



# England and Wales High Court (Chancery Division) Decisions

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**Neutral Citation Number: [2014] EWHC 144 (Ch)**

Claim No. HC13F02624

**In the High Court of Justice  
Chancery Division**

14th February 2014

Before:

**Mr. N Strauss Q.C.**  
(sitting as a deputy judge)

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**The Financial Conduct Authority (A Company**

**Limited**  **by Guarantee) Claimant**

**and**

**(1) Capital Alternatives**  **Limited**

**(2) Capital Secretarial**  **Limited**

**(3) Capital Organisation**

**Limited**

- (4) Capital Administration Services [redacted]  
Limited [redacted]
- (5) MH Trustees [redacted] Limited [redacted]
- (6) Marcia Dominique Hargous  
(7) Renwick Robert Haddow  
(8) Richard John Lyon Henstock
- (9) [redacted] African Land Limited [redacted]
- (10) Robert John McKendrick  
(11) Alan Howard Meadowcroft
- (12) Regency Capital [redacted] Limited [redacted]
- (13) Reforestation Projects [redacted]  
Limited [redacted]
- (14) Mark Andrew Ayres (also known as Mark Andrew Eyres)  
(15) Mark David Gibbs  
(16) The Personal Representatives/Estate of David William Waygood (Deceased) Defendants

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Mr. T. Penny and Mr. A Temple, instructed by the FCA, appeared for the claimant;  
Mr. D. Sweeting Q.C. and Mr. J. Mansell, instructed by Candey LLP, appeared for the 1st to 8th defendants;  
Mr. A Green Q.C. and Mr. P. Luckhurst, instructed by DAC Beachcroft LLP, appeared for the 9th to 11th defendants.  
The other defendants did not appear and were not represented.

Dates of hearing: 15th-18th, 22nd-25th October 2013

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#### HTML VERSION OF JUDGMENT

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#### Introduction

1. This is the trial of a preliminary issue in an action brought by the Financial Conduct Authority ("the FCA") in July 2013 against the promoters and operators of four investment schemes, to which I will refer as "the [redacted] African Land [redacted] scheme" and "the Carbon Credits Schemes" or "the CCC schemes".
2. The issue in each case is whether it is a collective investment scheme ("CIS") within the meaning of section 235 of the Financial Services and Markets Act 2000 ("FSMA").
3. Briefly described, the [redacted] African Land [redacted] scheme concerns a rice farm called Yoni Farm, which is situated about 25 miles from Bo, the second largest town in Sierra Leone. Investors buy sub-leases of plots of

**land**  at the farm, on the basis that they will receive the profit from the sale of the rice cultivated on the plot sub-leased to them. This scheme has been promoted since about November 2009 and, at the time the proceedings were brought, had attracted investment totalling some £8.1 million from some 1,160 investors.

4. There are three CCC schemes, relating to forest areas in Australia, Sierra Leone and the Amazon. These too involve the sale to investors of sub-leases or licences, on the basis that the operators will seek accreditation by a relevant body, resulting in tradeable carbon credits which can be re-sold at a profit. The Australian scheme involves reforestation, while the others involve the preservation of existing forest. These schemes have attracted investments totalling some £8.8 million from 919 investors.
5. Both kinds of investment have been part of the so-called "alternative investment" market, in common with other kinds of investment schemes in  **land** , including  **land**  banking, blocks of flats held as investments and fractional sales of hotel rooms, and in diverse other areas such as wine and memorabilia.
6. Section 235 of FSMA (derived from section 75 of the Financial Services Act 1986) defines a CIS in the following terms:-

"(1) In this Part "collective investment scheme" means any arrangements with respect to property of any description, including money, the purpose or effect of which is to enable persons taking part in the arrangements (whether by becoming owners of the property or any part of it or otherwise) to participate in or receive profits or income arising from the acquisition, holding, management or disposal of the property or sums paid out of such profits or income.

(2) The arrangements must be such that the persons who are to participate ("participants") do not have day-to-day control over the management of the property, whether or not they have the right to be consulted or to give directions.

(3) The arrangements must also have either or both of the following characteristics –

(a) the contributions of the participants and the profits or income out of which payments are to be made to them are pooled;

(b) the property is managed as a whole by or on behalf of the operator of the scheme".

7. The main issue, which is common to all the schemes, is whether, if the terms of an investment scheme provide that the property within the scheme is to consist of individual plots managed in such a way as to give individual returns for each investor based on the yield from his plot, this ensures that it will not be a CIS. The defendants' case, which reflects what seems to be a view commonly held in the alternative investment market, is that a scheme that is so organised has neither of the characteristics required by sub-section (3), pooling of profit or management as a whole, and is therefore not a CIS.
8. In my opinion, for the reasons given in more detail at paras. 60, 163-203, 208, 258-9, 265 below:
  - (a) pooling and management as a whole are separate issue; such an investment scheme will not involve pooling of profit or income within section 235(3)(a), but may nonetheless be "managed as a whole" within section 235(3)(b) and, if it is, and if it otherwise fulfils the relevant criteria, will be a CIS;
  - (b) all the schemes in this case are managed as a whole, because all the investment property is managed by or on behalf of the operator as one entity for the collective benefit of all investors, without any substantial regard for the individual interests of any of the investors, and without the investors themselves having any involvement in management; and
  - (c) in each case, the object of the division of the property into separate plots so as to generate individual income returns is to attempt to avoid the scheme being a "regulated activity" requiring its operators to be authorised persons, but this neither benefits investors nor involves any substantial individual as opposed to collective management, and therefore does not save it from being a CIS.

9. There is a further issue about the meaning of "property" in sub-section (3)(b). In my opinion, sub-section (3)(b) refers back to sub-section (1), and the property is whatever enables participants to benefit from its acquisition, holding,

management or disposal. On the facts of these cases, this is not, as the defendants contend, [redacted]

limited [redacted] to the investors' individual plots, but includes the whole of Yoni Farm and of the forest areas, because investors' income depends on their development and management, see further at paras. 154-6, 253 below.

10. There are also issues about the meaning of "pooling" of profits or income in section 235(3)(a). In my opinion, pooling requires the creation of a fund for the combined or common benefit of investors and, if each investor obtains an individual return based on the yield from his plot, there is no pooling of profits or income even if -

(a) the value of all investors' yield is subject to standard deductions for processing and expenses; or

(b) the value of all investors' yield is received first by the operator of the scheme and then distributed to the investors in accordance with their respective, individually calculated, entitlements. See paras. 58-9, 159-62, 207, 255-7 below.

However, in the case of two of the CCC schemes, I do not accept that there ever was any intention to pay investors individual returns based on the yield of their own plots: see paras. 261-271 below.

### The parties

11. The FCA is a body corporate, previously the Financial Services Authority, established under the provisions of the FSMA. Its regulatory objectives, as defined by sections 2(2) to (6) in force up to 1<sup>st</sup> April 2013 were to further confidence in, and the stability of, the UK financial system, the protection of consumers and the reduction of financial crime.
12. These objectives were changed on 1<sup>st</sup> April 2013 to the following three objectives, (1) the protection of consumers (2) enhancing the integrity of the UK financial system and (3) the maintenance of competitive markets and the promotion of effective competition.
13. The defendants are the promoters and operators, or individual persons or companies associated or allegedly associated with the promoters and operators, of the schemes referred to above. The defendants' positions and roles are described below.
14. The 1<sup>st</sup> to 5<sup>th</sup> defendants are the "Capital" companies, which are directly or indirectly involved in the promotion of alternative investments, including the schemes described above, or as receiving agents for operators. The 1<sup>st</sup> defendant ("CAL" or "Capital Alternatives" or "D1") promoted a large number of schemes, including the [redacted] **African Land** [redacted] and CCC schemes, and featured in early brochures for them. The 2<sup>nd</sup> defendant ("CS" or Capital Secretarial" or "D2") acted as agents to receive investors' funds. The 3<sup>rd</sup> defendant ("COL" or "Capital Organisation" or "D3") is said also to have received investors' money and to be responsible for the overall organisation of the Capital companies. The 4<sup>th</sup> defendant ("CAS" or Capital Administration" or "D4") and the 5<sup>th</sup> defendants ("MH Trustees" or "D5") also acted as receiving agents at certain times. All these companies, apart from D5, are balance sheet insolvent, according to their latest available accounts.
15. The 6<sup>th</sup> to 8<sup>th</sup> defendants ("Ms. Hargous", "Mr. Haddow" and "Mr. Henstock" or "D6" "D7" and "D8") are individuals involved in the running of the Capital companies. Ms. Hargous (who gave evidence) is a director and sole shareholder of Capital Secretarial, Capital Administration and MH Trustees, a director of Capital Organisation and formerly a director of Capital Alternatives. She is a solicitor, and is in effect the in-house solicitor for the Capital companies. She was a straightforward and truthful witness. Mr. Haddow, who is subject to a disqualification undertaking which precludes his acting as a company director, is nevertheless alleged by the FCA to have had a leading role in the running of these companies. Mr. Henstock is a director of Capital Alternatives. Neither gave evidence.

16. The 9<sup>th</sup> defendant (" [redacted] **African Land** [redacted] ", formerly Agri Capital [redacted]

**Limited** [redacted] or "D9") is the operator of the [redacted] **African Land** [redacted] scheme (sometimes referred to as "the Agri Capital scheme"). Early brochures for the scheme referred to Agri Capital as a "division" of Capital Alternatives. There is also a Sierra Leone company called Agri Capital Sierra Leone

[redacted] **Limited** [redacted] ("ACSL"), which was incorporated on 12<sup>th</sup> September 2011 and is owned as to 80% by [redacted] **African Land** [redacted] and as to 20% by a local businessman, Mr. Abdul Hamid Fawaz.

The precise division of responsibility for the [redacted] **African Land** [redacted] project between

[redacted] **African Land** [redacted] and ACSL is not entirely clear, but D9-11 conceded in the course of the hearing that the project is operated by or on behalf of [redacted] **African Land. African Land** [redacted] is balance sheet insolvent according to its latest available accounts.

17. The 10<sup>th</sup> and 11<sup>th</sup> defendants ("Mr. McKendrick" and "Mr. Meadowcroft" or "D10" and "D11") are both directors of

[redacted] **African Land** [redacted], and Mr. McKendrick is also a director of ACSL. Both gave evidence. Mr. McKendrick has had a varied career. He worked as a geologist in South Africa for some years and then in the family textile business and in the property market. He has considerable experience of West Africa, having interests in a mine in Sierra Leone and iron ore exploration in Liberia. He decided to set up the rice farming project at Yoni Farm in 2009, and it is clear from his evidence that he is deeply attached to it. Mr. Meadowcroft is a management surveyor with experience in construction and property development and was asked by Mr. McKendrick to become involved in [redacted] **African Land** [redacted] because of his project management expertise, and in particular to oversee the development of the infrastructure of Yoni Farm. In and after 2012, he became more generally involved with farm management and other issues. Both Mr. McKendrick and Mr. Meadowcroft were straightforward and truthful witnesses. Mr. McKendrick was not always accurate on detail and, by his own admission, accounting matters are not his forte.

18. Ms. Hargous was also a director of [redacted] **African Land** [redacted] from 26<sup>th</sup> August to 28<sup>th</sup> September 2009. She is also a director of ACSL, having agreed to be appointed because it was thought that a third director was needed. However she played no part in its affairs and had no recollection, when she gave evidence, of her appointment.

19. The 12<sup>th</sup> defendant ("Regency Capital" or "D12") is now the promoter of the [redacted] **African Land** [redacted] scheme, instead of Capital Alternatives, following disputes which arose between [redacted] **African Land** [redacted] and the Capital companies. It may also have some involvement in the CCC schemes. D12 has net assets of £1,336 according to its latest available accounts.

20. The 13<sup>th</sup> defendant, previously Capital Carbon Credit [redacted] **Limited** [redacted] ("Reforestation Projects" or "D13"), is the operator of the CCC schemes.

21. The 14<sup>th</sup> and the 15<sup>th</sup> defendants ("Mr. Ayres" and "Mr. Gibbs" or "D14" and "D15") are or were involved in the running of Reforestation Projects. Mr. Gibbs is, and Mr. Ayres was until December 2012, a director, and Mr. Gibbs is a director of Climate Care Global [redacted] **Limited** [redacted] ("CGL"), the Accreditations Specialist for the Sierra Leone and Brazil schemes. According to its latest available accounts, for the year ended on 31<sup>st</sup> December 2011, Reforestation Projects has net assets of £40,485.

22. The 16<sup>th</sup> defendants ("D16") are the personal representatives of Mr. Waygood, who was a director of Alternatives, Organisation and Administration.

**The preliminary issue**

23. The FCA's case is that all the schemes are CISs within the meaning of section 235 and are therefore regulated activities which cannot be carried out lawfully by unauthorised persons, and that they have been missold by a series of misleading statements, contrary to FSMA section 397.

24. The FCA applied for freezing and restraining injunctions against all the defendants except for Mr. Waygood (who had died), but accepted undertakings from D1-9 and D12, and did not proceed against D11. Roth J. granted freezing and restraining orders against D10 and D13-15 on 17<sup>th</sup> July 2013.

25. Roth J. directed the following preliminary issue:-

"whether the Agri Capital scheme (also known as the  **African Land**  scheme) and/or the Capital Carbon Credits schemes (also known as the Reforestation Projects schemes) are collective investment schemes within the meaning of section 235 of FSMA."

26. If the outcome of the preliminary issue, in relation to any of these schemes, is that it is a collective investment scheme, it will follow that it cannot lawfully be carried on, and that the defendants may have financial liabilities, and may be

liable to prosecution, under the provisions of FSMA. In the case of the  **African Land**  scheme, an adverse decision may involve shutting down a working farm employing hundreds of local people, unless it can be sold. If the outcome of the preliminary issue for any scheme is that it is not a collective investment scheme, then these proceedings will fail and, if any investors consider that they have a justifiable claim, it will have to be pursued in separate proceedings.

27. Because of the relatively brief time before the hearing of the preliminary issue, the parties have not succeeded in limiting the evidence to that which is relevant to it; I have tried to disregard evidence which is relevant only to the

allegations of misselling, and my findings of fact are  **limited**  to these which are relevant to the preliminary issue.

**The relevant statutory provisions**

28. Section 19 of FSMA sets out a general prohibition:-

"(1) No person may carry on a regulated activity in the United Kingdom, or purport to do so, unless he is –

(a) an authorised person; or

(b) an exempt person.

(2) The prohibition is referred to in this Act as the general prohibition".

29. Section 21 provides that a person must not, in the course of business, communicate an invitation or inducement to engage in an investment activity unless he is an authorised person or the content of his communication is approved by an authorised person.

