Consumer credit law for Insolvency Practitioners (IPs)

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This Practice Note provides a summary of consumer credit law following the transfer of regulatory oversight to the Financial Conduct Authority (FCA). In particular, the Practice Note will examine some of the changes which have impacted upon insolvency practitioners (IPs). For further details on consumer credit agreements, see Practice Notes: Regulated activities relating to consumer credit, FCA supervisory approach to consumer credit, The FCA consumer credit regime: an overview of rules relating to arrears, default and recovery (a subscription to Lexis®PSL Financial Services is required).

Regulatory oversight

On 1 April 2014, responsibility for consumer credit transferred from the Office of Fair Trading (OFT) to the FCA. Part of the consequence of this was to replace the OFT's licensing scheme under the Consumer Credit Act 1974 (CCA 1974) with the FCA's authorisation regime under Part IV (A) of the Financial Services and Markets Act 2000 (FSMA 2000). If a firm had:

References:
CCA 1974
FSMA 2000, Pt IV

- a consumer credit licence on 31 March 2014, and
- applied (before 1 April 2014) for an interim permission under FSMA 2000 (and paid the fee)

it continued to be authorised from 1 April 2014 (but was given a landing slot during which it would need to apply either a full or limited permission).

If a firm did not satisfy both of these requirements on 31 March 2014, its consumer credit licence ended immediately before 1 April 2014.

There is a general prohibition under FSMA 2000 that no one may carry on a regulated activity in the United Kingdom, or purport to do so, without being authorised or exempt. If a person or firm does so, there are a number of significant consequences. These include: (a) criminal sanctions and (b) unenforceability of agreements entered into by an unauthorised firm or person.

References:
FSMA 2000, ss 19, 23(1)

What type of consumer credit activities require authorisation?

The activities which required a consumer credit licence from the OFT under the CCA 1974 before 1 April 2014 now broadly require an authorisation under Part IV (A) of FSMA 2000 from the FCA (but there is a new regulated activity of operating an electronic system in relation to lending). The regulated activities are set out in the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001, SI 2001/544 (the RAO) and include:

References:
Financial Services and Markets Act 2000 (Regulated Activities) Order 2001, SI 2001/544

- entering into a regulated credit agreement as the lender (including exercising, or having the right to exercise, the lender's rights and duties under a regulated credit agreement)

  References:
  SI 2001/544, art 60B

- entering into a regulated consumer hire agreement as the owner (including exercising, or having the right to exercise, the owner's rights and duties under a regulated consumer hire agreement)

  References:
  SI 2001/544, art 60N
- credit broking

  References:
  SI 2001/544, 36A
- debt-related consumer credit activities (debt adjusting, debt counselling, debt collecting and debt administration)

  References:
  SI 2001/544, arts 39D, 39E, 39F, 39G
- operating an electronic system in relation to lending; and

  References:
  SI 2001/544, art 36H
- providing credit information services and credit references

  References:
  SI 2001/544, arts 89A, 89B

These activities are all specifically defined in the RAO (also see Practice Note: What is a Regulated Consumer Credit Agreement? a subscription to Lexis®PSL Financial Services is required).

Interim permission

Firms who previously had a consumer credit licence from the OFT under the CCA 1974 needed to register with the FCA before 1 April 2014 for an 'interim permission' if they wanted to continue credit-related regulated activities from 1 April 2014. The interim permission regime was introduced to provide firms with a breathing space to adjust to the new FCA regulation regime.

The interim permission only authorises a firm to carry out the same activities as under its consumer credit licence issued by the OFT. If, after 1 April 2014, a firm wants to carry out another regulated activity, it will need to apply for FCA authorisation for that new activity *and* all the other activities it wishes to be authorised for.

The interim permission regime runs until 1 April 2016. Any firm wanting to continue to undertake regulated activities will need to have applied to the FCA during their application window (which will be no later than 1 April 2016) for either full or limited permission from the FCA. The interim permission continues until the FCA has made a decision on the firm's application for a full or limited permission. Between 1 April 2014 and 31 March 2016, all firms with an interim permission are given a three month period to apply for full or limited permission. If this date is missed, the interim permission will lapse and the firm will no longer have the FCA's permission.

Whether or not a firm needs full or limited permission will depend on the nature of the activity it is undertaking. A firm with 'full' permission is subject to the full FCA regime. A firm with a 'limited' permission (which is limited to certain low-risk activities) is subject to a lighter-touch regime.

