****

**Validation Orders (VO) Application Forms - Notes**

If you entered into regulated credit agreements when you were unauthorised or did not hold the required lending permission – or if agreements were entered into following an introduction by an unauthorised credit broker or other third party – you cannot enforce them without a validation order from the FCA. An order may also be needed in other circumstances where agreements were entered into before April 2014.

This guidance explains what validation orders are and how you can apply for one. The FCA can only grant a validation order if we are satisfied that it is just and equitable to do so in the circumstances of the case. Firms are reminded that carrying on credit-related regulated activity without an appropriate permission may be a criminal offence.

**Background**

Before 1 April 2014, the Consumer Credit Act 1974 (CCA) enabled firms to apply to the Office of Fair Trading (OFT) for an order to validate consumer credit (or consumer hire) agreements that were entered into by an unlicensed creditor (or owner), or as a result of an introduction by an unlicensed credit broker. These orders were known as ‘validation orders’. In the absence of a validation order, the agreements were unenforceable against the debtor or hirer. The CCA also enabled firms to apply to validate contracts for ancillary credit services that were entered into by an unlicensed trader. On 1 April 2014 the regulation of consumer credit was transferred from the OFT to the FCA.

**Unenforceability**

Where a firm has entered into agreements that are unenforceable against the borrower, absent a VO, the firm cannot legally:

* sue on the agreement; or
* (in probability) enforce it by realisation of security.

If a firm brought legal action against a consumer, this would be as a precursor to entering judgment (which would clearly constitute enforcement of the agreement). We also note that threatening action that the firm knows it cannot legally take or follow through could potentially be regarded as misleading, unless the limitations of such actions are made clear to the customer.

The FCA has published guidance on the meaning of enforcement of a security (such as a guarantee or indemnity) in the context of the CCA, which can be found [here](https://www.fca.org.uk/publication/finalised-guidance/fg17-01.pdf). This guidance provides that the FCA considers ‘enforcement of security’ is not just limited to obtaining a court judgment. The guidance gives the view that an agreement is enforced if, following breach of the agreement by the borrower:

* the lender demands payment, or
* the lender takes payment from the guarantor by using a continuous payment authority or direct debit mandate that was previously provided and without at least appropriate prior notification to the guarantor.

Another example of where a securitised agreement could be enforced is where a pawnbroker has lent to a consumer and taken a security in “pledge”. Subsequently, where the borrower fails to repay, the lender then takes steps to enforce the agreement by selling the pledge.

Where a lender has entered into consumer credit agreements that are unenforceable against borrowers, the firm cannot take steps such as those outlined above unless a VO is granted to them by the FCA.

Agreements entered into on or after 1 April 2014

For agreements entered into on or after 1 April 2014 a new regime applies for the purposes of ‘validating’ agreements. This is set out in Part II of the Financial Services and Markets Act 2000 (FSMA). Unlike the CCA regime, it applies only to regulated credit agreements (and not consumer hire or ancillary service contracts).

A credit agreement may be unenforceable:

* under section 26 FSMA, because the lender was not authorised and so was contravening the general prohibition under section 19; or
* under section 26A FSMA, because the lender was authorised but did not have the correct permission and so was contravening section 20; or
* under section 27 FSMA, because although the lender was authorised, with the correct permission, the agreement was made in consequence of something said or done by a third party (typically a credit broker) who was;
  + not authorised or not exempt under s.39 and so was contravening the general prohibition under section 19
  + authorised but was carrying out a credit-related regulated activity (as defined for these purposes) in breach of section 20.

The legislation refers to a ‘credit-related regulated activity’ but this is limited in this framework to lending (article 60B[[1]](#footnote-2) of the Regulated Activities Order, RAO[[2]](#footnote-3)) and certain debt-collecting (article 39F(1)[[3]](#footnote-4) of the RAO). It does not include credit broking under article 36A of the RAO, so if a broker was authorised but without the correct permission (ie did not have permission to carry on credit broking), this does not make any resultant credit agreement unenforceable and so requiring validation.

In addition to agreements being unenforceable, the customer is entitled to recover:

* any money or other property paid or transferred under the agreement, and
* compensation for any loss sustained as a result of having parted with it

Section 28A provides that a firm can apply to the FCA to validate an agreement that was entered into in the course of carrying on a credit-related regulated activity and is unenforceable because of section 26, 26A or 27. The FCA can also, upon application, determine the amount of any compensation recoverable under those sections.

