Peer to Peer Lending

Despite the recent increase in the Bank of England's base rate, interest rates available through mainstream banks and building societies, including cash ISAs, remain very low. With many years of low interest rates behind us and no expectations of significant increases in front of us, it is no surprise that many UK savers have been looking at alternatives.

One alternative which has been growing in popularity is 'peer to peer lending'. In simple terms, this type of arrangement is based around a 'platform' which introduces potential lenders to potential borrowers without the usual middle-men – the banks.

While a leading source of data on interest rates, Money Facts, quotes easy access savings accounts as paying a very unimpressive rate of 0.52% p.a., some peer to peer (P2P) arrangements are quoting rates in excess of 9% p.a. And, like cash deposits, it is possible to hold peer to peer accounts within an ISA structure so that the interest is tax free.

It is basic common sense that higher returns generally come at the cost of higher risk and P2P is no exception. Although some P2P arrangements will be lower risk than other P2P arrangements, they must all be seen as higher risk than actual cash deposits. It is possible to lose some or all of your loan and the financial services compensation scheme does not apply to P2P plans.

There are a number of platforms available, mostly aimed directly at consumers, and they all have some measures in place to mitigate the risks of loss. Generally there will be a maximum of any loan which will be allocated to a specific borrower, personal or corporate, and they generally undertake due diligence on the borrowers before accepting them onto the platform.

As mentioned, P2P plans can be held within an ISA wrapper. The rules for these 'Intelligent Finance' (IF) ISAs were introduced in 2016 but very few arrangements were able to market these as the underlying platforms required approval by the Financial Conduct Authority (FCA) which is the main financial services regulator. This was a time consuming exercise but most platforms have now met that requirement and it is estimated that around 31,000 IF ISAs were set up in the 2017/18 tax year, a massive increase over the previous year. That said, this is a mere drop in the ocean in comparison with the 10.6 million cash and stocks and shares ISAs opened in the same period. But it is clear that IF ISAs are moving into the mainstream.

At present, anyone can invest in a P2P plan, irrespective of their investment experience, wealth, or risk appetite. But the growth in the market has caused the FCA to look more closely at it. At the end of July the FCA issued a consultation paper, CP18/20, entitled "Loan-based ('peer-to-peer') and investment-based crowdfunding platforms". Despite the fact that the platforms are already approved by the FCA, this consultation proposes further regulation to control the operations of P2P platforms to reduce the risks to consumers. A number of specific risks are highlighted, including that they may:

- not be given clear or accurate information, leading to the purchase of unsuitable financial products
- not understand or be aware of the true investment risk they are exposed to
- not be remunerated fairly for the risks they are taking
- not understand what might happen if the P2P platform administering their loan(s) fails
- not understand the costs they are paying for the services the platform provides, or
- pay excessive costs for a platform's services

The FCA's paper highlights a number of changes which platforms could make to reduce risk. But they are also proposing limiting access to P2P plans to certain categories of investor:

- those who are certified or self-certify as sophisticated investors
- those who are certified as high net worth investors
- those who confirm before a promotion is made that, in relation to the investment promoted, they will receive regulated investment advice or investment management services from an authorised person, or
- those who certify that they will not invest more than 10% of their net assets in readily realisable securities

Whilst these proposed limitations may serve to prevent consumers who do not understand P2P from investing and limit the damage which a total loss would cause to an investor, feedback to date suggests that limiting access in this way would not prove popular.

Young people's savings

Child Trust Funds

Children born between 2nd September 2002 and 2nd January 2011 benefited from the Child Trust Fund (CTF) introduced by the Labour government as an attempt to encourage children to save. Between these dates, new born children were given a £250 voucher each to be held in a CTF with an additional £250 credited at age 7. Parents were given the opportunity to select the CTF but, if they didn't, government selected it for them. Additional contributions were permitted up to a current limit of £4,260 pa. There were eligibility requirements but, broadly, if parents qualified for child benefit in respect of the child then the CTF was available. And, CTFs had all of the same tax advantages as ISAs.

These accounts are administered by the parents until the child reaches age 16 at which stage the child takes over the administration, including selection of investment funds. There is no access to the investment until the child attains age 18.

The CTF was replaced by the 'Junior' ISA (JISA) in 2011 and this had broadly similar limits but, because it was an ISA, there were far more providers available and JISAs were cheaper than the CTF as well as having much wider investment options. The lack of access to the investment until the child attains age 18 was carried forward into the JISA regime. CTFs are no longer available although it remains possible to contribute to existing CTFs BUT it is not possible to have a CTF and a JISA for the same child. Of course, the big difference is that there are no government contributions towards a JISA.

So, why the history lesson? Well, it seems that nearly £1 million CTFs are 'lost' as families have lost paperwork or moved home without remembering to tell the CTF provider etc. And with the 'average CTF' being worth £650 (£500 from government and some growth) that's a lot of money unaccounted for. And, of course, the first cohort of CTF beneficiaries is now reaching age 16 and can/should be taking control of their accounts themselves. Of course, since there are no more funds coming into the account from government, this is also the time to think about transferring the CTF into a JISA, which has been possible since April 2015 in order to benefit from the generally lower costs.

If you are the parent of a CTF beneficiary and can't remember where it is – the CTF, not the child – the tax man can help as they have pretty complete records. HMRC has set up a 'find your CTF' service which requires signing into the Government Gateway www.gateway.gov.uk