Overall impact of transfer from OFT to FCA

The impact of the transfer of consumer credit from the OFT to the FCA is significant. It does not necessarily follow that if a firm did not need a consumer credit licence, it does not need an interim permission from the FCA. Firms undertaking credit-related regulated activities now have a much more detailed system of regulation. This includes:

- the FCA Handbook (which includes modules on dispute resolution, conduct, systems and controls and approved person)
- firms needing to have individuals performing '*significant influence functions*' to be pre-approved by the FCA (which is entirely new)
- firms needing to bear in mind some of the significant changes between the old and new regimes, including for example, a new requirement on firms in CONC 1.2.2R to:
  - ensure their agents and employees comply with CONC, and
  - take reasonable steps to ensure other persons acting on their behalf comply with CONC
- firms needing to understand the concept of principle-based regulation by the FCA

Impact of the transfer from the OFT to the FCA on professional firms

Under the consumer credit licensing regime administered by the OFT, accountancy firms and IPs had the benefit of group licences issued to their regulators (for example, the Insolvency Practitioners Association (IPA) or Institute of Chartered Accountants of England & Wales (ICAEW)). This meant that individual IPs did not need to obtain their own consumer credit licence.

However, the FCA's authorisation scheme under FSMA 2000 does not allow for group licences. Firms who had the benefit of a group licence therefore had to ensure:

- they obtained an authorisation from the FCA (or obtained an interim permission) to carry out those activities
- they could rely on an exclusion; or
- they could rely on an exemption because of arrangements made by their regulators under Part XX of FSMA 2000

References:
FSMA 2000, Pt XX

Exclusions

While there are a number of exclusions, we consider two of the most relevant exclusions for professional firms (which were introduced following lobbying).

Exclusion for IPs

An IP, and those working for the IP '*in reasonable contemplation of an appointment*' as an IP, are excluded from needing authorisation from the FCA (but the IP will still need to comply with any applicable rules) for the following activities:

References:
IA 1986, s 388
SI 2001/544, art 72H

- debt adjusting

References:
Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) (No.2) Order 2013, SI 2013/1881

- debt counselling
- providing credit information services

It is important to note that this exclusion only applies in circumstances where it is reasonably anticipated that there will be a subsequent insolvency appointment. The exclusion does not cover debt arrangement schemes and other non-statutory debt solutions. If, after an IP has given his initial advice (given in contemplation of a potential appointment), he concludes that an appointment is not appropriate he must not undertake any further work without having the appropriate authorisation from the FCA.

If an IP is appointed, the IP (and probably those working for the IP so long as the steps are taken on the IP's behalf) are excluded from requiring authorisation from the FCA for:

- debt adjusting
- debt counselling
- debt collecting
- debt administration and
- providing credit information services

However, it should be remembered that this IP exemption does not extend to the regulated activities of:

- exercising, or having the right to exercise, the lender's rights and duties under a regulated credit agreement or
- exercising, or having the right to exercise, the owner's rights and duties under a regulated consumer hire agreement

IPs cannot, therefore, enter into regulated agreements, or exercise the lender's/owner's rights and duties under any regulated agreement.

Contentious business exclusion for solicitors and barristers

Solicitors who are carrying out certain credit-related regulated activities are excluded from the need to obtain authorisation from the FCA (but they must comply with any applicable rules (like the FCA's Consumer Credit Sourcebook)). Following lobbying from the Solicitors' Regulation Authority (SRA), solicitors do not need to obtain authorisation for debt collection where they carry on that activity in the course of providing litigation services (but this is unlikely to apply where there is no intention to litigate and the firm is undertaking non-litigious debt collection activities).

Exemption for regulators

Firms may also be able to rely on the exemption granted to members of designated professional bodies (including the SRA and ICAEW) under Part XX of FSMA 2000. The exemption applies where a firm is carrying out a regulated activity in circumstances where the provision of such advice is incidental to their main professional activities. If credit-related regulated activities are a major part of the practice of the firm (for example, a law firm whose primary business is debt collection), then this option is unlikely to be available.

References:
FSMA 2000, Pt XX

Part XXIV FSMA 2000 (insolvency)

IPs and their advisors should be aware that Part XXIV of FSMA 2000 now applies to firms undertaking credit-related regulated activities and who have an interim, full or limited permission from the FCA.