30. Section 22 defines a "regulated activity":-

"(1) An activity is a regulated activity for the purposes of this Act if it is an activity of a specified kind which is carried on by way of business and –

(a) relates to an investment of a specified kind; or

(b) in the case of an activity of a kind which is also specified for the purposes of this paragraph, is carried on in relation to property of any kind."

31. Section 23 provides that a breach of the general prohibition in section 19 is an offence, and section 25 provides that contravention of section 21 is an offence, unless the person concerned believed on reasonable grounds that the content of the communication was prepared or approved by an authorised person, or that he took all reasonable precautions and exercised all due diligence to avoid committing an offence.
32. Section 26 makes an agreement by an unauthorised person in the course of carrying on a regulated activity unenforceable, and entitles the other party to recover money or property transferred, and compensation for loss.
33. Section 382 enables the court to require persons who have contravened FSMA, or who have been knowingly concerned in a contravention, to make appropriate restitution to investors who have suffered loss.
34. Section 235, defining a CIS, is set out at para. 6 above. Articles 4(2) and 51(1)(a) of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 ("the RAO") provide that establishing, operating or winding up a CIS is a specified activity for the purposes of section 22(1)(b). Accordingly, when carried on by way of business, the establishment or operation of a CIS is a regulated activity if it is carried on in relation to property of any kind. Further, by Article 81 of the RAO, units in a collective investment scheme are a specified kind of investment for the purposes of section 22(1)(a).
35. Section 397 defines the offence of making a misleading statement, but this is not relevant to what I have to decide.

#### **Authorisation and approval under FSMA**

36. The authorisation process and its purpose are explained in the affidavit of Josie Durham, an associate in FCA's Enforcement Financial Crime Division, as follows:-

"23. The FCA is empowered under Part IV [now Part 4A] of FSMA to permit persons to carry on regulated activities in the UK, on receipt of an application for permission from that person. If granted permission, the applicant becomes an authorised person and will therefore be able to engage in regulated activities (within the scope of any regulatory permissions granted) without breaching the general prohibition. Authorised persons are also able to issue and approve financial promotions (subject to the regulatory requirements imposed by the FCA Handbook) for the purposes of section 21 of FSMA. While there are exemptions from the authorisation regime, no such exemptions apply to the present [defendants].

24. Authorised persons, having become such, are subject to graduated levels of on-going supervision by the FCA under the detailed terms of the FCA Handbook, depending on the type of business they do and the resulting risk they pose to the FCA's objectives described above. FCA supervision includes visits being made by the FCA and regular reporting to the FCA. Authorised persons are also subject to sanctions which can include the closure of their regulated business if they breach the terms of the FCA Handbook.

25. The FCA also regulates staff working within or at authorised firms through the "approved persons" regime. The approved persons regime relates to the performance of "controlled functions" within or at an authorised person. An approved person is a person in respect of whom the FCA has given approval pursuant to section 59 of the FSMA for the performance of a controlled function.

26. Approved persons perform particular controlled functions in relation to an authorised person: for example, Controlled Function 1 relates to the director function and Controlled Function 10 relates to compliance and oversight. Controlled Function 30 relates to the customer function which will involve the person performing the function dealing with clients, or dealing with property of clients of a firm in a manner substantially connected with the carrying on of a regulated activity of the firm - it has no application to banking business such as deposit taking and lending, nor to general insurance business. Through the approved persons regime the FCA is therefore able to vet persons carrying out such functions within or at authorised persons.

27. The Statements of Principle and Code of Practice for Approved Persons ("APER") contained in the FCA Handbook, set out the Statements of Principle which apply to the extent that an individual is performing a controlled function for which approval has been sought and granted. APER also sets out a clear code of practice to be followed by such approved persons. They are expected to act in accordance with the provisions of APER and are liable (as above) to sanction, including potential total prohibition from working in UK financial services, by the FCA if they do not. The FCA is thereby able to regulate the activity of approved persons after they are given approval under section 59 of FSMA."

37. Where a person deals with an authorised firm, the protections afforded to him include, in addition to the benefit of supervision by the FCA, access to the Financial Ombudsman Service and eligibility for compensation through the

**Authorisation and regulation of CISs**

38. Even though persons engaging in a CIS must be authorised, it does not follow that the CIS itself will be regulated. Ms. Durham states:-

"38. CISs established and operated by a person with the necessary authorisation are classified as one of two types: regulated or unregulated. Only certain types of CIS are capable of falling into the regulated category. Generally speaking, these are schemes invested in a range of permitted investments such as shares, debentures, gilts or warrants, and which are structured as unit trust schemes or open-ended investment companies.

39. Regulated CISs must also comply with the relevant FCA rules that enable investors and independent financial advisors to compare such schemes on a like for like basis and to make certain basic assumptions about the way the CIS will operate and the level of its involvement risk. The rules deal with matters such as unit pricing, redemption provisions, the use of derivatives and management requirements.

40. Further and importantly, regulated CISs constituted in the UK must also themselves be authorised by the FCA. The FCA keeps a register of authorised CISs, again as required by section 347 of FSMA. None of the schemes referred to in this affidavit are or have been on that register.

41. The unregulated types of CIS can hold a much wider variety of investments. Unregulated CISs include arrangements that enable investors to invest on a collective basis in such diverse investments as forestry, mortgages, wine and theatrical productions. The underlying assets within these schemes may not themselves amount to designated investments for the purposes of FSMA. Consequently, dealing in or managing such assets, if they were not within a CIS, would not be subject to regulation under FSMA.

42. Unregulated CISs tend to involve higher risk investments which are not suitable to be promoted to the general public. Sections 238 and 240 of FSMA therefore prohibit authorised persons from either promoting an unregulated CIS to the general public or approving a financial promotion in relation to an unregulated CIS that they could not have promoted themselves, unless an exemption is available. Consequently there is, generally, a prohibition on the promotion of unregulated CISs to the general public, even by authorised persons.

43. The provisions of FSMA referred to above mean that unregulated CISs are usually promoted only to certain types of sophisticated investors directly or through authorised intermediaries who will have to assess the suitability of the unregulated CIS against the circumstances of their individual clients before promoting it to those clients who are suitable.

44. It will be apparent from the above that, if an operator of an unregulated CIS is based in the UK, he must be an authorised person, even though the scheme does not need an authorisation. Whilst the statutory arrangements do not require the FCA to regulate the scheme itself, they do mean that the operator will be subject to the regulatory requirements applying to authorised persons and will be subject to supervision by the FCA. As also noted above, however, schemes constituted in the UK must be regulated and authorised to be marketed to the general public. The ... schemes described in this affidavit (in addition to the defendants' own lack of authorisation) are not so authorised."

39. None of the defendants currently appear as active on the Financial Services Register of authorised persons, with the exception of Ms. Hargous, who is authorised to carry out the control function of money laundering reporting with the

company called Independent Investor Services  **Limited** , which has no apparent connection with these schemes.

**The Perimeter Guidance**

40. Section 157 of FSMA authorises the FCA to give and publish "guidance consisting of such information and advice as it considers appropriate"; where such advice is to be given to regulated persons generally, it must first publish a draft of the guidance, inviting representations to which it must have regard (section 157(3) and section 151, (1), (2)(d) and (4)).

41. The FCA has published a Perimeter Guidance Manual ("PERG") to give guidance about the circumstances in which authorisation is required, or exempt persons status available, including guidance on the activities which are regulated



by FSMA and available exclusions. Because PERG was not guidance given to regulated persons generally there was no obligation to consult, but there was in fact a consultation process. The evidence also shows that the FCA gives some guidance to persons making enquiries about individual schemes; however it is the evidence of Ms. Hargous, which I accept, that the FCA will often refuse to consider the full details of a proposed scheme, and will leave it to the promoter or operator to take its own legal advice.

42. The defendants submit that certain aspects of PERG imply that the schemes under consideration in the present case are not CISs, and that the FCA's contentions in these proceedings are inconsistent with PERG, which should be presumed to be correct, and also with informed guidance given in individual cases to D1-8's solicitor, Mr. Bretherton.

### **The authorities on CISs**

43. I have been referred to the following main authorities on CIS:-

The Russell-Cooke Trust Company v. Elliott ("Russell-Cooke") [2001] WL 753378, 16<sup>th</sup> July 2001 (Laddie J. concerning a scheme for using a solicitor's clients' funds for loans secured on real property).

Financial Services Authority v. Fradley ("Fradley") [2006] 2 BCLC 616 (C.A., concerning a horse race betting scheme).

Re The Inertia Partnership ("Inertia") [2007] Bus LR 879 (Jonathan Crow Q.C., concerning the sale of shares in a Seychelles company).

Re Sky [redacted] Land [redacted] Consultants plc ("Sky [redacted] Land [redacted]") [2010] EWHC 399 (Ch) (David Richards J., concerning a "[redacted] land [redacted]-banking" scheme).

The Financial Services Authority v. Watkins ("Watkins") [2011] EWHC 1976 (Ch) (Proudman J., concerning a [redacted] land [redacted] banking scheme).

Brown Innovatore v. Innovator One ("Brown") [2012] EWHC 1321 (Comm) (Hamblen J., concerning investment schemes).

The Financial Services Authority v. Asset [redacted] Land [redacted] Investment Inc. ("Asset [redacted] Land [redacted]") [2013] EWHC 178 (Ch) (Andrew Smith J., concerning a [redacted] land [redacted] banking scheme, permission to appeal has been given).

The Secretary of State for Business, Innovation and Skills v. Chohan ("Chohan") [2013] EWHC 680 (Ch) (Hildyard J., concerning a [redacted] land [redacted] banking scheme).

44. In addition, I have been referred to the Financial Markets Law Committee report of July 2008, entitled "Operating a Collective Investment Scheme: legal assessment of problems associated with the definition of Collective Investment Scheme and related terms", written by Michael Brindle Q.C. and Richard Stones of Lovells LLP., which discusses certain of the issues that have arisen in relation to the interpretation of section 235 ("the FMLC report").

45. As indicated earlier, the main issues in the present case relate to the identification of the "property" comprised in a CIS, the operation of the "pooling" provisions in sub-section 3(a), and the meaning of "managed as a whole" in sub-section 3(b). I will refer to the relevant passages in the authorities when I come to discuss these issues, but it is helpful to refer at the outset to other matters established or discussed in the authorities on other topics.

46. First, should section 235 be construed strictly, in the event of ambiguity, in favour of the person who might be subject to a criminal sanction? In Fradley, above, Arden L.J. said at para. [32]:-

"... since contravention of the general prohibition in s.19 may result in the commission of criminal offences, s.235 must not be interpreted so as to include matters which are not fairly within it."

47. However, in the case of In re Digital Satellite Warranty Cover [redacted] **Limited** [redacted] [2011] Bus LR 981, which concerns an alleged breach of FSMA section 19 by carrying on unauthorised insurance business, an issue arose as to the proper construction of the schedule setting out the classes of prohibited business, and Warren J. dealt with an argument that the provision should be construed restrictively in the following way:-

"60. [Counsel] ... submits that the provisions of Schedule 1, and in particular, paragraphs (b) and (c) of paragraph 16, should be construed restrictively so as to bring within the scope of regulation only types of contract which clearly fall within those provisions. This is because breach of the general prohibition in section 19 of FSMA is a criminal offence and penal provisions are not to be found in the absence of clear language. The principle on which he relies is dealt with in *Bennion on Statutory Interpretation*, 5<sup>th</sup> ed (2008) in Part XVII of The Code. It is referred to as "the principle against doubtful penalisation" which requires strict construction of penal enactments.

61. This principle is, no doubt, an important principle of public policy. But a penal enactment will not, as Bennion explains on p.828, be given a strict construction if other interpretative factors weigh more heavily in the scales. For instance, Sir Nicolas Brown-Wilkinson V-C in *In re Lo-Line Electric Motors Ltd* [1988] Ch 477 rejected the submission that the word "director" in the Company Directors Disqualification Act 1986 should be strictly construed because the Act contained penal sanctions; the issue of construction was to be approached on the ordinary basis because the paramount purpose of the disqualification is the protection of the public: see Morritt LJ in *Secretary of State for Trade and Industry v. Deverell* [2001] Ch 340.

62. In the present case, one of the central purposes of FSMA and the RAO is to regulate insurance business both for the protection of the public and to implement the requirements of the First Directive as amended. The First Directive itself demonstrates that its purposes include not only harmonisation across member states but also protection of the consumer: see in particular the third and tenth recitals. In those circumstances, a restrictive construction is not called for simply because certain conduct incurs penal sanctions. I propose to apply ordinary canons of construction to the interpretation of Schedule 1 to the RAO."

48. The Court of Appeal upheld Warren J.'s decision, but there was no discussion of this point.

49. Secondly, the application of section 235 depends on the specific facts of the case, as determined by the court: see

Fradley at [32] and Sky [redacted] **Land** [redacted] at [17].

50. Thirdly, Andrew Smith J. in Asset [redacted] **Land** [redacted] at [11-4] rejected the argument that the FCA had to prove breaches of FSMA beyond reasonable doubt, holding instead that:

"... the seriousness of the allegations means that the court's starting point is that the defendants probably did not behave as the FSA alleges, and it has to prove its case the more cogently."

51. Fourthly, it is clear from several of the authorities that "arrangements" has a wide meaning, and may include non-contractual arrangements which exist on their own or in parallel with contractual arrangements. See Fradley at [33], where Arden L.J. referred to Re Duchwari [1999] Ch. 253, in which the Court of Appeal had held that the word "arrangement" was widely used by Parliament to include agreements or understandings with no contractual effects.

See also Sky [redacted] **Land** [redacted] at [16]; Inertia at [46]; Asset [redacted] **Land** [redacted] at [158, 164].

52. Fifthly, section 235 refers to the "purpose or effect" of the arrangements, and what matters is the way in which the scheme is run in practice, not contractual terms which may not reflect reality, i.e. the substance and not the form: see for example Chohan at [90], [123]; Brown at [1170] ("... how the scheme was designed to and did operate in

practice ..."); Sky [redacted] **Land** [redacted] at [76, 78-9].

53. Therefore:-

(a) Whether there is day to day control depends on whether such control is actually exercised, not on whether investors have a contractual right to exercise it. See Brown at [1170].

(b) All investors must exercise such control: Russell-Cooke at [26]; Fradley at [46].

(c) Whether a scheme is a CIS or not may change over time, depending on how it is operated in practice. For example, both in Sky [redacted] Land [redacted] and in Chohan, the court considered whether the scheme had ceased to be a CIS taking into account changes in its terms following discussions with the FSA.