If the FCA is satisfied that it is just and equitable in the circumstances of the case, it may by written notice to the applicant allow:

* the agreement to be enforced, and/or
* money paid or property transferred under the agreement to be retained

We refer to this as a ‘validation order’ although this term is not used in FSMA.

The FCA may, if it thinks fit, limit a validation order to specified agreements, or agreements of a specified description and/or made at a specified time. It can also make the order conditional on the doing of specified acts by the applicant.

There is a separate process under section 28 FSMA enabling a firm to apply to the court to validate agreements which are unenforceable because of section 26 or 27 but were not entered into in the course of carrying on a credit-related regulated activity. This would include consumer hire agreements.

Agreements entered into before 1 April 2014

For agreements entered into before 1 April 2014, a modified regime applies. This regime is not limited to credit agreements (it also includes consumer hire agreements and ancillary service contracts).). In addition, under this regime (unlike under section 28A of FSMA), unenforceability can arise if the credit broker was licensed but not for credit broking.

There is a separate application form in respect of pre-April 2014 agreements. If a firm has agreements which are unenforceable, some of which were entered into before 1 April 2014, and some on or after that date, both forms will need to be submitted. (Please refer to the fees section below to understand how this may impact the fee payable).

In determining whether to grant a validation order, the FSMA test will apply and we can only grant an order if we consider it would be just and equitable to do so. As above, the FCA may, if it thinks fit, limit a validation order to specified agreements, or agreements of a specified description and/or made at a specified time. It can also make the order conditional on the doing of specified acts by the applicant.

For agreements entered into before 1 April 2014, the customer has no right to recover monies paid or property transferred under the agreement, or compensation for loss.

Qualifying criteria

A firm can only apply to validate agreements if it is a ‘relevant firm’.

For agreements entered into on or after 1 April 2014, this means the lender – that is, the person who entered into the relevant agreements or a person to whom the lender’s rights under the agreements have been assigned.

For agreements entered into before 1 April 2014, this means the lender or owner or other person who would be entitled to enforce the relevant agreements.

Application forms

There are separate application forms for agreements pre- and post-1 April 2014.

Pre 1 April 2014 - <https://www.fca.org.uk/publication/forms/cc-validation-order-form-pre.docx>

Post 1 April 2014 <https://www.fca.org.uk/publication/forms/cc-validation-order-form-post.docx>

The applicant firm must complete the application form in two stages. Applicants should complete sections 1-4 initially (‘Stage 1’) and submit those completed sections to the FCA. Once the FCA has confirmed in writing that the relevant agreements are unenforceable, and that the Authority has jurisdiction to determine the application, you should at that point go on to complete sections 5-7 (‘Stage 2’). At that stage, the applicant will be required to provide a detailed assessment of consumer harm, which will include the applicant conducting a consumer contact exercise. Before you undertake that exercise the Authority will review and provide input into your proposed questions to consumers (but always on the basis responsibility for ensuring the sufficiency of the exercise and wider harm assessment rests solely with the applicant).

**Overview of the application form**

The application forms for both the pre and post 1 April 2014 are comprised of two distinct stages, which (with a view to saving applicants time and cost) we ask that applicant firms complete these separately, submitting Stage 1 first and not submitting Stage 2 until invited to do so by the FCA.

Stage 1 - (Sections 1-4)

Applicant firms should complete and submit sections 1-4 of the application form initially, providing all relevant evidence in support of the questions in sections 1 and 2.

* Sections 1 and 2 of each application form requests contact details, information on the agreements you wish to validate, evidence that the agreements are unenforceable, and one or more legal opinions (over which all claims to legal professional privilege are waived) that confirm various specific matters that (in effect) confirm that the FCA has jurisdiction to determine the VO application.
* Section 3 relates to the application fees for stage 1.
* Section 4 is the signature and declaration where an authorised person on behalf of the applicant firm must agree and sign in respect of Stage 1.