In summary, Part XXIV of FSMA 2000 empowers the FCA to:

- apply for an administration order or present a winding-up petition in relation to a company or partnership which is or has been an authorised person, is or has been an appointed representative, or is carrying on or has carried on a regulated activity in contravention of the general prohibition

  References:
  FSMA 2000, ss 359, 367
- present a bankruptcy petition against an individual who appears unable to pay a regulated activity debt; or appears to have no reasonable prospect of being able to pay a regulated activity debt

  References:
  FSMA 2000, s 372
- apply for an order under section 423 of the Insolvency Act 1986 (transactions defrauding creditors) (see Practice Note: Transactions defrauding creditors--claims under section 423 of the Insolvency Act 1986)

  References:
  FSMA 2000, s 375
- participate in insolvency proceedings, attend creditors meetings and receive creditors' reports if an authorised person or company enters into insolvency or proposes a voluntary arrangement
- office holders are also under a duty to report to the FCA if they think a regulated activity is being carried on in contravention of the general prohibition

Significantly, the written consent of the FCA is now required before the directors of a firm holding an authorisation for credit-related regulated activities can file a notice of intention to appoint administrators or apply for an administration order. Following the merging of the interim permission register and the Financial Services register (see The Financial Register), the confusion over which register to search should hopefully disappear.

References:
FSMA 2000, s 362A

Things to watch out for: how can you unwittingly fall foul of FSMA 2000?

Consumer credit is a very complex area of law. As a result of moving responsibility from the OFT to the FCA, consumer credit law has been shoehorned into FSMA 2000, and as a result this has led to a lot of unanswered questions. Just some of these are:

Regulated credit agreements

It is very easy to enter into a regulated credit agreement. The definition simply says that a regulated credit agreement is an agreement under which a lender provides:

- to an individual or a relevant receipt of credit (which includes sole traders and unincorporated partnerships or two or three partners, not all of whom are corporates)
- credit of any amount (which includes, but is presumably not limited to, a cash loan or any other form of financial accommodation)
- where the agreement is not exempt

It is, therefore, arguable that if a debt is immediately due and payable, giving a debtor further time to pay (and contractually agreeing to defer those payments) could create a regulated credit agreement where the debtor is an individual or '*relevant recipient of credit*' (but there may be exemptions which can be relied upon).

Debt collecting by IPs

One of the main functions of any IP is to realise the assets of the insolvent company including collecting any debts owed to it. After the IP is appointed as an IP, he is excluded from the need to obtain authorisation for '*debt collecting*' (within the particular meaning of the RAO). However, complicated issues arise if the insolvent company has entered (perhaps unwittingly) into a number of regulated credit agreements without authorisation. While the IP may be able to collect the debts due under those agreements, they may be unenforceable under FSMA 2000 without, for example, the court's permission. If the IP threatens to do something which it cannot, or gives a misleading impression to the debtor, it is likely that the IP is in breach of CONC and his actions may give grounds for the debtor to argue there is an unfair relationship within the meaning of Section 140A of the CCA 1974. IPs will therefore need to ensure they act within the law and do not assume they, or any third party, can collect debts due to the insolvent company.

References:
CCA 1974, s 140A

Pursuing debts under regulated consumer credit agreements

If there is a regulated credit agreement, there are various post-contractual notices which must be served before further action can be taken. The types of notices depend on the type of agreement. For example, if a regulated credit agreement is a fixed-sum credit agreement for a fixed duration, a lender will need to send a default notice under Section 87(1) of the CCA 1974 (in the prescribed form) before taking steps to (for example) end the agreement early, recover possession of goods or land or demand earlier payment of any sum. The lender must also send a periodic notice under Section 77A of the CCA 1974 at least every year. If a borrower falls into arrears, the lender will normally be required to send a notice of sums in arrears under Section 86B of the CCA 1974 within 14 days of the borrowers' arrears, equally two monthly repayments. Further notices will need to be sent at least every six months while the borrower remains in arrears. There are serious consequences for non-compliance with these rules. For example, if a periodic statement is not sent then:

References:
CCA 1974, ss 77A, 87(1), 86B

- the agreement becomes unenforceable during the period of non-compliance and
- the borrower has no liability to pay interest and charges during the period of non-compliance