The [redacted] African Land [redacted] scheme

#### Overview

54. The main basis of the FCA's case on the [redacted] African Land [redacted] scheme as presented at the outset of the hearing was that investors receive a share of the overall profits from the sale of rice cultivated at Yoni Farm, in proportion to the size of their plot, and that D1-11's case that each investor was paid for the yield from his own individual plot, separately harvested and weighed, was based on "window-dressing", i.e. that it was a pretence.
55. Both Mr. Sweeting Q.C. for D1-8 and Mr. Green Q.C. for D9-11 criticised the FCA because (a) it had no evidence to support the allegation at the time the proceedings were commenced, (b) the allegation was made notwithstanding that, in a period of investigation lasting some 3 years, it had never sought to interview Mr. McKendrick and (c) it had not responded to an invitation to view Yoni Farm to see the operation for itself. There is some force in these criticisms. The duration of the investigation is also unfortunate, resulting it appears from a hiatus of about 15 months between June 2011 and September 2012, in which the FCA had insufficient resources to pursue its investigations, so leaving the future of an operating farm in doubt for an unnecessarily long period.
56. After the proceedings were started, the FCA did obtain evidence to support the allegation, in the course of an interview under compulsion with Mr. MacFarlane, the farm manager from September 2011 to March 2013; he said that there was no separate harvesting or calculation of individual plots' yields while he was at Yoni Farm. For reasons explained later in this judgment, I do not accept his evidence, and I am satisfied that the position is as [redacted] African Land [redacted] states.
57. On that basis, D1-11 submit that this was an investment which afforded investors their own individual property, producing its own return, distinct from the return from other plots on the farm, involving neither pooling nor management "as a whole".
58. The FCA however submits that, even on the assumption that the rice from each investor's plot was harvested and weighed separately, there was a pooling of profits or income within the meaning of section 235(3)(a) because all the rice was or might be sold together. As Mr. Green submits, this is a logical *non sequitur*, because each investor's return could relate to the yield from his plot, even if one buyer bought all the rice produced by all the plots. Contrary to the view of Mr. Thorp, the investigator principally concerned, pooling does not arise merely because there is no separate sale of the rice from each individual plot.
59. In closing submissions, Mr. Penny argued that there was pooling because there were standard percentage deductions for milling and general expenses: I reject this, because it does not seem to me that such deductions, at least in circumstances in which there is no evidence that the value of the rice would be affected by any substantial variation between such expenses as between individual plots, can amount to a pooling of profit or income. See further paras. 159-162 below.
60. The FCA also contends that, irrespective of whether the investors' income was based on separate harvesting and weighing of the rice from each plot, the property within the scheme was "managed as a whole" within the meaning of section 235(3)(b). This allegation was made at the hearing before Roth J. but, curiously, was not pleaded until the Re-Amended Particulars of Claim; the application for permission to re-amend, "for the avoidance of doubt" was made, without opposition, at the hearing. This issue is one of some difficulty; for the reasons discussed at paras. 154-6 and 163 onwards, I have concluded that the relevant property was Yoni Farm, and that it was managed as a whole, even

though the income paid to investors was indeed based on the rice yield from their individual plots. All the management is carried out by [redacted] **African Land** [redacted] or by ACSL on its behalf, and all the important decisions about individual plots (such as whether rice would be grown in a particular year, and if so what variety of rice and in how many harvests) are taken by the management on the basis of what would be right for the project as a whole. The investors are armchair investors; their practical involvement is [redacted] **limited** [redacted] to receiving occasional written progress reports about Yoni Farm and, in the case of some, being shown round it.

The terms of the scheme

61. Several brochures describing the [redacted] **African Land** [redacted] investment are in evidence, promoting essentially the same scheme. In short, investors were offered 49 year sub-leases on a plot or plots of an acre of "prime rice farming [redacted] **land** [redacted]", to be harvested by local workers to produce rice crops. Investors own their own plot(s) and are entitled to 40% of the net profit from the harvests on those plots, and to the full value of the leases, if they wish to sell them (less 3% if [redacted] **African Land** [redacted] arranges the sale). It was agreed between the parties that it was sufficient for me to consider two of the brochures, each of which contained a description of the scheme and its attractions and, at the end, the terms by which investments were to be governed.

62. The earlier of these two brochures was obtained from an investor, who dated her receipt of it November 2009. The title page has the Agri-Capital logo in the top left hand corner and states:-

"We harvest – you profit.

Gain exposure to a sector that is attracting significant investment from governments, asset managers of institutional investors.

We offer you direct access to low cost agricultural [redacted] **land** [redacted] with a valuable high yield crop and high yield income and strong capital growth prospects."

63. The next page identifies the Key Parties and Advisors as Capital Alternatives (Promoter and Sponsor), the Agri Capital [redacted] **Limited** [redacted] Management Team as Mr. McKendrick, Executive Chairman, Mr. Fawaz, Marketing and Distribution Director, Mr. Meadowcroft, Facilities Director and Mr. Moore, non-executive director. The receiving agent was Capital Secretarial. The main attractions of the investment are described as follows:-

(a) Minimum investment no more than £1,250 per one acre, made up of £750 for the [redacted] **land** [redacted] and £500 for a one off cultivation fee.

(b) On purchasing the investment, investors to receive "your leasehold deed for your areas of [redacted] **land** [redacted]" (this did not happen).

(c) Investors are entitled to 40% of the net profit for the rice crop on their plot, estimated to yield 15% p.a.

(d) Investors are entitled to any increase in the capital value of their plot if they wish to sell, with an expected 50% increase in value immediately after the [redacted]

land  becomes productive.

(e)  **African Land**  will buy the investor's

land  if they wish to sell, or arrange for a sale for a fee of 3%.

(f)  **African Land**  aim to generate a potential return of at least 175% including annual income over 5 years.

(g) Investors are entitled to a refund of their contribution if rice production does not begin within two years.

64. Page 8 of the brochure sets out a table showing how the annual estimated yield of 15% was made up on the basis of 40% of the net profit from milled rice after deducting expenses:-

Costs	1 Acre
Tonnes per year paddy rice	3.105
Milled rice 69% of paddy rice	2.1
	£
Retail price per MT in Sierra Leone*	415
Gross profit	871
Farm management	20
Drying charge	36
Fertilizer	
Pounds of Nitrates per Acre 130 lbs/Acre	42
Pounds of Psthates per Acre 40 lbs/Acre	21
Pounds of Potassium per Acre 60 lbs/Acre	27
Fungicide	13
Herbicides	26
Insecticides	7

Irrigation Supplies/Gates	2
Seed	23
Fertilizer Application Cost	12
Planting Cost	4
Hauling Cost	11
Labour Costs	10
Tillage/Harvest Fuel Cost 16 gal/Acre	21
Irrigation Fuel Cost 54 gal/Acre	72
Repair and Maintenance	14
Miscellaneous - Donations - Health Education	30
Total Rice Variable Costs	390
<input type="text"/> <b>Land</b> <input type="text"/> Owners Ground Rent	15
Profit	446
Investor Profit Share (40%)	186.4
Investment per acre	1.250
Annual estimated yield	15%

65. The detailed terms at the end of the brochure provide that the agreement is to be governed by English law, and contained an entire agreement clause.

66. The terms provide that within 28 days of receipt of the duly completed Application Form the investor will receive confirmation of the Field(s) allocated to them by way of the Sublease Certificate.

67. The following definitions are relevant:-

"Field: a parcel of  **land**  equivalent to one (1) acre within the leased area."

"Field Revenue: 40% of the net income solely attributable to the production of rice in the Investor's Field(s) after deduction of all costs and expenses incurred in connection with the management, cultivation and sale of rice and payable on an annual bases (sic) during the Term."

"The leased area: refers to the 3000 acres of farming  **land**  leased by the Company."

"Sublease: refers to the Investor's Field(s) subleased to the investor ..."

"Sublease certificate: refers to the confirmation sent to the investor."

"Term: refers to a period of 49 years commencing from the date recorded on the Sublease Certificate."

68. Para. (b) of the terms provides that within 28 days of receipt of a duly completed application form, the investor will receive "confirmation of the Field(s) allocated to them by way of a Sublease Certificate".

69. Para. (e) of the terms provides as follows:-

"Applications must be made on the Application Form. By completing an Application Form you as the applicant(s) agreed to buy the Field(s) allocated to You at the Company's discretion by way of a Sublease on the following terms:

(i) ...

(ii) the Fields are subleased for farming purposes only;

(iii) upon payment of the investment, the Investor irrevocably and unconditionally agrees

to the Company being solely responsible for managing and cultivating the

**land**  on behalf of the Investor.

(iv) the Company will procure that the Investor will receive the Field Revenue for a period of 49 years payable within six weeks after receipt by the Company of such monies after the sale of the rice.

...

(vi) should the company not commence the production of rice within two years from the date of the Sublease Certificate, the lease and Sublease will automatically terminate and the Investment will be refunded to the Investor after any fees, taxes and changes have been deducted from the Investment to be capped at a maximum of 10% of the investment made by the investor;

(vii) the Investor accepts that the Sublease is subject to a lease issued by the Landlord to the Company, and the termination of this lease will terminate the Sublease; and

(viii) the Investor accepts the description of the Leased Area upon any plan contained in the Company's marketing material is approximately correct and such plan is used for the purposes of identification only and no warranty is given or implied as to the accuracy and for the avoidance of doubt the Investor hereby acknowledged that the Company shall be entitled in its absolute discretion to change the layout of the plan provided the total area of the Leased area is not reduced."

70. Para. (h) of the Terms provide as follows:-

"You may transfer your Sublease to a third party at any time after the initial 12 month period subject to clause (1) in which case you may request in writing that the Company assist to find a third party Investor. The Company will not be under any obligation to find an Investor but will use its reasonable endeavours to find an Investor in which case the Company will be entitled to a fee or 3% of the total proceeds of any transfer which it procures or arranges on the Investors' behalf."

71. Para (o) contain a series of disclaimers:-

"The Investor hereby acknowledges that:

(i) the Company does not claim specialist knowledge or expertise as to the future price of the Leased Area;

(ii) any representation made by the Company's sales consultants, agents or sales literature either in paper or electronic form do not form part of this agreement;

(iii) the Company gives no warranty as to the future value of the Leased Area;

(iv) historical rise in the value of the [ ] [ ] land [ ] is not a reliable guide to the future prices of [ ] land [ ];

(v) whilst [ ] land [ ] prices may rise there is no guarantee that the Leased Area sold by the Company will increase in value and no return can be guaranteed from the Sublease;

(vi) the Company cannot guarantee that the price paid for the Sublease represents market value or that it will be able for a third party Investor to find the [ ] land [ ] ..."

72. The other brochure to which I was referred was produced at some time between November 2012 and February 2013.

By this time, the [ ] **African Land** [ ] scheme had been running for 3 years, and its benefits are described in even more glowing terms, including claims that the last harvest has produced an average return of 14% on investments, and that [ ] **African Land** [ ] was one of the largest farms in West Africa with over 50,000 acres under management. The employment afforded by the project in Sierra Leone, and the support of its government, are stressed.

73. The description of the management team no longer refers to [ ] **African Land** [ ] as a division of Capital Alternatives, and adds Norman Lott as Finance Director and Dr. Vo-Tong Xuan (otherwise known as "Dr. Rice") and Rusty Hestir as rice consultants. ACSL is referred to as the "Preferred Management Company", and the management is referred to as an "experienced farm management team with over 17 years [ ] **African** [ ] farming experience".

74. As to the actual terms of the scheme, there are the following main changes:-

(a) The minimum investment is now £11,250 for 5 acres, including an optional £600 per acre cultivation fee; investors were entitled to appoint their own manager (but so far no investor has done so).

(b) The definition of "the Leased Area" has been dropped, as has the promise of a "leasehold deed for your acre(s)".

(c) There are to be at least 2 harvests annually, from year 3.

(d) The investors' share of net income has risen to 50%.

(e) The period of the sublease is reduced to "48 years (dependent on timing of investment)".



(f) The money back guarantee has been dropped.

(g) The Sublease Certificate is defined as "the confirmation of investment, numbers of acres and proof of leasehold title ownership ...".

(h) The investor may give 3 months notice to terminate management by ACSL (but nobody has).

(i) Ownership of seedlings, harvest, machinery and intellectual property remains with

**African Land** .

(j) There is an additional disclaimer to the effect that  **African**

**Land**  cannot guarantee any annual return.

#### The practical operation of the scheme

75. As stated earlier, the  **African Land**  scheme is operated by or on behalf of

**African Land**  with ACSL primarily responsible for local management. Mr. McKendrick who is a director of both companies, has been closely involved throughout, and visits Sierra Leone about every 5-6 weeks. Mr. Meadowcroft visited Sierra Leone 5 times in 2012-3, for about 10 days each time.

76. The first farm manager at Yoni Farm was Mr. Marius Gerber, who held the position from late 2010 to the summer of 2011. He was succeeded by Mr. James McFarlane, who held the position from September 2011 until he was dismissed for alleged misconduct in March 2013. Mr. Meadowcroft's evidence was that he had "extreme doubts" as to how much time Mr. MacFarlane spent working, and that his performance deteriorated over time. Mr. McKendrick's evidence was

to similar effect. After his dismissal,  **African Land**  and ACSL appointed a Vietnam-controlled UK company, GMX Consulting ("GMX"), which had been employed as consultants for some months, to be the managers. Mr. Quan Le is its managing director. Mr. McKendrick's view is that GMX is very professional, and is in the course of greatly improving Yoni Farm. Mr. Mohammed Sillah is the foreman at Yoni Farm. Mr. MacFarlane and Mr. Quan Le gave oral evidence. Mr. MacFarlane dismissed Mr. McKendrick's, Mr. Meadowcroft's and others' criticisms as unfounded, and he had a number of criticisms of the way Yoni Farm was run.

77.  **African Land**  entered into the lease of what became Yoni Farm on 11<sup>th</sup> November 2009 at a rent of a bushel of rice per acre. Mr. McKendrick's evidence is that it was understood that the rent would be based on the number of acres cultivated at the time of each rental payment. The term of the lease was 50 years from 1<sup>st</sup> November 2009. A bushel of rice is 25kg of unmilled rice. Part of the payment due is now made in cash. In addition, it was understood that the local community would benefit, through employment opportunities and otherwise, from a substantial farming operation in the area.

78. The sublease certificates referred to in the terms and conditions were duly sent to investors, and certified that the investor was "the owner of ... Acres of  **Land**  with allocated Acre numbers" followed by numbers beginning with the letters SLA e.g. for Margaret Doig, SLA 1658 to SLA 1660. However, the SLA numbers were only reference numbers, and no specific  **land**  was allocated to investors at the time the certificates were sent.

