order made under section 3 gives effect to section 4, it will be necessary for the Treasury to authorise distributions and prescribe limits for subsection (3) of section 4 to work.
36. **Section 4** is similar to the provisions on distributions of funds on mergers of building societies in s.96(4) to (6) of the Building Societies Act 1986. An order implementing this section will create a less onerous procedure for distributions of funds in transfers to subsidiaries of other mutuals, in particular for distributions in transfers of building societies, which are currently limited to shareholding members of two or more years' standing under s.100(9) of the 1986 Act.

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37. Subsection (7) provides that subsections (4) to (7) of section 3 apply to an order made under section 4. This means that an order which only makes provision under subsections (3) and (4) of section 4 and does not modify primary legislation will be subject to the negative resolution procedure. However, the section 4 powers may be exercised at the same time as the section 3 powers in an affirmative resolution order.

Section 5: Channel Islands and Isle of Man

38. This section allows any provisions of the Act to be extended, with or without modifications, to any of the Channel Islands or to the Isle of Man. Some of the mutuals legislation which may be modified under the Act (see section 3(11)) either extends to the Islands or may be so extended.

Section 6: short title, commencement and extent

39. Subsection (2) provides for the Act to be commenced by one or more Treasury orders. Subsection (3) provides that the Act extends to the whole of the United Kingdom. However, as the Industrial and Provident Societies Act 1965 does not extend to Northern Ireland, any modifications to that Act made under section 3 will not extend there.