GOUGH SQUARE CHAMBERS' CONSUMER CREDIT COLUMN: FEBRUARY 2016

This document is published by Practical Law and can be found at: uk.practicallaw.com/**5-622-9046**
Request a free trial and demonstration at: **uk.practicallaw.com/about/freetrial**

James Ross, Ruth Bala, Thomas Samuels and Lee Finch are all specialist consumer credit counsel at Gough Square Chambers. On a regular basis, they share their views with Practical Law Financial Services subscribers on topical developments or key issues relating to consumer credit.

In the February column, Ruth Bala considers the meaning of the phrase "carried on by way of business".

Ruth Bala, Gough Square Chambers

RESOURCE INFORMATION

RESOURCE ID

5-622-9046

RESOURCE TYPE

Article

PUBLISHED DATE

9 February 2016

JURISDICTION

United Kingdom

CARRIED ON BY WAY OF BUSINESS

Queries about the meaning of the phrase "carried on by way of business" are increasingly common, as prospective lenders seek to identify the ambit of FCA regulation.

Significance of carrying on a regulated activity by way of business

Section 22 of the Financial Services and Markets Act 2000 (FSMA) provides that an activity is a "regulated activity" if it is an activity of a specified kind that is carried on by way of business. Accordingly, an unauthorised person may enter into a regulated credit agreement or regulated mortgage contract without contravening the general prohibition, if they can show that the activity of lending was not carried on by way of business.

Those wishing to rely on this argument should be cautious, as the consequences of getting it wrong are serious. If an unauthorised person carries on a regulated activity, this is a criminal offence under section 23 of FSMA and renders the resulting credit agreements unenforceable, with any payments made by the borrower being recoverable (section 26, FSMA).

In some cases it will be clear that the lending is not by way of business (for example, a one-off loan from a family member). However, grey areas are common, for instance in peer-to-peer lending. In borderline business/non-business cases, it may be prudent to ensure that you possess an alternative argument that some exemption or exclusion applies.

For those relying principally on the non-business argument, it may provide some comfort that the phrase "by way of business" in section 22 of FSMA is narrower than the phrase "in the course of business" (see *Lomnicka & Powell Encyclopaedia of Financial Services Law p2A-99*). This means that in some cases, lending may occur "in the course of" another business operated by the lender, without the loan itself being "by way of" business. The test is whether the act of lending itself has the characteristics of a business.

FCA guidance

For borderline cases, a number of different factors will need to be weighed in deciding whether the loan is made by way of business. The FCA's view is that, in general, no single factor is likely to be conclusive. Further guidance on this is set out in the FCA's Perimeter Guidance manual (PERG), in particular, PERG 2.3.3G.

For certain regulated activities (for example, arranging and advising on regulated mortgage contracts, and debt-counselling carried on by charities), reference should be made to the Financial Services and Markets

Reproduced from Practical Law Financial Services with the permission of the publishers. For further information visit practicallaw.com or call 0207 542 6664. Copyright © 2016 Thomson Reuters (Professional) UK Limited. All Rights Reserved.

THOMSON REUTERS™

Act 2000 (Carrying on Regulated Activities by Way of Business) Order 2001 (*SI 2001/1177*) (Business Order). However, the Business Order is inapplicable to the activities of entering or administering credit agreements or mortgages.

In assessing whether lending is by way of business, the first relevant factor mentioned in PERG 2.3.3G is the degree of continuity. Two contrasting cases under other legislation are of note here:

- *Hare v Schurek [1993] CCLR 47.* It was held that one-off or occasional loans by a motor trader were not made in the course of his motor business for the purposes of section 74 of the Consumer Credit Act 1974 (CCA).

- *GE Capital Bank Ltd v Rushton [2006] 1 WLR 899*. It was held that an individual who purchased seven cars as a one-off transaction, with a view to resale at a profit, was carrying on a business of purchasing vehicles under the Hire Purchase Act 1964.

There was no "continuity" in either of these cases, yet diametrically opposed results were reached.