79. The FCA's witness, Mr. Michael Davies, whose evidence about segregated harvesting is referred to at paras. 100-2 below, also gave detailed evidence about conversations with the Deputy Minister of Agriculture and with various officials in Sierra Leone, from which he concluded that consent had not been given for the letting of parts of Yoni Farm, and that the lease was liable to be terminated. On the other hand, enquiries made by D9-11's solicitor, Mrs. Lucy Kersey, suggest strongly that this is not so, and that valid consent has been given. Although important, this is not

an issue which affects what I have to decide.

80. The lease was of 3,000 acres of uncultivated [redacted] **land** [redacted], covered in elephant grass and with a north and south area, roughly equal, bisected by a river. The initial task was to create the necessary infrastructure, including a road from the local village, Yoni village, a farmhouse and other farmhouse buildings, which were finished by the end of 2010 and, simultaneously, to clear some of some of the [redacted] **land** [redacted] by burning the 9 foot high elephant grass that covered it. Heavy farm equipment was ordered in October 2010 and arrived in December 2010. There was a small trial harvest in 2010.
81. Mr. McKendrick walked over the entire property, looking for suitable areas for investors' plots. So far, only part of the southern area has been cleared and developed and about 10% of it is not suitable. By April/May 2011, about 300 acres had been cleared and were ready for cultivation. Harvesting was in November/December 2011. By March 2013, it was a little over 1,000 acres.
82. Investors were not allocated specific plots immediately. There was, in effect, a queue of investors and specific plots, with their co-ordinates fixed by GPS, were allocated to them as and when it was clear that the area was suitable, which might be before it was actually cleared and ready for cultivation. No formal notification of the allocation of specific areas, or "leasehold deed for your acre(s)", was sent to investors, but on 1<sup>st</sup> July 2013, sub-lease agreements were entered into between [redacted] **African Land** [redacted] and at least some of the investors for a term of 46 years, with an option to renew for a further 50 years, at a nominal rent, and the Schedule to these agreements did identify the co-ordinates of the sub-leased [redacted] **land** [redacted]. The basis for the option to extend the lease for 50 years is unclear: the head lease contains no such right.
83. According to Mr. McKendrick, CAL oversold the investment, selling some 5,000 acres in all, and did not account to [redacted] **African Land** [redacted] for all the proceeds. This led to a dispute between [redacted] **African Land** [redacted] and CAL, which was settled. It would not be possible, and nor is it appropriate, for me to go into the merits of the dispute between [redacted] **African Land** [redacted] and CAL, but it appears that investors have acquired rights over more than the available area of suitable [redacted] **land** [redacted], which is something less than 3,000 acres. Mr. McKendrick is confident that he will be able, under agreements in principle entered into by a separate company he and Mr. Haddow set up in the BVI, to acquire the necessary additional [redacted] **land** [redacted], but so far none has been acquired.
84. At the time the proceedings were commenced, according to the information available to the FCA, 1,165 investors had purchased 5,365 acres and 1,876 acres had been allocated to 563 investors. This leaves about 600 investors who are entitled to about 3,500 acres. With only about 1,000 acres left unallocated at Yoni Farm, rights to about 2,500 acres will have to be satisfied from [redacted] **land** [redacted] still to be acquired, which will then have to be cleared and made ready for cultivation, and may require further infrastructure. Whether [redacted] **African Land** [redacted] is contractually entitled to allocate [redacted] **land** [redacted] outside "the leased area", defined in some but not all brochures, may also be questionable. This is not a comfortable situation.
85. Mr. McKendrick's notebook has notes of the yields for each investor's plot for each of the 2010 to 2012 harvests, taken down from information previously noted by Mr. Sillah. There are also records of the amounts paid to the investors. There is no suggestion that either the notebook or the records are anything other than genuine contemporaneous documents.
86. The first harvest was a trial harvest of only 4 acres that had been cultivated, in September/October 2010. 3 investors

were paid £415 per ton of milled rice, without any deductions for expenses. Mr. McKendrick's explanation for this was that he thought that expenses were covered by part of the cultivation fee.

87. The next harvest took place around the time of Mr. Macfarlane's arrival in September/October 2011. By this time, 303 acres had been allocated to 90 investors. The standard price had risen to £450 per ton, but £200 was deducted for the cost of lime and additional fertiliser which was thought to be necessary to enhance yields in later years, and investors received 40% of £250 per ton of milled rice. There was no deduction for expenses other than the lime and fertiliser.

88. The 2012 harvest involved 372 investors and a total of 1066 acres. They were paid 40% of the standard price for milled rice, without any deduction for expenses. Mr. McKendrick said that, despite the definition of "Field Revenue" (para 67 above), that is how he understood the arrangements, and therefore had not made any deductions except to allow for milling. The effect of this (intended or otherwise) is to increase the percentage income for investors with plots, which can be used in promoting the scheme in later brochures.

89. By the time of the 2013 harvest, GMX was in charge. The agreement for agriculture management services dated 7<sup>th</sup> March 2013 made them responsible for "all aspects of the farming operations", which were itemised in general terms. There is no provision for services to be rendered to investors on an individual basis.

90. GMX's responsibilities under the management agreement include developing infrastructure, sourcing seeds, fertilisers and specialist agricultural equipment, as well as managing the financial systems and developing good relations with suppliers and with the local community. They give written weekly reports, which demonstrate the extent of their responsibilities. In 2013, GMX's main innovations were the design of and construction of improved irrigation for part of the farm and planting new varieties of seed with a view to seed multiplication. A 13 hectare area (about 30 acres) was irrigated and planted, which would provide enough unmilled rice to plant about 700 acres in 2014, as well as producing a high yield for the fortunate owners of plots in the 13 hectares.

91. The cost of GMX's work meant that, for 2013, rice was grown on only about 700 acres, because of a lack of funds, and that the owners of about 300-400 acres will receive no income. However, the owners of the 13 hectares will get a particularly good yield, and the expectation is that future yield generally will be enhanced. Mr. McKendrick described GMX's innovations as an experiment which was "for the greater good of the farm". Payments for 2013 have been delayed because, due to a machine breakdown, the rice cannot be milled. The 2013 season was also adversely affected by a dispute, now resolved, with the Volima people, who were not happy with Yoni Farm's activities and prevented clearance of an area of about 1000 acres.

92. Thus, the overall position is that the purchasers of some 4300 acres have so far received no return, and most of them still have no  **land**  allocated to them. The evidence as to the project's financial position was not sufficiently detailed or sufficiently analysed to provide an accurate position, but Mr. McKendrick agreed that the contributions of all the investors had been spent on general expenses or on the payments to the minority of investors who have received a return in 2012 and/or 2013. He is now financing the running of Yoni Farm himself. The future of the scheme, if it continues, will depend on the extent to which GMX's methods succeed, and the speed with which more  **land**  can be acquired and/or cleared and prepared for cultivation.

93. Various updates and bulletins written by Mr. McKendrick show the progress of the project and how it is managed. There are occasional references to the measurement of yields from individual plots, but in general they refer to Yoni Farm as a whole. For example:-

(a) In a letter dated 1<sup>st</sup> February 2011:-

"Planting of an experimental nursery began back in June with three varieties of rice being tested. The results were in line with expectations and the first investors have received their returns.

Large scale ploughing of the  **land**  has now begun at a rate of about 10 acres a day. As the ploughing takes place then we are demarcating investors  **land**  on a first-invest, first-serve basis up to 400 acres. Once we reach 400 we will irrigate and plant (hopefully end of March to end of April). Ploughing will then commence again on the next 400 acres probably in May/June."

(b) From a "Director's progress report" later in 2011:-

- "a) since February 2011, an initial 273 acres has been cultivated;
- b) 5 hybrids of rice have been planted for testing;
- c) The first varieties will be harvested in mid-September to late October;
- d) Investors should receive their dividend cheques no later than one month after the rice is sold;
- e) Once rains have ceased in November, work will begin on cultivating the next batch of 1,000 acres. This will be ready for planting by April 2012, and harvested in September 2012."

(c) A letter dated 14<sup>th</sup> September 2011, which included a number of updates on how 'the farm has been transformed':-

- i) An initial 273 acres (almost one-tenth of the farm) was ploughed;
- ii) Limestone from crushed sea shells was added to the soil to reduce acidity;
- iii) 5 test varieties of rice planted;
- iv) Harvests will commence in September to October 2011. Investors should receive their cheques within 1 month after the rice is milled, bagged and sold;
- v) A decision had been made to grow only 1 rice harvest per year (not 2). Ground nuts will now be planted instead of the second rice crop;
- vi) After November, work will begin on planting the ground nuts and ploughing the next batch of 1,000 acres – which will be planted with ground nuts first.

(d) A 'Bulletin' produced by CAL dated July 2012 says that "major progress has been made in the development of [redacted] **African Land** [redacted]'s rice farm project in Sierra Leone. The Company now has over 1,200 acres planted, and the yield from last year's harvest gave investors a 14% annual gross return."

(e) One investor (Margaret Doig) received an email dated 30<sup>th</sup> July 2012 from Alex Walia of CAL, which included an update from Mr. McKendrick. This email explained that the harvest takes a long time as they had to measure each individual acre harvested so that they can calculate individual investor returns. The email further explained that 1080 acres had been planted due to a target he had set the works a month earlier; he promised a bonus of one month's wages if they hit a target of 1,000. The email also says that

"We [redacted] **African Land** [redacted] are in the process of buying our own rice milling machinery and ...

We are also having to buy an extra combine harvester..."

(f) On 15<sup>th</sup> April 2013, Ms. Doig received an email signed by Mr. McKendrick providing a further update on the [redacted] **African Land** [redacted] Investment:-

- a) "Our initial investors have now seen up to 3 returns averaging 8% per annum;
- b) We have made a number of significant improvements to the business one of these was to upgrade our administration and process and that meant a move away from Capital Alternatives, in March 2013, who have been undertaking this work for the last 3 years;

c) The other major decision was to move away from the use of [redacted]

**African** [redacted] Rice Hybrids in order to maximise crop yields. To facilitate this move we have signed an agreement with internationally recognised rice consultancy GMX."

(g) On 5<sup>th</sup> June 2013, Mrs. Doig received an update in an email from Mr. Meadowcroft, who reported that Yoni Farm was "progressing extremely well" under the local management by GMX. The following details were given in an update of progress over the previous 6 months;

i) The provision of a modern fleet of 4WD tractors including the largest (300HP) agricultural tractor operating in Sierra Leone;

ii) A highly successful trial programme of Vietnamese long grain rice varieties achieving yields of almost 10 metric tonnes per hectare under trial conditions. These varieties now are being used to provide our own stocks of seed rice using seed multiplication techniques;

iii) The commencement of construction works to create new irrigated fields from which we are looking to attain two harvests per annum;

iv) The current planting programme of local [redacted] **African** [redacted] varieties is anticipated to progress until early June;

v) The commissioning of the company's own seven stage rice mill.

vi) [redacted] **African Land** [redacted] had "terminated its relationship with Capital Alternatives [redacted] **Limited** [redacted]", with a letter from [redacted] **African Land** [redacted]'s solicitors suggesting there had been court proceedings between [redacted] **African Land** [redacted] and CAL.

#### Distribution of income

94. D1-11 say that the [redacted] **African Land** [redacted] scheme was carefully structured, with the benefit of legal advice, so as to comply with FSMA, that is in such a way as to avoid it becoming a CIS. An important feature of this was the allocation to each investor of the income i.e. the Field Revenue derived from his particular plot, and any resulting increase in capital value. It is common ground that if, as the FCA alleges, investors were in practice paid a proportionate share of the total income from sales of rice grown at Yoni Farm, the scheme would be a CIS. This is both because income would be pooled (as well as contributions which, it is accepted, were pooled), and because

[redacted] **African Land** [redacted]'s management would undoubtedly then be management "as a whole", therefore, the scheme would fall within both (a) and (b) of section 235.

95. In short, allocation to investors of the income derived from the rice grown on their own individual plots was seen as necessary – and obviously necessary – to the lawfulness of the scheme, in circumstances in which the operators did not intend to become authorised persons and, I find, believed that this was not required if income was so allocated.

96. The FCA's case is that, whatever may have been intended, there was no such individual allocation of income. For this, the FCA relies principally on the evidence of Mr. MacFarlane, the dismissed farm manager. He was interviewed under compulsion in August 2013 and said:-

"MCFARLANE :	You know, there's a certain type of rice you would grow on swamp <input type="text"/>  <b>land</b> <input type="text"/> , bolly <input type="text"/> <b>land</b> <input type="text"/> , upland ... yes, so they all come ready at different times which is -- you don't want it all ready in the same day.
DURHAM:	No. But where you have these different types of rice growing you harvest it all at the same -- once it's ready, so the bolly <input type="text"/> <b>land</b> <input type="text"/> rice ...
MCFARLANE:	Yes.
DURHAM:	... you do it all at once. You don't separate by plot?
THORP:	Acre by acre or whatever?
MCFARLANE:	No. No, no, no, no.
DURHAM:	Again, because it's just not practical or ...
MCFARLANE:	Couldn't do it.
DURHAM:	Yes.
MCFARLANE:	Couldn't do it.
DURHAM:	Okay.
THORP:	Why do you say you couldn't do it?
MCFARLANE:	Well, you'd be there forever.
THORP:	Okay.
DURHAM:	Okay.
THORP:	And was the <input type="text"/> <b>land</b> <input type="text"/> -- when you're harvesting, because obviously we know and you know initially, that they were selling these plots as investments. So were they -- was it marked up in any way? Segregated in any way, the <input type="text"/> <b>land</b> <input type="text"/> ?
MCFARLANE:	Well, I balked against that. When I went out there at first, they said, "You know, we'll need to harvest this by acre by acre".
THORP:	Yes.

MCFARLANE:	I said, "What? You know, you can't do this. This is just impossible." Because for a start with no combine and you could have to cut by hand, okay. And this is all things -- bearing in mind, you know, I'd just gone to Sierra Leone to grow rice.
THORP:	Yes.
MCFARLANE:	Now I'm learning every day's a school day for me. You know, you cut it by hand, you bunch it. The girls put it on their heads to bring it back to the farm. You then thrash it and then you dry it. And then -- and all this time, you know, you're going to have to keep it separate. It was just an impossibility.
THORP:	Yes.
DURHAM:	Yes.
MCFARLANE:	It was just an impossibility. It was. And I was there for large scale farming. That's what I was there for.
THORP:	Yes.
MCFARLANE:	And ... no. It wasn't done, no. But there was plots marked out. I've seen a couple of maps with, you know, with satellite mapping and all this kind of stuff. But ...
THORP:	It wasn't marked out on the ground?
MCFARLANE:	No.
DURHAM:	So if I could just show you ...
MCFARLANE:	Robert and Mohamed Sillah, they did all the plotting and Sillah was quite the expert, with the GPS. ..."