**Question 2.3**

Below you can find an example of a table that you can use to complete Question 2.3 to detail the agreements you wish to validate.

|  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **Loans unenforceable as a result of the lender being unauthorised, or lending without the correct permission** | | | | | | | | |
| **Name / type of agreement** | **Description of agreements** | **Number of agreements entered into** | **Total number of customers** | **Interest charged** | **Additional charges** | **Total value of credit** | **Total sums paid** | **Number of live agreements** |
|  |  |  |  |  |  |  |  |  |
| **Loans unenforceable as a result of a credit broker or other third party not being authorised or exempt** | | | | | | | | |
| **Name / type of agreement** | **Description of agreements** | **Number of agreements entered into** | **Total number of customers** | **Interest charged** | **Additional charges** | **Total value of credit** | **Total sums paid** | **Number of live agreements** |
|  |  |  |  |  |  |  |  |  |

Once we have assessed Stage 1 of your application, we will confirm whether we agree that the relevant agreements are within the scope of the FCA’s power to grant a validation order under s28A FSMA. If we do agree that they are, you will need to start designing your consumer harm exercise (see the notes below and the Guidance Notes: Stage 2 – Consumer Harm Assessment on what this involves); we expect to see your proposed Consumer Harm Exercise in final draft and, whilst it is ultimately solely your responsibility to ensure it is fit for purpose, we may (if not likely will) make suggestions as to parameters to be included in it.

**Stage 2 – (Sections 5-7)**

Once the FCA has completed its initial review of your completed Stage 1, it will direct you to complete Stage 2 (Section 5-7).

Section 5 will require you to conduct a consumer harm exercise (part of which will be informed by a consumer contact exercise) to identify the extent of any actual or potential consumer harm that may have been caused as a result of customers entering into the relevant agreements.

The purpose of this assessment is to identify any actual or potential consumer harm that may have occurred or may occur in the future in connection with the relevant agreements into which affected consumers have entered. The assessment will involve four steps which are:

 1. Customer journey walkthrough

2. Customer contact exercise

3. Report results to the FCA setting out your consumer harm assessment

4. Request from FCA for clarification and/or to discuss your findings

**IMPORTANT**: We will grant a validation order only if we are satisfied that it is just and equitable to do so in the circumstances. In reaching our decision, we must consider all relevant factors.

The applicant must undertake a robust and comprehensive consumer contact exercise and provide a robust and comprehensive assessment of consumer harm. If the applicant does not do so, the likelihood is that the FCA will not be able to reach the positive conclusion that it is “just and equitable” to grant a validation order – and so the validation order will not be granted.

For agreements entered into on or after 1 April 2014, we must have specific regard to whether (depending on how unenforceability arose):

* the lender reasonably believed that in making the agreement it was neither contravening the general prohibition nor acting without permission
* if applicable, the lender knew that a credit broker or other third party, involved prior to the agreement, was either contravening the general prohibition or acting without permission
* For agreements entered into before 1 April 2014, we must give specific consideration to whether the applicant firm (i.e., the person who (disregarding the provisions rendering the agreement(s) not enforceable) would be entitled to enforce the agreement(s)) either:
* reasonably believed that a licence under the CCA was not required by the ‘lender’, ‘owner’ or ‘trader’ (as the case may be) to enter into the relevant agreement(s); or
* reasonably believed that a licence under the CCA was not required by the credit broker when introducing the underlying consumer(s) to the ‘lender’ or ‘owner’.

**For full details on what is required in Stage 2, please review the Validation Orders (VO) Application Forms – Guidance Notes: Stage 2 – Consumer Harm Assessment.**

Section 6 relates to the application fees for Stage 2.

Section 7 is the signature and declaration where an authorised person on behalf of the relevant firm must agree and sign in respect of Stage 2.

**Outcome of application**

Once you have submitted Stage 2 of your application with Sections 6-9 now complete, and you have provided the FCA with such further information as we reasonably consider necessary to enable us to determine the application, we will be in a position to begin our assessment. Once our assessment has progressed sufficiently, we will communicate our initial view on Stage 2 of the application by way of a draft of the Notice of Determination that we propose to issue. You will then have the opportunity to make written representations on that draft Notice, before we determine the application and issue our final Notice of Determination.

A decision can be made to grant, refuse, or to limit the validation order or to attach conditions. For example, the FCA may allow enforcement of agreements but decide not to allow monies to be retained by the firm, or only in part, if we consider this to be just and equitable in the circumstances. The notice will also include an indication of the right of any person aggrieved by the determination (which may include the applicant firm or a consumer who is a party to an agreement subject of the Application) to have the matter referred to the Tribunal and the procedure for doing so.

