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Gough Square Chambers' consumer credit column: June 2021

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Status: **Published on 15-Jun-2021** | Jurisdiction: **United Kingdom**

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Ruth Bala, Lee Finch, Sabrina Goodchild and Thomas Samuels 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 June 2021 column, Lee Finch considers what it means to carry on a regulated activity "by way of business" under the Financial Services and Markets Act 2000 (FSMA).

By way of business: a reminder

Introduction

As will be well known to readers of this column, the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (*SI 2001/544*) (RAO) specifies a number of activities which, if carried on "by way of business", are made "regulated activities" by section 22 of the Financial Services and Markets Act 2000 (FSMA). By virtue of section 19 of FSMA, no person may carry on a regulated activity unless they are authorised or exempt; this is called the general prohibition.

The effect of the forgoing is that if you (or your client) is neither authorised nor exempt but nevertheless want to carry out one of the activities specified in the RAO, it is essential to determine whether or not you will be acting "by way of business".

This issue has been considered before in this column, notably in the column published in September 2015 and the column published in February 2016, but the topic bears further consideration. This is especially in the light of the recent decision in *Jackson v Ayles and another [2021] EWHC 995 (Ch)* (see Legal update, Loan unenforceable under section 26 of FSMA (High Court)).

For an overview of what it means to carry on a regulated activity "by way of business", see Practice note, Carrying on regulated activities by way of business.

What does "by way of business" mean?

There is no definition of "by way of business" in either FSMA or the RAO. However, it is worth noting that the Financial Services and Markets Act 2000 (Carrying on Regulated Activates by Way of Business) Order 2001 (*SI 2001/1177*) (Business Order) amends the general "by way of business" requirements for certain activities to make the test more specific and less general. Outside of these special activities with their own nuanced requirements, we are left with the general wording of FSMA, the FCA's view set out in its Perimeter Guidance manual (PERG) and guidance from the courts.

Factors indicating an activity is being carried on "by way of business"

Perhaps the starting point should be PERG 2.3.3G, which states:

> "Whether or not an activity is carried on by way of business is ultimately a question of judgement that takes account of several factors (none of which is likely to be conclusive). These include the degree of continuity, the existence of a commercial element, the scale of the activity and the proportion which the activity bears to other activities carried on by the same person but which are not regulated. The nature of the particular regulated activity that is carried on will also be relevant to the factual analysis."

Further, PERG 4.3.7G confirms that, in contrast to the more specific test of "carrying on the business" in the context of mortgage lending, the general "by way of business" test could be satisfied by an activity undertaken on an isolated occasion. Reference should also be had to PERG 4.3.6G, 4.3.8G and 4.3.9G.

The forgoing is helpful but does not take matters very far. We have to turn to the courts for further assistance and three cases, in particular, are worth considering:

- *Helden v Strathmore Ltd [2010] EWHC 2012 (Ch)* (see *Helden v Strathmore*).

- *Financial Services Authority v Anderson and others [2010] EWHC 599 (Ch)* (see *Financial Services Authority v Anderson*).
- *R v Napoli [2012] EWCA Crim 1129* (see *R v Napoli*).

Helden v Strathmore

In *Helden v Strathmore Ltd [2010] EWHC 2012 (Ch)*, Newey J specifically considered whether or not Strathmore had provided loans to Helden "by way of business" within the meaning of section 22 of FSMA. Newey J identified eight factors that resulted in a finding that Strathmore had acted in the course of business:

- Strathmore had made a sizeable number of loans.
- The loans were made over a period of years and with some regularity.
- Substantial amounts of money were advanced.
- The loans were made with a view to profit.
- The friendship between the parties grew out of the financial relationship not the other way round.
- Informality is not inconsistent with business and, in any event, solicitors were often instructed, the loans were generally secured and records were kept.
- The loans involved a chain of not dissimilar transactions.
- Strathmore was a limited company with, it was understood, commercial objectives.

The Court of Appeal upheld Newey J's findings insofar as they related to Strathmore's acting by way of business.

Further useful guidance can be gained from two cases considering deposit taking (notwithstanding the more specific test set down by article 2 of the Business Order 2001 for that regulated activity) (see *Financial Services Authority v Anderson* and *R v Napoli*).

Financial Services Authority v Anderson

In *Financial Services Authority v Anderson and others [2010] EWHC 599 (Ch)*, Lewison J found that each of the defendants took deposits "by way of business" for six reasons:

- The deposits were taken or purported to be taken with a view to making money.
- Deposits were taken over a substantial period of time and at regular intervals.
- The number of deposits taken by each defendant was substantial.
- The amounts involved were very large (in the millions of pounds for each defendant).
- Some deposits were paid into "business" bank accounts.
- A number of the defendants specifically referred to their activities as a "business", "business venture" or "commercial".