97. Mr. MacFarlane also referred to a conversation in which either Mr. McKendrick or Mr. Sillah had suggested that harvesting should be done plot by plot, but that he had said that this was not practicable: he just "blew it off". Nothing further was then heard of the suggestion and "we just got on with doing the harvest".

98. In his oral evidence Mr. MacFarlane confirmed this account; he said that Mr. McKendrick had agreed "to do it my way".

99. Mr. MacFarlane's evidence on this issue was, to put it mildly, unconvincing. It is inherently improbable that Mr. McKendrick would, tamely and without discussion, have accepted the assertion, by a farm manager who was new to Sierra Leone, that a procedure which Mr. McKendrick believed was essential to the lawfulness of the whole project was impracticable. Nor did Mr. MacFarlane, either in his account of the discussion at the time or in the course of his interview or his evidence in court, provide any convincing reason why harvesting plot by plot, and measuring the yield of each plot, was impracticable or anything more than inconvenient and more expensive; this makes it even less likely that Mr. McKendrick agreed "to do it my way".

100. The FCA also relied on the evidence of Mr. Davies, who was involved in various ways in the alternative investment market, and has been acting informally on behalf of Margaret Doig, in an attempt to obtain repayment of what she has

invested in the  **African Land**  scheme. Mr. Davies visited Yoni Farm in August 2013 (during the rainy season), and was met by two Sierra Leone employees of ACSL, Mr. Francis Sanu and Mr. Sheku Buckarie. He understood that Mr. Sanu was "the Head Man" of Yoni Farm; there was a sign to that effect on his motorbike. Various points were discussed, but for present purposes what is relevant is that, according to Mr. Davies,

both Mr. Sanu and Mr. Buckarie said that the combine harvester collected rice from the whole block, that bags were not individually marked and that it was not possible to show which bags came from which plot or which investor.

101.Mr. Meadowcroft's evidence, which I accept, is that Mr. Sanu was in fact one of 6 bird catchers. He said that the suggestion that he was head man was "laughable". Mrs. Kersey visited Yoni Farm on two occasions, in each case for 5 days. On the second occasion, in September 2013, she spoke to Mr. Sanu, who had no recollection of saying that the harvester collected rice from the whole block, nor of indicating this by a sweep of his arms, as Mr. Davies said. She also spoke to Mr. Buckarie, whose English was poor.

102.I accept the evidence of Mr. Meadowcroft and Mrs. Kersey and, while I accept Mr. Davies' evidence as to what he understood Mr. Sanu and Mr. Buckarie to have said, and also that he believed the sign on Mr. Buckarie's motorbike to represent his true status at Yoni Farm, I do not place any weight on this hearsay evidence.

103.D9-11's evidence on this issue is, as Mr. Green submits, overwhelming.

104.First, Mr. McKendrick's clear evidence is that he always knew it was essential to the lawfulness of the scheme that the harvest from each plot should be segregated, and the investors paid the income from the rice harvested from their plot. Individual plots were physically demarcated, initially by the construction of large mud levies, and subsequently by placing large wooden poles in the ground at the perimeter of investors' plots at harvest time; the boundaries of plots were fixed by the use of the GPS systems. All this is amply supported by photographic evidence.

105.Mr. McKendrick's evidence is corroborated by the evidence of an investor, Jennifer Botto, who visited Yoni Farm on 2011 and asked Mr. McKendrick why he did not harvest more efficiently, by harvesting the whole farm at once and pro-rating the income between investors; Mr. McKendrick told her that it could not happen that way. He readily accepted during cross-examination that individual harvesting was indeed inconvenient. See also the email to Margaret Doig referred to at para. 93(e) above.

106.Secondly, Mr. McKendrick's evidence (supported by Mr. Sillah's witness statement) is that he gave instructions, which were followed for each of the harvests, starting in 2010, to be done on a segregated basis, and he explained the procedure. Briefly, between 2010 and 2012, the rice was cut down in the fields, individually demarcated, put through the thresher, bagged, dried, re-bagged and then weighed. In 2012, a combine harvester was used for some plots.

107.Thirdly, Mr. McKendrick's evidence is supported by the witness statement of Mr. Sillah, who says that he was surprised when told, before any of the [redacted] land [redacted] had been cleared for trials, that it was necessary to keep separate 1 acre plots, since this would be more complicated and slower, but that it was made clear to him that this procedure had to be followed. It is also supported by the evidence of Mr. Brian Rawstron, who provided occasional consultancy services to [redacted] African Land [redacted] in 2010 and 2011, as to the initial demarcation of the [redacted] land [redacted] and the initial harvesting, on an individual basis, of the small amount harvested in 2010.

108.Fourthly, Mr. McKendrick prepared detailed calculations of the amounts due to each investor for each of the years 2010 to 2012, from information provided to him by Mr. Sillah which he recorded in his notebook. It was not, and could not sensibly have been, suggested to him that he was not provided with these figures by Mr. Sillah, or that Mr. Sillah provided him with false figures, or that his notes were made up or false. It follows that the yield from each plot was recorded, which would only have been possible if the rice was separately harvested, and would have been pointless unless investors' income was to depend on the yield from their individual plots. What the notes show is set out at paras. 85-8 above.

109.Fifthly, Miss Botto's unchallenged evidence directly contradicts Mr. Macfarlane's evidence that Mr. McKendrick had agreed to "do it my way":-

"I asked Mr. McKendrick and Mr. McFarlane during the tour of the Farm, why the harvest was being undertaken in this way and why the [redacted] land [redacted] had been set out into these distinct plots by these little markers.

I suggested to Mr. McKendrick that I thought it would be more cost effective and efficient if all the rice was collected and harvested as one large harvest rather than having to harvest it from each individual



plot of [ ] **land** [ ]. Mr. McKendrick explained to me that each investor had a specific plot of [ ] **land** [ ], the size of which depended on how many acres they had purchased. Each of the investors' [ ] **land** [ ] was then marked out by the markers. Mr. McKendrick explained to me that the [ ] **land** [ ] was marked out and divided in this way so that the Farm and [ ] **African Land** [ ] Ltd were able to calculate what return had been achieved from that particular investor's plot of [ ] **land** [ ]."

110. Sixthly, Mr. Le's evidence was that he had always understood that the plots were to be harvested individually (on a semi-mechanised basis) so that the number of bags of rice attributable to each investor could be ascertained. He confirmed that the 2013 harvest had indeed been carried out in this way (as did Mrs. Kersey). He confirmed that it made no difference what type of rice was grown since the market was relatively unsophisticated in Sierra Leone and there was a single price.

111. I have no hesitation in accepting Mr. McKendrick's evidence on this issue, and I find that the rice grown at Yoni Farm is and always has been harvested on a plot by plot basis, and that the effect of the arrangements was that ACSL [ ] bought it from investors, and paid for it at a standard price. Investors have been paid by ACSL or [ ] **African Land** [ ] for the value of the rice grown on their individual plots. All the rice grown on Yoni Farm has then been sold or otherwise used or disposed of by ACSL or [ ] **African Land** [ ], but the amount paid to investors was unaffected by what happened to the rice after its sale to ACSL.

The authorities on [ ] **land** [ ] banking

112. D1-11 seek to rely on the principal authorities on [ ] **land** [ ] banking, Sky [ ] **Land** [ ], Asset [ ] **Land** [ ] and Chohan, above. Mr. Green in particular submits that they establish that for the purpose of sub-section (3)(b) what matters is the management of the activity that is essential to the investment objective which, in this case, is the individual harvesting of the rice.

113. These authorities are similar to the present case in that the property acquired by the investor is a plot of [ ] **land** [ ] which is part of a larger area to be exploited for profit. They differ from the present case in that the anticipated profit is a capital profit arising from a change or potential change in the permitted use of the whole of the [ ] **land** [ ], whereas in the present case the anticipated profit is income from agricultural use: any capital profit would arise only from the sale of an individual plot of [ ] **land** [ ] at a price based upon the income yield.

114. In Sky [ ] **Land** [ ], the operators of the scheme acquired options over two separate pieces of

[redacted] **land** [redacted] and sold small plots to investors, on the basis that the operators would apply for planning permission for the whole site, and that the purchasers of the individual plots would then be required to sell at the future market value, once permission was obtained; they could however resell in the meantime, provided that the new purchaser undertook the same obligation to sell once planning permission was obtained. Following intervention by the FSA, changes were made to the terms, so that the company was no longer responsible for seeking planning permission or for selling the individual plots, nor were the purchasers of the individual plots under any obligation to resell if planning permission was obtained. Nevertheless, David Richards J. found that in fact the operators continued to represent to investors that they would deal with the planning and sale of one of the plots with a view to obtaining planning permission for the entire site and then selling it: see [45, 70].

115. It was common ground between the parties that the scheme did not involve pooling within the meaning of section 235(3)(a), presumably because the purchasers' contributions were not pooled, but David Richards J. emphasised at [13] that pooling was not an essential element of a CIS, citing a passage in the FMLC report:

"... and the contrast with the alternative "pooling", makes it clear that arrangements can ... amount to a CIS even though each participant is entitled to a distinct part of the property if all such property is "managed as a whole".

116. On section 235(3)(b) – "the property is managed as a whole ...", David Richards J. said [17] that the issue was "mainly concerned with whether the activities of the company, if any, could constitute management as required by sub-5(3)." He considered first what "the property" was:

"74. Mr. McGee for the company focussed on "the property" for the purposes of questioning whether s.235(1) applied to the arrangements operated by the company. It was, he submitted, either the site as a whole or the individual plots. The scheme does not have as its purpose or effect that participants will receive profits from the acquisition and sale of the whole site. Their profits will come exclusively from the acquisition and sale of their individual plots, and indeed an investor was entitled under the new arrangements to sell his plot on its own. Equally, though, if "the property" means the individual plot, there cannot be a collective investment scheme involving one plot owner and the company or a series of such schemes.

75. In my view, this submission proceeds on a false analysis of "the property". I consider "the property"

to be the [redacted] **land** [redacted] comprising the individual plots sold to investors. It is that [redacted] **land** [redacted], very probably as part of a larger site which includes areas retained by the original owner and areas acquired by the company, for which planning permission and a buyer would be sought by the company. The investors participate by each becoming an owner of part of the property. While it is legally possible for an investor to sell his plot on its own, that is not what is intended or likely to happen. The purpose is to obtain planning permission, for, and to sell, the property as a whole."

117. He then went to hold that the property was managed as a whole, even though the operators were not concerned with

the current agricultural use of the [redacted] **land** [redacted], which was managed by the owners:

"76. Section 235(2) requires that the arrangements must be such that the participants do not have day-to-day control over the management of the property. As earlier observed, this is a question of the reality of how the arrangements are operated. In my judgment, there is no real issue on it in this case. There was no aspect of the management of the property over which the investors had day-to-day (or any other) control. Steps with a view to obtaining planning permission and with a view to developing or selling the

property were in the hands of the company. The physical management of the [redacted]

**land** [redacted] continued, as it had before, to be under the control of those farming the

[redacted] **land** [redacted]. In his closing speech, Mr. McGee accepted that it was difficult to sustain the argument that investors had day-to-day control over their individual plots and he did not suggest that they had collective control over the site comprising their individual plots.

77. As regards s.235(3), arrangements will constitute a collective investment scheme if they satisfy at least one of the paragraphs (a) or (b). The Secretary of State relies on paragraph (b), that the property was managed as a whole by or on behalf of the operator of the scheme. If there is a scheme, its operator was the company. The question here is what is meant by "managed". What constitutes management is dictated by the property. Some property, short-dated deposits for example, require active and constant management. The management of property of long-term nature may involve only intermittent activity.

78. As regards the [ ] **land** [ ] in question, management could be said to involve (i) long-term goals, such as planning permission, development and sale, and (ii) the short-term physical stewardship of the [ ] **land** [ ]. The latter was of no real concern to the investors.

This was not intended to be an investment in agricultural [ ] **land** [ ]. In any event, it seems clear that the arrangements envisaged that the original owner would continue to use the [ ] **land** [ ] as part of his agricultural business until possession was needed for development or sale. It was the company which in practice had a relationship with the owner and the reasonable inference from the evidence is that investors were content to leave it to the company to agree the use of the [ ] **land** [ ] pending development or sale.

79. The purpose was to make a profit from an actual or prospective change from agricultural to residential or other use. The management of the property, so far as relevant to the investors, was taking steps with a view to obtaining planning permission and developing or selling the [ ] **land** [ ]. Such activities fall naturally within the ambit of management of [ ] **land** [ ]. The respondent's submission that individual participants were left to deal with their own plots as they see fit has no basis in the evidence."

118. On that basis, disregarding the management of the farming activities on the [ ] **land** [ ] as irrelevant, David Richards J. concluded at [80] that the arrangements promoted and operated by Sky [ ] **Land** [ ] were at all times a CIS.

119. In Asset [ ] **Land** [ ], pooling was again not an issue: see [28]. Andrew Smith J. found that the evidence of investors, who all purchased small plots which were part of a larger site, established that the scheme presented to them was one in which Asset [ ] **Land** [ ] would seek planning permission for the sites, or have them re-zoned for residential development, that they would then procure sales to developers and that investors would be paid a share of the total consideration paid by the developer; investors would not have to do anything about obtaining planning permission, but would benefit from planning permission or re-zoning [71-6].

120. On the question of what was "the property", Andrew Smith J. said at [157] that he agreed with what David Richards J. had said in Sky [ ] **Land** [ ], including his view that the property with respect to which the arrangements were made was "the sites acquired by Asset [ ] **Land** [ ]", and at [168] he said that "the property" was "the site where each investor invested in a plot or plots". However, he said that it made no difference even if the relevant property in the case of each investor was his own plot or plots.

121. On the question of "management as a whole" he held:

"172. The third issue is whether the arrangements were such that the property was managed as a whole or by or on behalf of the operator of the scheme, within section 235(3)(b) of FSMA. Like section 235(2), section 235(3) is about the arrangements and is directed to whether they had the "characteristics" specified in section 235(3)(a) or 235(3)(b): FSA relies only on section 235(3)(b). As I have said, the essential nature of the schemes was that plots were investments, and the plan was that they were to be sold as part of the sites after their value had been enhanced through planning permission or the prospect of development after re-zoning. The "management of the property" relevant for identifying the "characteristics" of the arrangements is therefore, as I see it, management directed to

what David Richards J called in the Sky [redacted] **Land** [redacted] Consultants case at para.

78, the "long term goals". The arrangements were that Asset [redacted] **land** [redacted] would deal with those management matters and the whole structure of the schemes made it obvious that only

Asset [redacted] **Land** [redacted] would do so and realistically investors could not do so. (This is so whether the "property" be the sites or the individual plots.)"