Section 28B addresses providing a copy of the notice to persons who appear to be affected by the decision. We will agree with you a suitable strategy for providing a copy of the notice to the customers whose agreements were the subject of the Application. We will also consider whether any further action should be taken, in light of the specific facts and circumstances.

**Challenging the FCA’s decision**

Under s28B(3) of the Act, any person who is aggrieved by the Authority's determination of the Application (which may include the Firm or a Customer) has the right to refer the matter to the Upper Tribunal (formerly known as the Financial Services and Markets Tribunal). The Authority determines the Application by way of the final Notice of Determination.

Paragraph 2(2) of Schedule 3 of the Tribunal Procedure (Upper Tribunal) Rules 2008 provides that any person wishing to refer a determination to the Upper Tribunal will have 28 days from the date after notice was given of the Authority’s determination to deliver their reference notice to the Upper Tribunal.

For further information please refer to the Upper Tribunal website: <http://hmctsformfinder.justice.gov.uk/courtfinder/forms/t400-eng.pdf>

Other unenforceability

A validation order makes the agreement potentially enforceable against the customer, by removing the FSMA bar to enforcement (or, for agreements entered into pre-April 2014, the bars to enforcement referred to in regs 48, 48A and 48B of SI 2013/1881). However, it does not correct any other deficiencies which may make the agreement unenforceable under other legislation.

In particular, an agreement may be unenforceable under the CCA without a court order (for example, because it was improperly executed) or until the breach is remedied (for example, because post-contractual statements and notices were not provided or were not compliant). In the latter case, the lender may also not be entitled to interest and default sums in respect of the period of non-compliance.

The firm should consider seeking legal advice as to its position with regard to any CCA non-compliance, and what steps it may need to take to remedy this. It should not in any case mislead customers as to the legal status of the agreement.

**Fees**

Validation orders are charged in two stages, in line with the 2-stage process.

**Stage 1 fees**

The stage 1 fee is based on the number of third parties used by the applicant firm at the time of entering into the agreements (for example, how many credit brokers, or Appointed Representatives (ARs):

|  |  |
| --- | --- |
| **Number of third parties used** | **Fee** |
| 0-1 | £1,000 |
| 2-3 | £2,500 |
| 4-10 | £5,000 |
| 11+ | £7,500 |

These fees also apply to unauthorised firms. If your firm was unauthorised and did not use any third parties, the application fee would be £1,000. This is because no third parties were used.

If completing both a pre-1 April 2014 and post-1 April 2014 application form, only one fee needs to be submitted for the total number of third parties if the application forms relate to the same set of circumstances.

**Stage 2** **fees**

The time and costs involved in assessing Stage 2 of the application can vary significantly for each VO application.

Firms will be charged a Validation Order Project Fee (VOPF) for Stage 2 of the application. This will capture all time and costs allocated to the Stage 2 assessment by the FCA, up until we issue a notice of determination. This includes any fees and disbursements invoiced to us by external persons to assist in the Stage 2 assessment. The hourly rates are set according to the prevailing rate for the Special Project Fee for Restructuring in [FEES 3 Annex 9 (11)R](https://www.handbook.fca.org.uk/handbook/FEES/3/Annex9.html).

We will give you a non-binding estimate of what the final costs might be at the start of Stage 2. We will keep you informed of changes to the VOPF costs throughout this stage of the application.

We will issue a final invoice once the application is determined (or if you withdraw the application). In some cases, we may also issue interim invoices throughout the assessment of Stage 2 of the application. The fee must be paid within 30 days of us issuing you with an invoice.

If your firm wishes to withdraw the VO application, you can do so at any point. You will only be subject to the costs incurred up to the point of withdrawal.

You can make payment by debit/credit card by calling our Payments Helpline on 020 7066 6014. The line is open 10am-4pm Monday-Friday. If you wish to discuss other payment methods, please speak with your case officer.

For full details of Validation Order application fees, please refer to FEES 3 Annex 15R (5).

1. Entering into a regulated credit agreement as lender, or exercising or having the right to exercise the lender’s rights and duties under a regulated credit agreement. [↑](#footnote-ref-2)
2. Financial Services and Markets Act 2000 (Regulated Activities) Order 2001. [↑](#footnote-ref-3)
3. Taking steps to procure the payment of a debt due under a credit agreement or a relevant article 36H agreement (peer-to-peer lending). [↑](#footnote-ref-4)