GOUGH SQUARE CHAMBERS' CONSUMER CREDIT COLUMN: JUNE 2017

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In the June column, Ruth Bala considers the interpretation of "consumer" in relation to consumer credit.

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IDENTIFYING THE "CONSUMER" IN CONSUMER CREDIT

Introduction

Despite starring both in the title to the Consumer Credit Act 1974 (CCA) and in its centrepiece concept of a "consumer credit agreement", there is no definition of "consumer" in the CCA. This is because consumer credit agreements are said to be agreements with "individuals", rather than agreements with consumers (*section 8(1), CCA*). As such, the borrower's purposes in seeking credit are not relevant to their identity as a CCA consumer. Nonetheless, the borrower's purposes often determine the applicability of consumer credit exemptions and protections and so the traditional concept of a consumer is drawn upon.

The "individual"

"Individuals" are defined in the CCA so as not only to include natural persons, but also certain small partnerships and unincorporated bodies (*section 189, CCA*). However, in the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (*SI 2001/544*) (RAO), the latter two entities are termed "relevant recipients of credit" and the term individual is restricted to natural persons (*article 60L, RAO*). The reason for this split is that under the RAO, while the borrower under a regulated credit agreement may be either an individual or a relevant recipient of credit (matching the CCA), the borrower under a "regulated mortgage contract" may only be an individual in this narrower sense (or trustees) (*articles 60B(3)* and *61(3), RAO*).

Notably, there is no requirement that the individual who enters a consumer credit agreement be a consumer as commonly understood, that is, acting for purposes outside their trade, business or profession. Indeed, the notion of a borrower is so divorced from the generally understood notion of a consumer, that the RAO includes deeming provisions to the effect that borrowers are to be "treated" as consumers for the purposes of interpreting the FCA's general consumer protection duties and consumer redress schemes (see *articles 60LA and 60S, RAO*).

As such, a borrower's purposes in seeking credit are not relevant to their superficial identity as a CCA or RAO consumer. However, the purposes of the borrower are often relevant to the applicability of exemptions or exclusions from regulation. The investment property loans exemption and second charge business loan exemption for regulated mortgage contracts, and the business purposes exemption for consumer credit agreements all share one condition in common: that the agreement is entered into by the borrower "wholly or predominantly for the purposes of a business carried on, or intended to be carried on, by the borrower" (*articles 60C(3) and 61A(6), RAO*). To benefit from these exemptions, the borrower must not be a consumer as commonly understood.

Even where a credit agreement is regulated, borrowers acting for business purposes cannot enjoy certain protections. Hirers acting for business purposes are generally deprived of the statutory right to terminate (*section 101(7), CCA*) and there is differential treatment of authorised business and non-business overdrafts. Significantly, the Consumer Credit Directive (*2008/48/EC*) (CCD) uses the traditional concept of consumer. Therefore, borrowers acting for business purposes cannot benefit from the CCA provisions added to implement the CCD (for example, section 55C of the CCA (copy of draft agreement), section 61A of the CCA (copies of agreement), section 75A of the CCA (connected liability) and section 77B of the CCA (statement of account upon request)). Such borrowers are also excluded from the scope of secondary legislation implementing the CCD (see the Consumer Credit (Agreements) Regulations 2010 (*SI 2010/1014*) and the Consumer Credit (Disclosure of Information) Regulations 2010 (*SI 2010/1013*)), although there is a means of "opt in".

As regards regulated mortgage contracts, certain provisions in the Mortgages and Home Finance Conduct of Business sourcebook (MCOB) in the FCA Handbook can be tailored if they were entered into by the individual for business purposes (*MCOB 1.2.3R*).

Finally, whether a borrower is a consumer determines whether terms and conditions in the credit agreement are reviewable for fairness under the Unfair Terms in Consumer Contracts Regulations 1999 (*SI 1999/2083*) (UTCCRs) (for contracts made before 1 October 2015), or the successor provisions in the Consumer Rights Act 2015 (CRA). Of course, even where unfair terms legislation is inapplicable, the borrower may achieve a similar result by relying on the CCA "unfair relationship" provisions. Here, the borrower need not prove they are a consumer; it suffices if they are an individual. In the context of unfair terms, whether the borrower is a consumer will assume greater importance in relation to regulated mortgage contracts where the CCA unfair relationship provisions are inapplicable.

The traditional concept of consumer

Regulation 3 of the UTCCRs defined consumer as:

> "Any natural person who, in contracts covered by these Regulations, is acting for purposes which are outside his trade, business or profession."

This replicated the definition in the underlying Unfair Terms in Consumer Contracts Directive (*93/13/EEC*) (Unfair Contract Terms Directive). In interpreting the Unfair Contract Terms Directive, the approach of the Court of Justice of the European Union (CJEU) has been to determine whether or not the individual's entry into the contract is "for the purpose of satisfying the individual's own needs in terms of private consumption" (*France v Di Pinto (361/89) [1991] E.C.R. I-1189; Benincasa v Dentalkit C-269/95 [1997] E.C.R. I-3767*). The English courts have followed the CJEU by adopting this test (*Overy v Paypal (Europe) Ltd [2012] EWHC 2659 (QB)*).