122. On that basis, he concluded section 235(3)(b) was satisfied, and that the schemes were therefore CISs.

123. Chohan was a case in which the Secretary of State brought proceedings under the Directors Disqualification Act 1986 on the basis that the respondent had been acting as a de facto director of the company which had been operating

a [redacted] **land** [redacted] banking scheme which was an unauthorised CIS.

124. The main issue related to what was referred to as "the Second Scheme", operated in accordance with counsel's advice, under which the company would retain up to 25% of each site, in respect of which it would apply for re-zoning, with the likely result that customers' plots would benefit from the re-zoning, but that it would not undertake or assume any responsibility to apply for planning permission for the sites.

125. Hildyard J. accepted the Secretary of State's argument that it was necessary to ascertain the true nature of the investment as viewed by the investors from the evidence as to the manner in which the scheme was actually promoted and managed, and that, so viewed, the object was to enable investors to benefit from an increase in the collectivised value in the individual plots arising from the re-zoning of the entire site of which the plots formed a part: the object

was not an investment in the [redacted] **land** [redacted] itself but a view to its use and profit, but to profit from an enhanced value generated by re-zoning, this to be achieved through the company's use of its expertise and experience, funded at least in part by the investors: see [90, 116-7].

126. Hildyard J. left open the question of pooling [121]. One of his reasons for saying that pooling was probably not involved was that each investor was entitled to sell his own plot at a time (and presumably at a price) of his own choosing.

127. On the issue of management as a whole, Hildyard J. held as follows:

"116. As to (1) in paragraph 115 above, and as in the Sky [redacted] **Land** [redacted] Consultants case, the object of the investments solicited was plainly, in my judgment, to enable investors to benefit from an increase in the collectivised value of the individual plots they were invited to invest in, which was to be brought about by rezoning the entire site of which such plots formed a

part. The object was not an investment in the [redacted] **land** [redacted] itself with a view to its use and profit thereby: the object was profit from an enhanced value generated by rezoning of the site, and thus the prospect of sale of each plot with the potentiality of planning permission. ....

122. Turning to the second alternative characteristic, what constitutes "management" is helpfully

addressed in both Sky [redacted] **Land** [redacted] Consultants and Asset [redacted]

**Land** [redacted]. I have already cited (see paragraph 71 above) a passage from the judgment of

David Richards J in Sky  **Land**  *Consultants* at paragraphs 77 to 79, which seems to me substantially to apply in this context also.

123. Bearing in mind the necessity to look at substance rather than form, it seems to me clear that the arrangements in reality were for UKLI to realise the common objective of all the participants by doing what was necessary with their support to obtain rezoning of the site: that was what the plots were bought for and it is the purpose to which their ownership was directed."

128. In all these cases, therefore, it was held that there was management as a whole of the activities that were relevant to the attainment of the investment objective, which was an increase in the value of all the property as a "long-term goal" by securing planning permission or rezoning, from which each investor would derive his individual profit, at a time and in a manner of his own choosing. There was no doubt that, on the facts of each of these cases, the management of the process of applying for planning permission or rezoning was entirely in the hands of the operator i.e. the relevant management was carried out by the operator "as a whole".

#### Guidance under section 157: PERG and informal guidance

129. Para. 1.1.2 states:

"The purpose of this Manual is to give *guidance* about the circumstances in which *authorisation* is required, or *exempt person* status is available, including *guidance* on the activities which are regulated under the *Act* and the exclusions which are available"

130. Para. 1.2.2 states:-

"(1) The *Act*, and the secondary legislation made under the *Act*, is complex. Although *PERG* gives *guidance about regulated activities and financial promotions*, it does not aim to, nor can it, be exhaustive.

(2) References have been made to relevant provisions in the *Act* or secondary legislation. However, since reproducing an entire statutory provision would sometimes require a lengthy quotation, or considerable further explanation, many provisions of the *Act*, or secondary legislation made under the *Act*, are summarised. For the precise details of the legislation, readers of the manual should, therefore, refer to the *Act* and the secondary legislation itself, as well as the manual. ..."

131. Para. 1.3.1 relating to the status of the guidance states as follows:

"This *guidance* ... represents the *FCA's* view and does not bind the courts ... anyone reading this *guidance* should refer to the *Act* and to the relevant secondary legislation to find out the precise scope and effect of any particular provision referred to in the *guidance* and any reader should consider seeking legal advice if doubt remains. If a *person* acts in line with the *guidance* in the circumstances mentioned by it, the *FCA* will proceed on the footing that the *person* has complied with the aspects of the requirement to which the *guidance* relates."

132. The parties have referred me to the following extracts from PERG Ch. 11, guidance on property investment clubs:-

#### **"Q1. What is the purpose of these questions and answers ("Q&As") and who should be reading them?"**

These Q&As are principally aimed at those involved in the running of property investment clubs or

schemes involving the sale of plots of  **land**  with arrangements for

obtaining planning permission in respect of them or for the disposal of the

**land**  as a whole. They are intended to help such persons understand whether they will be carrying on a *regulated activity* or need to be an *authorised person* or *exempt person* under section 19 of the Financial Services and Markets Act 2000.

...

## Q2. What are property investment clubs?

In general property investment clubs, (sometimes also known as buy-to-let schemes, buy-to-let syndicates or property investment syndicates) are schemes allowing members of the public to invest in property and which possess some or all of the following characteristics:

- a pooling of resources to allow investment in, or collective management of, real property;
- much or all of the property purchased being financed by money borrowed by the members of the scheme (a typical split being 15% equity and 85% debt), with the borrowing often being arranged by the property investment club itself for members;
- the offer of educational training on the property market;
- other help given to members by the property investment club, including help with the purchase, and the sale, of the property (sometimes involving forward purchase contracts);
- the properties concerned are often newly, or not yet, built; and
- discounts are often offered, or are purported to be offered, on the price of the property (usually from the developer in recognition of a bulk purchase by club members).

...

## Q7. The participants in my property investment club do not get involved in every single management decision, but appoint agents to take decisions for them in accordance with criteria agreed between them. Have the participants lost day-to-day control?

We do not consider that day-to-day control means that each participant would themselves need to be involved in each and every decision taken, so long as they retain day-to-day control over the management. For example, delegating rent collection, cleaning and management services in relation to a property, by appointing agents to carry out these tasks would not necessarily mean that the participants lose day-to-day control, so long as the participants retain day-to-day control over the management of the agency contracts.

...

## Q.12 I run a scheme where each person owns individual properties or parts of properties in the property investment club. Each person owns property either directly, or indirectly (for example,

through a  limited  company or a  limited

liability partnership of which he is the owner or through a  limited  partnership). Is this scheme likely to be a collective investment scheme?

No, unless the properties belonging to each person, company,  limited

liability partnership or  limited  partnership are managed as a whole by or on behalf of the operator of the scheme. So, the mere fact that the operator is managing a number of properties and achieves economies of scale in his management charges or in things such as insurance cover would not mean that the properties are being managed as a whole. Neither would the fact that the operator may be able to offer reductions in sale price because of bulk discounts negotiated with developers. This is provided the operator is managing each property on an individual basis.

As an example, if a managing agent manages a block of flats on the basis that the only profit or income each individual flat owner obtains is what arises from the management of his property, there is no management as a whole. However, if the managing agent managed the flats in such a way that each individual flat owner received an income from total lettings, regardless of whether that person's flat was let or not, the properties are managed as a whole and the arrangements are likely to be a collective investment scheme.

...

**Q14. I run a property investment club where the participants own their own individual properties which are rented out but the rental income is pooled and I decide on which property should be rented at any time and to whom. Is this likely to be a collective investment scheme?**

Yes. This is because:

- the property in respect of which the arrangements are made is the property belonging to each of the participants;
- you are managing that property as a whole; and
- the participants do not have day-to-day control over the management of that property.

**Q20. I run a business arranging for the sale of individual plots of development  land  to investors who are also required to use my services in obtaining planning permission for or disposing of the  land  as a whole (or both). Might I need to be authorised?**

Yes, this is likely to be the case. This will be because the role you have in obtaining planning permission or in negotiating and effecting the sale of the  land  (or both) may mean that you are operating a collective investment scheme (see Q4). The purpose or effect of the arrangements would appear to be to enable investors, as owners of parts of the  land , to receive profits arising from your services in obtaining planning permission or arranging disposal in respect of the  land  as a whole. If the planning or disposal process is such that individual investors do not have day-to-day control over it, the arrangements are likely to amount to a collective investment scheme, and to operate it you would need to be authorised or exempt.

...

**Q21. I run a business which arranges for individual plots of  land  to be sold to potential investors and, whilst I refer to the possibility of obtaining planning permission as a way of increasing the value of the  land , I don't, nor does anyone connected to me, have a role in pursuing any such permission nor any other control over the  land  as a whole. Do I need to be authorised?**

No. If all the participants have control over the obtaining of planning permission relevant to their individual plots of  land  the arrangements will not be a collective investment scheme ..."

133. In essence, D1-11 contend that the advice contained in PERG 11 is that a property investment club will not be caught by section 235(3)(b) merely because it is managed by or on behalf of the operator. It will only be managed "as a whole" if the essential profit-generating activities are managed with a view to producing a profit for the body of

investors, rather than for investors individually; further, either the  **African Land**  and CCC schemes are property investment clubs, or there is no material difference between property investment clubs and the property-based schemes before the court in this case. Particular reliance is placed on the answer to Q.12.

134.D1-11 also rely on informal guidance given to them on various proposed projects, including the CCC schemes, by either the PERG team, the CIS team or the General Counsel's Division.

135.On 6<sup>th</sup> November 2006, D1-8's solicitor, Mr. Bretherton, then of Fladgate Fielder, wrote to a member of the General Counsel's Division:-

"As discussed last week my client, which is a company authorised and regulated by the FSA, is in the process of buying a hotel in Prague and is proposing to offer an investment opportunity to the public in the UK. The main proposals can be summarised as follows:

1. It is proposed that individual investors will enter into an agreement with my client whereby each investor agrees to pay a fixed sum in consideration for the right to use a specific room in the hotel for one week per year. The hotel will be managed by an independent local company and consumer protection provisions required by the Timeshare Act 1992 (as amended) will be included in this agreement.

2. Each investor will be given the option of (a) staying in his specified room for one week each year free of charge, or (b) receiving a percentage of the revenues attributable to his room during his allocated week. Each investor's allocated week will be rotated on an annual basis to ensure that investors are not unfairly prejudiced.

3. If the owner sells the hotel each investor will be entitled to a fixed percentage of the net proceeds attributable solely to his room. Chapter 11 of the Perimeter Guidance Manual relating to property investment clubs states that "if a managing agent manages a block of flats on the basis that the only profit or income each individual flat owner obtains is what arises from the management of his property there is no management as a whole" and this would not therefore be considered a "collective investment scheme".

My client's proposal is that each investor will receive income/profits attributable solely to his own specified hotel room. No investor would have the right to occupy, or receive income/profits from, any room other than the one specifically allocated to his at the outset. In my opinion this arrangement would not constitute "management as a whole" and falls outside the definition of "collective investment scheme". My understanding is that there are therefore no restrictions under FSMA 2000 on my client circulating the proposed the proposed investor agreement to the public in the UK.

I would be grateful if you could let me have your opinion on this matter at your earliest convenience."

136.The reply was as follows:-

"As you will know, the interpretation of FSMA legislation is ultimately a matter for the courts to determine. We cannot, therefore, offer firms or their adviser any general assurance that certain activities will not be subject to regulation. We would expect firms to reach their own conclusions on the basis of the guidance we provide and in the light of any legal advice they may have obtained. We can, nevertheless, offer you the following general comments but they are of necessity, based solely on the fact as you have presented them. You will appreciate that, if there were to be any material facts which have not been drawn to the FSA's attention regarding this matter, these facts might alter our view as expressed below.

Based on the information you have provided on the scheme your client proposed to offer, it is unclear whether there will be a pooling of potential investors' contributions. If it will be the case that investors are allocated or acquire a particular room which may be different from that of other investors and the profit/income they may receive relates solely to what is generated by their room irrespective of what income or profit may arise from the sale and/or renting of any other investment rooms, then this is likely to fall outside the scope of a collective investment scheme. If, on the other hand, for example, the rooms in the hotel were identical and were all rented out together and any profit/income is split between the investors, then this is very likely to fall within the definition of a collective investment scheme.



Even if you conclude that there is no pooling of contributions, there must also not be management as a whole. Each room must be managed separately for each individual investor and profit/income must be based on the particular room i.e. if a particular investor's room is not let out for the week then he will not receive any income/profit even though his fellow investors room may have been let out the same week and therefore he would receive the revenue."

137. In April 2008 and again in September 2008, Mr. Bretherton wrote to a member of the CIS team about a similar scheme relating to a hotel in Hungary:-

"1. My client is buying a hotel in Hungary and intends to sell the right to receive income/profits from allocated hotel rooms to members of the public. Each investor will pay a fixed sum for the right to receive (a) the rental income from an allocated room within the hotel for one week per year (each allocated week will be rotated on an annual basis to avoid unfair prejudice) and (b) a proportion of any profit attributable to his/her allocated room if the hotel is sold. My client will guarantee a minimum 7 per cent return on investment for the 12 months.

2. The investors will not have the right to stay in their allocated room but (if they do not invest through a SIPP) will be entitled to a 50 per cent discount on bookings for any other room. SIPP investors will not be entitled to any discount on room bookings. We do not consider that this arrangement will fall within the Timeshare Regulation exemption referred to by Aliya below as we are not selling the right to use the hotel accommodation merely the right to receive income/profits.

**3. There will be no pooling of investment as the income/profit which each investor receives will solely relate to his/her own room (irrespective of the income/profits generated from the rent/sale of other hotel rooms).**

**4. There will be no management as a whole as each room will be managed separately for investors by a local operator and any income /profit will be calculated for each room on an individual basis (irrespective of the income/profits generated from the other hotel rooms).**

On the basis set out above we do not consider that the proposed arrangement will constitute a "collective investment scheme" and there will therefore not be any restrictions under FSMA 2000 on my client circulating the proposed offer document and application form to the public in the UK." (**my emphasis**)

138. She replied that, on the basis of the confirmations in paras. 3 and 4, the CIS and PERG teams considered that the proposed scheme would not be a CIS because sections 235(3)(a) and (b) did not apply, adding that this was based solely on the facts as presented and that, if there were material facts which had not been drawn to the FSA's attention, that view might alter.

139. Similar guidance was sought and obtained in September 2008, in relation to a hotel which had not yet been built.

140. The difficulty with all this is that Mr. Bretherton does not explain in his letters how the hotel or the room lettings are to be managed, or what he means by saying that each room will be managed separately, and the FCA's responses do not address the question of what would and what would not amount to management as a whole. The only issue that is squarely addressed is pooling, and that without taking into account the need for pooling of contributions and income.