R v Napoli

In *R v Napoli [2012] EWCA Crim 1129*, the Court of Appeal applied *Financial Services Authority v Anderson* and found that a properly directed jury could conclude that Napoli had accepted deposits "by way of business" for six reasons:

- The sums of money involved were very large.
- The deposits were made pursuant to commercial contracts.
- The moneys received were paid into corporate bank accounts.
- The deposits were made in anticipation of substantial returns.
- Napoli purported to accept deposits by way of business.
- In his CV, and when interviewed by police, Napoli described his financial activities in terms of a business.

Ultimately, each case will turn on its own facts but the reasoning of the courts in *Helden*, *Anderson* and *Napoli* provide practitioners with useful guidance.

Consequences of carrying out regulated activities without authorisation

Conducting a regulated activity by way of business without the relevant authorisation has severe consequences: it is a contravention of the "general prohibition" in section 19 of FSMA and is a criminal offence under section 23 of FSMA. Further, any contract entered into in breach of section 19 of FSMA is unenforceable under section 26 of FSMA (or section 26A of FSMA for credit-related activities) and the FCA could apply to court for injunctions and restitution orders under sections 380 and 382 of FSMA.

Avoiding the consequences

Where a party has carried on a regulated activity in breach of the general prohibition and the agreement is unenforceable under section 26 of FSMA, the court nevertheless has discretion to allow the agreement to be enforced if it is just and equitable to do so (*section 28, FSMA*). In exercising its discretion, the court must have regard to "whether the person carrying on the regulated activity concerned reasonably believed that he was not contravening the general prohibition by making the agreement" (*section 28(5), FSMA*). Under section 28A of FSMA, the FCA is granted equivalent power in relation to credit-related activities.

In *Helden*, Newey J reached the conclusion that it was just and equitable to permit enforcement for the following reasons:

- Mr Helden had benefitted from the lending.
- Strathmore had received no return from the loan.
- The property had increased substantially in value (providing Mr Helden a profit).
- Mr Helden had been a mortgage broker and had not been taken advantage of.
- Mr Helden had not been prepared to pursue alternative funding.
- Mr Helden had failed to identify any respects in which he would have been better off if Strathmore had been authorised.
- Crucially, it was not reasonable for Strathmore to realise that lending could be regulated.

Jackson v Ayles

The recent decision in *Jackson v Ayles* serves as a useful reminder of how the provisions can operate to the detriment of the unwary lender. Mr and Mrs Ayles were property developers and Mr Pumphrey lent them money secured on their matrimonial home. Chief ICC Judge Briggs considered the facts of the case and determined that Mr Pumphrey had been acting by way of business for the following reasons:

- The relationship between the parties arose out of the commercial dealing not any prior friendship.
- Mr Pumphrey had sought advice from a law lecturer about private lending.
- Mr Pumphrey had obtained a charge template for the purpose of securing his lending to ensure he got his money back.
- The lending was not built on trust.
- This was not an isolated occasion, Mr Pumphrey had made several loans to Mr and Mrs Ayles over many years.
- Since 2005, Mr Ayles had lent more than £3.5 million to 14 different individuals and companies.
- Mr Pumphrey accepted he wanted a return on his money.
- All loans made by Mr Pumphrey provided for interest in excess of market rates.

The court then turned to the question of whether to allow enforcement under section 28 of FSMA. Chief ICC Judge Briggs first considered the specific issue in section 28(5) of FSMA. He concluded that it was not reasonable for Mr Pumphrey to believe he was not contravening the general prohibition in circumstances where:

- The lender was an experienced businessman with financial acumen.
- There was no impairment on seeking legal advice.
- A choice was made not to take advice on the lending.
- The FSMA provisions had been in operation for a number of years.
- The lender was content for the borrower alone to act through legal representatives. That amounted to a weighty factor against the granting of relief that the other factors advanced in favour of allowing enforcement (summarised at paragraph 38 of the judgment) could not outweigh.

Jackson v Ayles is a useful reminder of the risks of engaging in lending, which may be regulated, without first seeking appropriate legal advice. It also emphasises the primacy of the consideration in section 28(5) of FSMA and is a further indication that subjective ignorance of the rules is unlikely to save an unauthorised lender.

Gough Square Chambers' consumer credit columns

For previous consumer credit columns written by barristers at Gough Square Chambers, see Practice note, Gough Square Chambers' consumer credit column.