Dual purposes

Difficulties arose in applying the definition of consumer where an individual was motivated by dual purposes. In *Gruber v BayWa AG C-464-01; [2006] Q.B. 204* (on the identical definition of consumer in the Brussels Convention), the CJEU held that the pertinent question was not which was the predominant purpose: the individual could only be a consumer if the business purposes were "negligible or insignificant". For example, an individual who was motivated 70% by private purposes and 30% by business purposes would not qualify as a consumer. This approach was followed in English case law on the UTCCRs (see *Overy v Paypal*).

The European Parliament and the Council of the EU rejected this approach in the Consumer Rights Directive (*2011/83/EC*) (CRD) which provided, in recital 17:

> "The definition of consumer should cover natural persons who are acting outside their trade, business, craft or profession. However, in the case of dual purpose contracts, where the contract is concluded for purposes partly within and partly outside the person's trade and the trade purpose is **so limited as not to be predominant** in the overall context of the contract, that person should also be considered as a consumer." [emphasis added]

As a result, the UK legislation implementing the CRD (in particular the Consumer Contracts (Information, Cancellation and Additional Charges) Regulations 2013 (*SI 2013/3134*)) used a modified definition of consumer (regulation 4):

> "An individual acting for purposes that are **wholly or mainly** outside that individual's trade, business, craft or profession." [emphasis added]

Subsequently, the UK Parliament has deployed the same definition in the CRA (section 2(3)), which revoke and replace the UTCCRs.

The addition of the words "wholly or mainly" clarifies that where an individual is motivated by dual purposes, it is necessary to identify which purpose is the predominant or primary purpose. If the individual's predominant purpose is to satisfy their own needs in terms of private consumption, then they will be a consumer. Accordingly, the example individual who was motivated 70% by private purposes and 30% by business purposes is capable of being a consumer under the CRA, although they would not have qualified under the *Overy/Gruber* approach.

The wording of the consumer credit exemptions considered above uses the materially identical words "wholly or predominantly", but by reference to the other, business, purpose. As such, the consumer credit exemptions are mirror images of the CRA definition and necessarily inapplicable to CRA consumers.

Recent Ashfaq decision

In May 2017, the Court of Appeal handed down judgment in *Ashfaq v International Insurance Company of Hannover plc [2017] EWCA Civ 357*. Mr Ashfaq had purchased an insurance policy covering a buy-to-let (BTL) residential property. He contended that he had been acting for dual purposes: the private purpose of property ownership combined with the business purpose of letting for profit. He was a company director whose business was IT, not property ownership or letting.

Mr Ashfaq effectively conceded that he could not be a consumer under the UTCCRs, as he was unable to characterise the business element of these purposes as "negligible or insignificant" (the position would have been different if the CRA had applied). However, he maintained that he was a consumer for the purposes of rule 2.1.1(3) of the Insurance: Conduct of Business sourcebook (ICOBS) in the FCA Handbook. The guidance in ICOBS 2.1.3(2) suggested that an insured would be a consumer where they entered the policy "mainly" for purposes unrelated to their trade or profession, and so the position was similar to that under the CRA.

The court held that Mr Ashfaq had no real prospect of success in establishing that he acted "mainly" for private purposes. Someone who purchases a policy covering a BTL property is acting for business purposes, irrespective of the fact that their main profession may be in another field and irrespective of the type of mortgage they have. Mr Ashfaq's application had been for a residential let policy, not for ordinary domestic insurance.

Consumers and buy-to-let transactions

The Court of Appeal in *Ashfaq* considered that the purchase of an insurance policy covering a BTL property was a business transaction. The court was influenced by the guidance in ICOBS 2.1.4, which classifies someone who purchases an insurance policy covering property bought under a BTL mortgage as a commercial customer. The court extended this approach to the case where a BTL property had been bought with a residential mortgage.

BTL properties are often purchased as investments to fund retirement. Arguably someone who enters a transaction to aid the purchase or renovation of such a property would qualify as a consumer applying the general Benincasa test (satisfying individual needs in terms of private consumption). By analogy, in *Standard Bank London Ltd v Apostolakis No 1 [2000] I.L. Pr 766*, the High Court found that two individuals who used their personal funds for dealings in foreign exchange were acting as consumers: their "needs" were an appropriate use of their income, that is, to make profit.

In reality, taking a similar approach to BTLs would catch virtually every BTL transaction; therefore consumer tends to be construed narrowly. For instance, in determining whether a BTL mortgage is either exempt as an investment property loan or excluded as a consumer BTL, there is a specific statutory business purposes test. Only a small minority qualify as consumer BTLs: generally those secured on previously purchased properties which have been inherited or previously lived in by the borrower (see *Article, Gough Square Chambers' consumer credit column: October 2016*).

It is different where the loan is secured on the borrower's own home: the FCA considers that a regulated mortgage contract secured on the borrower's home to finance the purchase of a single BTL property will not be for business purposes (*MCOB 1.2.5G*).

Gough Square Chambers' consumer credit columns

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