141. In July 2009, the FCA initiated investigations into a scheme called Room to Invest, and obtained a copy of the brochure. The FCA concluded that the scheme was "unlikely to have breached the general prohibition". The essence of the scheme was that investor bought a week each year in a room, and were to be paid 75% of the income for that

week; to ensure fairness rooms were rotated. There was an income guarantee for a

**limited**  period. The correspondence shows that the FSA was told that this scheme concerned the hotel in Hungary previously referred to, in relation to which it had been told that "the hotel rooms would be managed separately for investors by a local operator and that the hotel would not be managed as a whole" (see para. 136 above). There is nothing in the brochure to suggest that the rooms would be managed separately, except for the segregation of 75% of the income from the room allocated to each participating investor in each year. In fact, Room to Invest had nothing to do with the hotel in Hungary; the investment offered was in a hotel in Morocco called the Riad Aladdin.

142. In September 2009, Mr. Bretherton sought guidance in relation to a hotel to be built in Albania:-

"One of my clients intends to offer to investors an opportunity to invest in a hotel in Albania. The proposed offer will be as follows:

1. The client's Albanian subsidiary will build a hotel in Albania and offer members of the public in the UK (and other jurisdictions) the right to receive income/profits from allocated rooms in the hotel. The hotel will be managed by an independent operator.

2. Each investor will pay a fixed sum (in not more than four instalments over a 12 month period) for the right to receive:

(a) the rental income solely generated from his/her allocated hotel room(s); and (b) any profit solely attributable to his/her allocated room(s) (excluding hotel common parts) if the hotel is sold.

3. Investors who do not invest through a SIPP/SSAS will be entitled to stay in their allocated hotel room(s) for up to [28] nights per year for a nominal fee per night. We do not consider that this arrangement will fall within UK Timeshare Legislation as not all investors will be entitled to sue their hotel room(s) and those that do will have to pay a fee to do so.

4. We do not consider that there will be any pooling of investment as the income/profit which each investor receives will solely relate to his/her own room(s) (irrespective of the income/profits generated from the rent/sale of other hotel rooms). Investors must invest in separate hotel rooms and buy 100% of the income/profits solely attributable to their hotel room(s) so will not be any sharing of their income/profits with any other investors.

5. We do not consider that there will be any management as a whole as each room will be managed separately for investors: hotel room income/profit will be calculated separately for each investor on an individual basis.

We believe that this proposal is comparable to the example referred to in Q12 of PERG 11.2 and that there will therefore be no "management as a whole" and "no pooling of investment". On this basis we consider that: (a) the proposed arrangement will not constitute a collective investment scheme (as defined in section 235 FSMA 2000); and (b) there will not be any restrictions under FSMA 2000 on my client marketing the proposed scheme and entering into agreements with investors in the UK."

Again, it is unclear what is meant by "each room is managed separately for investors."

143. Subject to caveats to the effect that the interpretation of Act was a matter for the courts, and that comments were based on the facts as presented, the guidance given by the General Counsel's Division was in the following terms:-

"A scheme of the kind you describe is unlikely to be a collective investment scheme as long as each room is acquired by a single investor (i.e. no pooling of investment in a single room other than a joint investment by husband and wife for example); and the income (from rent) or profit (from sale of the hotel) relates solely to what is generated by the investor's room irrespective of what income or profit may arise from the sale and renting of any other investment rooms."

144. In September 2010, Mr. Bretherton sought advice in relation to "an environmental  **land**  project", which became the CCC schemes:-

"...ENVIRONMENTAL  **LAND**  PROJECT

I am writing on behalf of a UK company which intends to offer an environmental

**land**  project to investors in the UK. The UK intends to acquire

**land**  in South America or Africa and apply for voluntary emissions reduction (VER)

credits under REDD by avoiding the deforestation of such [ ] **land** [ ]. The proposal is as follows:

1. The UK company will offer investors in the UK the right to participate in the project by paying an initial sum to acquire a [49] year leasehold title to specific plot(s) of

[ ] **land** [ ] which will be registered by local lawyers. The UK company intends to acquire the freehold title to the [ ] **land** [ ] using a local subsidiary company but will not pool investors contributions.

2. Each UK Investor will have the following options:

(a) to appoint an independent third party (selected by the UK company) to apply for VER credits under REDD in which case they will pay an accreditation fee (which will be refundable if accreditation is not obtained within a set period of time). If accreditation is obtained each investor will be able to trade the VER credits which are solely attributable to his/her

plot(s) of [ ] **land** [ ] and will be entitled to the income/profits from such VER credits; or

(b) to arrange for VER accreditation to be obtained by another party or his/her choosing in which case he/she will be able to trade the VER credits which are solely attributable to his/her rainforest plot(s) and will be entitled to the income/profits from such VER credits; or

(c) to use his/her rainforest plot(s) for any other purpose which does not adversely affect the surrounding plots of [ ] **land** [ ] or their VER accreditation.

3. Each [49] year lease will be freely transferable by the UK investors (subject to any

restrictions under local [ ] **land** [ ] laws and/or the VER accreditation process). Investors will not be entitled to any profits or income other than

those which are solely attributable to their individual plot(s) of [ ] **land** [ ].

We consider that this will not amount to a collective investment scheme under section 235 FSMA 2000 on the basis that: (a) the contributions of the participants and the profits/income from their separate

plots of [ ] **land** [ ] will not be pooled; and (b) the rainforest plots will managed on an individual basis (not as whole) as each investor will have the choice to determine how his/her plot(s) are managed (see Q12 and Q21 of PERG 11.1). We therefore consider that there will not be any restrictions under FSMA 2000 on the UK company from marketing the proposed scheme and entering into agreement with investors in the UK (as PERG 8.20 and other restrictions under FSMA 2000 on investment activities will not apply)."

145.The PERG team gave what was effectively a non-committal response.

"Having considered the content of your enquiry, as long as the conditions in PERG 11 you have outlined have been satisfied, it would appear that your client would not require authorisation...it will be a matter for your client to demonstrate how the conditions in PERG 11 have been satisfied".

146.Finally, in December 2010, Mr. Bretherton sought guidance about a proposed investment in Lithuanian

[ ] **land** [ ], the structure of which has similarities with the [ ] **African**  
**Land** [ ] scheme:-

"One of my UK clients intends to offer an investments in Lithuanian [ ] **land** [ ]  
to retail investors in the UK and would be grateful for your guidance at your earliest convenience.

1. Each investor will be offered a sub-lease over a specifically designated plot of  
agricultural [ ] **land** [ ] in Lithuania at a fixed fee per hectare.

Each investor will therefore have an interest in a clearly defined plot of [ ]  
**land** [ ].

2. Each investor will have the option to pay a fixed cultivation fee in consideration for the  
appointment of:

(a) the owner of the freehold title to the [ ] **land** [ ]

to manage the cultivation of [ ] **land** [ ]: the local  
manager will make recommendations in relation to, and manage, the  
cultivation harvest and sale of crops grown on the investor's plot(s) of

[ ] **land** [ ] and arrange for insurance against any  
damage to the crops before and after harvesting; and

(b) an independent local agent (eg lawyer) who will liaise with each  
investor separately on an individual basis by:

(i) taking instructions as to whether he/she agrees with the  
local manager's crop recommendations; and

(ii) arranging for the distribution of any income/profits solely  
attributable to the cultivation of crops on his/her plot of

[ ] **land** [ ].

3. The local manager will use satellite imagery to estimate the yield attributable to each  
individual plot of [ ] **land** [ ] and give such information to the  
independent agent.

4. The aggregate of the actual yields attributable to all the plots will be calculated and  
compared against the aggregate of the estimated yields – this information will be used to  
calculate (and adjust if necessary) the profits solely attributable to each separate plot  
which will be distributed to the investors on an individual basis by the independent local  
agent.

5. If the local manager wants to sell the freehold/leasehold title to any plot of  
[ ] **land** [ ] he must obtain the consent of the relevant investor. If  
consent is obtained from the relevant investor will be entitled to a percentage of any  
profits solely attributable to the sale of his/her plot and such proceeds will be distributed  
to the relevant investor(s) separately on an individual basis by the independent local

agent.

6. Each investor may choose not to pay the cultivation fee in which case he/she may appoint another manager/agent of his/her own choosing or make other arrangements in

respect of the cultivation of his/her plot(s) of  **land** .

We consider that this will not amount to a collective investment scheme under section 235 FSMA 2000 on the basis that:

(a) the contributions of the participants and the profit/income from their separate plots of

**land**  will not be pooled; and

(b) the plots will managed on an individual basis (not as whole) as each investor will have

the choice to determine how his/her plot of  **land**  is managed (see Q12 of PERG 11.2 and Q21 of PERG 11.3)."

147. The response from the Customer Contact Centre did not address management as a whole. Its advice, with the usual caveats, was as follows:-

"As you will be aware, the main issue will be whether the participants of the scheme each exercise day to day control. You have set out how, according to PERG 11 you believe the arrangement will not be seen as a CIS.

Stating that in principle that the client has a degree of control that means that neither pooling or the exercise of day to day control by a person other than the investor, or a person of the investor's choosing is not sufficient for our purposes, as it is too easy for an arrangement to be set up, but not followed up in practice. ~We would expect the agreement to be followed up in practice before we would be satisfied that a CIS was not present. For example, if the agreement states that an investor has a choice about who exercises control on his behalf, we would take account of how realistic the choice held would be.

If you can demonstrate that at all times that the reality of the scheme that the investor in fact able to exercise control over his investment, it may not be viewed as a CIS. It will of course be the reality of the scheme which will decide its regulatory position."

#### The elements of a CIS

148. The elements of the definition of a CIS are as follows:-

(a) arrangements with respect to property of any description;

(b) the purpose or effect of such arrangements must be to enable participants to participate in or receive profits or income from the property;

(c) no day-to-day control by the participants over the management of the property;

(d) pooling of contributions and profits or income; or

(e) management as a whole by or on behalf of the operator.

149. The only issues between the FCA and D1-11 relate to "property", pooling of profits or income and management "as a

whole", but as D12 did not participate in the proceedings, and may be affected by the outcome on the

**African Land**  issues, I must make findings on all issues.

#### Arrangements

150. I find that there were arrangements with respect to property in the [redacted] **African Land** [redacted] scheme. The arrangements were contractual, on the terms of whichever brochure was used by the investor. Whether the property was the whole of Yoni Farm or only the plots allocated to investors, the arrangements were undoubtedly with respect to "property".

The purpose of the arrangements

151. The purpose of the arrangements was clearly to provide investors with profit from the property or part of it, by the receipt of income from the rice grown on their plots.

No day-to-day control over management

152. Although some investors contracted on terms entitling them to appoint their own managers or, possibly, to manage their own plot themselves, no investor has so far done either. It is possible that, in the future, a large investor or a group of investors will do so but, unless and until all investors do so, which is almost inconceivable, this element of a CIS will continue to be satisfied: see para. 53(b) above.

Pooling of contributions

153. There is no suggestion in any of the brochures, or in the Terms and Conditions, that investors' contributions (or the cultivation fee part of them) will be segregated and used exclusively for expenditure on their plots. Given the delay before rice was to be grown on plots purchased by the investors, it is obvious that their contributions were to be available to meet the costs of developing and running Yoni Farm, and Mr. McKendrick confirmed that they have been used for these and other purposes.

Property

154. It is clear that "the property" referred to in sub-section (3)(b) is the property as described in sub-section (1), that is, not the property obtained by one investor, but all the property which is subject to the arrangements enabling all

participants to receive income or profits from its acquisition, holding, management or disposal: see Sky [redacted]

Land [redacted] at [75]; Asset [redacted] Land [redacted] at [157, 168].

155. D1-11 submitted that "the property" consisted of the investors' interests in the plots leased to them; that is what they would have seen as their investments or "the vehicle" for their investments. Mr. Penny submitted that the property included the whole farm, not just the totality of the investors' plots from time to time. Investors' income, and the prospect of an increase in the capital value of their investment, depended on the efficient management of the whole farm.

156. This issue depends on whether the meaning of "acquisition, holding management or disposal" in sub-section (3)(b) is restricted to acquisition etc. by the investor, or whether it extends to acquisition etc. by the operator of property which then generates profit for the investor. In my view, in the context of provisions relating to collective investment, it is the latter. Therefore the "property" will include property managed by the operator so as to profit investors.

157. I therefore agree with Mr. Penny on this. What is "the property" in any case depends on its facts. In this case "the property" is Yoni Farm, rather than just the individual plots from time to time allocated to investors, because investors are intended to derive profit from the management of the whole Yoni Farm operation, including farm buildings, roads, irrigation areas and other parts of it which are not part of their own plots, but which are necessary to enable the operation to run, and without which no or less income would be available for them.

158. Mr. Penny also submitted that, given the way in which the purchase money paid by investors was used to fund the operation, including payments made to other investors higher up the queue to whom a plot had been allocated, the money paid by the investors was also part of "the property" within sub-section (3)(b). I do not think that this is right. The investors' purchase money represented contributions which were pooled, but I do not think that they were part of

the property that was "managed"; they were just paid into [redacted] **African Land** [redacted]'s account and used as required. It would be different if they had been set aside and invested, but they were not.

Pooling of income or profit

159. There appears to be no authority on the meaning of pooling of profits or income in section 235. In my opinion, it bears its ordinary meaning. There is pooling where the profit from the investment property provides a fund to be used for the combined or common benefit of all investors.

160. I have found earlier in this judgment that ACSL bought the rice grown on each investor's plot, which had earlier been separately harvested, set aside and weighed, for sums which, although not conforming to, and generally higher than, the Field Revenue, did represent the price for the precise amount of rice grown. Therefore, it is not the case that the overall proceeds of sale of the rice were divided amongst investors, or "pooled". Mr. Penny relies on the impossibility of relating individual sales to a wholesale buyer or through local shops to the rice owned by particular investors, but by that stage the investors no longer had any interest in the rice. Indeed, ACSL having bought the rice, what happened to it after that was of no direct consequence to investors and of no relevance to the pooling issue.

161. Mr. Penny again relies in this context on the fact that the contributions of "new" investors has been used to pay returns to "old" investors but, while this is part of the factual basis for finding that there was a pooling of contributions, no pooling of profit or income is involved.

162. Finally, Mr. Penny submits that pooling is involved in the standard percentage deductions for drying the rice and for milling it, and for the deduction of £200 per ton for expenses in 2011. It is true that this might conceivably mean that minor variations in the actual losses through drying and milling, or in the amount of fertiliser used, might not be reflected in the price paid to investors, but there is no evidence that any significant difference in these respects from one lot of rice to another was likely. It is true that some of the rice, which was to be used to plant the following year's crop, would not actually be milled, but I do not think that this makes any difference; investors were paid a standard price based on the value of the rice, and there would have been no justification for paying a much higher price to those investors whose rice was to be used in this way, rather than sold.