The second relevant factor is the existence of a commercial element. In the FCA's view (see PERG 4.3.9G and PERG 8.34.2G) "normally" an activity will not be by way of business unless the person is "expecting to gain a direct or indirect financial benefit of some kind". This financial benefit need not be profit – receipt of commission or transfer of benefit to a related company may suffice.

Difficulties arise where the lender operates in the charitable sphere. The lending will inevitably not be profitable, but if it is connected to the charitable body's aims it is arguably by way of business. On the other hand, pursuant to article 3E of the Business Order, a charity is regarded as carrying on debt-counselling, or debt-adjusting, by way of business if its own charitable activities consist of, or relate to, that activity, yet article 3E does not apply to the activity of lending by a charity. The omission of lending from article 3E could suggest that charitable lending will not normally be by way of business, subject to other factors.

The third relevant factor is the scale of the activity, such as (so that it is in contradistinction to the first factor) the size of the loan.

The fourth relevant factor is the "proportion" which the activity bears to other unregulated activities carried on. For instance, two loans advanced by a company with an ongoing clothing retail business are likely to be viewed very differently from two loans advanced by a special purpose vehicle, which was established specifically for the purpose of making those advances and is not really carrying on any other activities.

For further analysis of whether lending is by way of business, see *Helden v Strathmore Ltd [2011] CTLC 158 ([41]–[42])* and *Article, Gough Square Chambers' consumer credit column: September 2015 (www.practicallaw.com/8-618-5164)*.

For more information on carrying on regulated activities by way of business, see *Practice note, Carrying on regulated activities by way of business (www.practicallaw.com/7-201-8783)*.

Consequences of lending not being by way of business

If a person can establish that their lending is not by way of business, it follows that their lending is not a regulated activity. This means that they need not seek FCA authorisation, or find one of the exemptions or exclusions to rely upon. They are not committing a criminal offence under section 23 of FSMA and there is no prospect of their agreement being unenforceable under section 26 of FSMA.

Further, if the lending is not by way of business, the FCA's Consumer Credit sourcebook (CONC) will be inapplicable. This is because the phrase "by way of business" also appears in the FCA Glossary definition of the term "credit-related regulated activity". Equally, in respect of regulated mortgage contracts, the FCA's Mortgages and Home Finance Conduct of Business sourcebook (MCOB) will be inapplicable, as it only applies to a "firm", which is defined in the FCA Glossary as an "authorised person".

Reproduced from Practical Law Financial Services with the permission of the publishers. For further information visit practicallaw.com or call 0207 542 6664. Copyright © 2016 Thomson Reuters (Professional) UK Limited. All Rights Reserved.

It is important to remember that, even when not lending by way of business, the contract which is formed may nonetheless be a regulated credit agreement or regulated mortgage contract if it is not exempt. This is because the requirement for the activity to be carried on by way of business is only an element of the definition of a regulated activity, and not part of the definition of a regulated credit agreement or regulated mortgage contract.

Assuming no exemption is applicable, it will usually be possible for a lender in these circumstances to rely on section 74 of the CCA, which excludes "non-commercial agreements" from many CCA provisions, including the agreement form and content requirements. The scope of this partial exclusion is considered in *Article, Gough Square Chambers' consumer credit column: September 2015 (www.practicallaw.com/8-618-5164)*.

However, the test for non-commercial agreements is that the loan was not made "in the course of a business" carried on by the lender (section 189, CCA) and, as stated above, this phrase is somewhat wider than "by way of business". As a result, there may be situations where the lending is not "by way of" business (so that authorisation is not required), yet the loan is made "in the course of" the lender's business (so that it cannot be excluded as a non-commercial agreement). In such cases, the unauthorised lender would need to ensure that the loan was either exempt from the provisions of the CCA, or drafted as a CCA regulated loan.

Reproduced from Practical Law Financial Services with the permission of the publishers. For further information visit practicallaw.com or call 0207 542 6664. Copyright © 2016 Thomson Reuters (Professional) UK Limited. All Rights Reserved.