Managed as a whole on behalf of the operator

163. This is the main issue. D1-11 originally submitted that Yoni Farm was managed by ACSL on behalf of the investors, not by [redacted] **African Land** [redacted], the operator. This argument did not survive scrutiny of the brochures, which make it clear that [redacted] **African Land** [redacted] is responsible for the project, operating "through" ACSL. It was abandoned by Mr. Green and was not pursued by Mr. Sweeting. Both the brochures and the evidence of Mr. McKendrick and Mr. Meadowcroft establish that the scheme was promoted and operated without any clear distinction being drawn between [redacted] **African Land** [redacted] and ACSL, and I find that ACSL's management activities are carried out for [redacted] **African Land** [redacted], as are the activities of GMX under its consultancy and management contracts.

164. It is therefore now undoubtedly the position that all the management activities at Yoni Farm are carried out by or on behalf of [redacted] **African Land** [redacted], the operator. Whether or not I am right about what is "the property" in this case, whatever the property is undoubtedly managed by or on behalf of [redacted] **African Land** [redacted]. The issue is whether it is managed "as a whole". There is little in the authorities as to what is meant by "as a whole" in this context, as explained earlier "as a whole" was not in issue in the [redacted] **land** [redacted] banking cases.

165. D1-11's submission may be summarised as follows:-

(a) Because breach of section 235 may be a criminal offence, subject to the due diligence defence, it should be construed narrowly, or at least "conservatively".

(b) In order to determine whether the operator is managing the scheme "as a whole" the right approach is (i) to identify the main objectives of the investment and what acts of management are central to those objectives being achieved; and (ii) to consider whether

those acts of management are carried out collectively or for each investor individually.

(c) In the present case, the investment objective is to obtain income and capital appreciation from the rice yield on individual plots; the clearance and allocation of plots, the sowing of rice and its harvesting, followed by weighing and sale to ACSL, are the essential acts of management, and they are performed individually for each investor with a view to enhancing that investor's income. The separate harvesting of each investor's separate plot is the core management activity which creates the investor's profits.

(d) That the essential acts of management are individual and not collective is illustrated by the inconvenience involved in separating individual plots and ascertaining the yield from each; it would obviously be simpler and less expensive not to have to go to such lengths (as indeed Miss Botto said to Mr. McKendrick when she was being shown around).

(e) It is entirely logical that there should be no management of the property as a whole if income is derived solely from the investor's individual property since, per Arden L.J. in Fradley at [3]:-

"At the heart of the concept (if a CIS) ... is the requirement for the sharing of profit or income by participants who do not have day-to-day control of the management of the property."

(f) An approach which determines in the first instance what are the essential acts of management, and whether they are conducted individually, has the advantage of certainty, which is of importance given (i) the criminal and civil sanctions imposed for operating in unregulated CIS, (ii) the unenforceability of agreements entered into in the course of doing so and (iii) the different tax consequences of the scheme being a CIS.

(g) The alternative approach of the FCA, which is to weigh up all the acts of management involved in a scheme and consider whether they are predominantly collective as opposed to individual, involves much greater uncertainty.

(h) The three authorities dealing with  **land**  banking are distinguishable, in that in all those cases the investment objective was the long-term goal of increasing value by obtaining planning permission or rezoning for the whole site; income from farming was irrelevant. In the present case, the investment objective is income from farming, and this is dealt with on an individual basis.

(i) Further, these authorities support D1-11's case, in that they establish that the relevant management activities for the purpose of sub-section (3)(b) are the activities which are relevant to the investment objective; in this case those are the activities which are designed to enhance the income from rice growing, which are carried out by reference to individual plots and not "as a whole".

166. In relation to PERG and the informal guidance given by the FSA, D1-11's submissions may be summarised as follows:-

(a) PERG 11 is directly applicable to the  **African Land**  scheme, which falls within the broad definition of a "property investment club"; in any event, it is to be seen as guidance which is generally applicable to other schemes which might fall within section 235.

(b) The FCA's answer to Q.12 demonstrates the FCA's view that, on the proper construction of section 235, whether there is "management as a whole" is determined by whether or not the individual investments are treated separately in relation to the profit-earning aspect of the investment; if so, the fact that the operator of the scheme is providing management services that are common to all the properties does not constitute management as a whole, because the core feature of the investment (in that case income generation through rent) is separately treated and accounted for.

(c) This constitutes definitive, publicly available guidance, to the effect that collective



expenses will not make a scheme a CIS, so long as there is no collective income; the FCA's case is inconsistent with the guidance.

(d) The informal guidance given to Mr. Bretherton particularly in relation to the hotel

schemes, which are conceptually indistinguishable from [redacted] **African**

**Land** [redacted], is understandable only if that is the correct understanding of "management as a whole"; obviously such schemes must involve extensive common management activities, but this in the FCA's view does not mean that they are managed as a whole.

(e) There is a strong presumption that the FCA's interpretation of section 235 is correct, because:-

(i) The FCA's guidance has quasi-legislative status by reason of the obligations to consult and notify the Treasury (sections 157-8, now sections 139A and 139B).

(ii) The FCA's functions include advising firms whether or not schemes fall within the section, and whether to bring proceedings for alleged contraventions; it is the body with the greatest experience as to how section 235 applies to factual situations, and its considered views (PERG has been in place unamended since March 2006) are likely to be correct.

(iii) If the court were to disregard clear guidance on the proper interpretation of the statute, the consequences may be disastrous and unfair; contractual arrangements for investments entered into in good faith would be avoided and promoters and operators may be financially ruined, as well as being liable to criminal sanctions.

(f) Applying the dictum of Arden L.J. in Fradley at [32], section 235 should not be interpreted so as to include matters which are not fairly within it, and a court should not adopt an interpretation inconsistent with general guidance such as that in PERG.

(g) The courts are reluctant to disturb a settled interpretation and practice based on that

interpretation: see per Lord Philips in Bloomsbury International [redacted]

**Limited** [redacted] v. Sea Fish Authority [2011] WLR 1546 at [55-9].

167. The FCA's submissions, on the basis that the evidence of separate harvesting is accepted, as it has been, may be summarised as follows:-

(a) Section 235 should not be construed narrowly: see Re Digital (paras. 47-8 above).

(b) The purpose of section 235 is to protect investors who have put money into a scheme in circumstances in which they have lost control of their investment because it is pooled or subject to collective management. It would be remarkable if it did not apply to this scheme, in which (i) all the management is carried out by or on behalf of the operators and (ii) the investors have no control.

(c) Section 235(3)(b) requires a balancing exercise in which the individual and collective elements of management are assessed; there is management "as a whole" if the collective elements outweigh the individual element or, putting it another way, if they are predominant.

(d) In the case of [redacted] **African Land** [redacted], the collective elements are clearly predominant:-

(i) Plots are allocated to investors, on a random basis, by

**African Land** /ACSL; there is no question of an investor choosing the asset which he purchases, as in the case of, for example, a buy-to-let scheme.

(ii) Yoni Farm is and always has been managed as a single project by

managers appointed by  **African Land**  or ACSL. Investors have no contact with managers, play no part in management and are not consulted; they are armchair investors.

(iii) Most of the management activities necessary to create a viable farm, without which investors will not benefit from their individual plots, are carried out "as a whole": the creation of roads and buildings, burning the 9 foot elephant grass, the construction of many large wells, providing accommodation for farm managers and employees, employment and payment of staff, selection of suitable land for rice growing prior to allocation of plots, irrigation, selection of rice varieties, preparation of large areas for planting, appointment of appropriate farm managers and technical experts, purchase of plant and machinery, seed multiplication of selected

areas of  **land**  and post-harvest activities including drying, milling, storage and sale.

(iv) Irrigation in particular is of great importance and depends upon large scale infrastructure improvements, requiring their own separate

**land** .

(v) Other management activities can be seen as activities which are undertaken as a whole or as activities which are carried out on each individual plot, such as for example the sowing of seed, bird-scaring, the application of nutrients and fertilizer and pest control.

(vi) The only aspect of management that is undertaken on an individual basis is the actual harvesting and weighing of the rice for each investor's plot.

(vii) Fundamental decisions taken by the management for the benefit of the farm as a whole may affect individual investors, without their having any say in the matter. For example, the major irrigation work undertaken by GMX in 2013 meant that the owners of about one-third of the cultivated plots obtained no harvest, whereas those whose plots were used for seed multiplication had higher yields as a result.

(viii) Whilst it is correct that one of the objectives was capital appreciation, that too was to be achieved by creating a thriving farm by the overall

management of the  **land** .

(ix) In practice, the farm is treated as a single entity, with overall management. GMX's contract with ACSL does not provide for individual management and their weekly reports demonstrate overall management. Mr. McKendrick said in evidence that GMX had "complete autonomy" over the whole farm. GMX has no contract, or contact, with individual investors.

(x) D1-11's approach is wrong because it treats as relevant only one of the many management activities that are necessary to realise the investment objective, that is the harvesting of the rice, neglecting the many other steps

earlier in the process carried out collectively which are at least equally important.

(xi) Looking at the reality of the scheme, the individual elements of management are tiny in comparison to the overall management.

(e) Mr. Penny submits that [redacted] **land** [redacted] banking cases provide no support for D1-11's argument. If the argument was correct, an operator of the [redacted] **land** [redacted] banking scheme would not be a CIS, because the profit is derived from an individual title deed and an individual sale, and this is what generates the profit; all the rest is preparatory.

(f) While the FCA accepts that there are presumptions that PERG, containing a long-standing interpretation by the body with the greatest practical experience, is correct, Mr. Penny submits that there are limits to that presumption since the FCA is not in a better position than the court in construing the law. In any event, nothing in PERG 11 provides guidance applicable to the [redacted] **African Land** [redacted] scheme. PERG 11 relates to buy to let schemes and [redacted] **land** [redacted] banking schemes, not to agricultural schemes, and there are significant differences in the content of management, as between buy to let schemes involving rented accommodation and [redacted] **African Land** [redacted]. In particular, the income from a flat is mainly derived from the flat itself, and management requires far less input; a plot of [redacted] **land** [redacted] at Yoni Farm would yield no income at all without the operator's skilled overall management of the whole project. Reliance on the answer to Q.12 in the wholly different context of Yoni Farm is misplaced.

## Discussion

### Narrow construction

168. I do not accept D1-11's argument that section 235 is to be construed narrowly, for the reasons given by Warren J. in Digital (paras. 46-7 above). I do not think that what Arden L.J. said in Fradley was part of the ratio, and in any event she went no further than to say that section 235 should not be construed in such a way as to cover schemes that were "not fairly within it", which is not inconsistent with Digital and with which I respectfully agree. I think that the right approach is, as Mr. Sweeting suggested during the argument, to construe the section "conservatively".

### The purpose of section 235

169. I accept Mr. Penny's submission: the purpose of section 235 is to provide protection for the investor in collective investments, where there is pooling or collective management.

170. While Arden L.J. did say in Fradley at [3] that profit sharing without day-to-day control was "at the heart" of the concept of a CIS, this reflects sub-sections (2) and (3)(a) only, and not sub-section (3)(b). As David Richards J. said in Sky [redacted] **Land** [redacted] at [13], citing the FMLC report, pooling is not a necessary element of a CIS. See para 114 above.

### The structure of section 235

171. The structure of section 235 is not entirely easy to understand, in that it is not obvious why section 235(3)(a) should only be satisfied if both contributions and income or profit are pooled; either would seem to call for investor protection. However, as noted above, it is clear that, where there is only one kind of pooling, or neither, management as a whole is an alternative.

172. Two points arose in the course of the argument on the structure. The first was whether the investors' involvement in management, even if less than day-to-day control, can be relevant to whether there is management as a whole by the operator.
173. D1-11 submitted that the investors' participation in management was only relevant to sub-section (2). As Mr. Sweeting put it, once it is shown that the threshold of day-to-day control over management was not crossed, "it is not logically possible to recruit the fact that there is no day-to-day control as part of the analysis in sub-section (3)". Therefore, D1-11 submitted, the FCA's reliance on the "armchair" investors' non-involvement in management on the "management as a whole" issue was misplaced; it was irrelevant to sub-section (3)(b).
174. I do not accept this. There is nothing in section 235 to justify it, and it would be quite possible for investors' participation in important decisions to justify finding that the operator's management was not "as a whole" within sub-section (3)(b), while not being sufficient to amount to day-to-day control within sub-section (2). For example, in a buy-to-let scheme, investors might well be able to choose their flat, make decisions on decor and furniture, and decide whether to let it to tenants found by the manager, for what periods and on what terms, or even find tenants himself, and consider what to do if the tenant fell into arrears. This would not be day-to-day control over management, but it might well suffice to take the scheme outside section 235(3)(b). There is no logical reason to leave it out of account. Equally, there is no reason to exclude the complete absence of any investor involvement when, on any sensible view, it is clearly relevant to whether the operators are managing "as a whole".
175. The second point is whether section 235(3)(b) did not, on D1-11's argument, simply duplicate pooling of income or profit under section 235(a): if there was pooling of profit or income there would also be management as a whole, if not, then not. Mr. Sweeting submitted that section 235(3)(b) was there to cater for cases in which section 235(3)(a) was not satisfied because contributions were not pooled. This was not a convincing argument as, if that had been the intention, pooling of contributions and income/profit would have been alternatives, and there would have been no need for "management as a whole". But there are cases in which, even on D1-11's argument, there can be management as a whole without sharing of profit or income e.g. the  **land**  banking cases. Therefore, it is not an objection to D1-11's argument that it would render section 235(3)(b) otiose.

#### The meaning of "as a whole"

176. It is, as always, necessary to consider carefully the language of the statute. Here, section 235(3)(b) does not apply if the property is "managed" by the operator or if the "whole of the management" is by the operator; it has to be "managed as a whole". Reference to a standard dictionary or thesaurus reveals a range of meanings for "as a whole", involving some which approximate to "on the whole". In this context, however, it seems clear, as all parties contend, that what is meant is collective management of Yoni Farm as one entity, as opposed to management of the investors' individual interests.
177. One obvious difficulty is that whether work is done on property "as a whole" or not may differ, depending on from whose perspective one is considering the question. A window cleaning firm employed to clean the windows of a block of flats might see itself as employed to work on the property as a whole, while the owner of each flat might think that his windows were being cleaned. D9-11 submit that what matters is the standpoint of the investor but, since section 235(3)(b) is about management, it seems logical to look at the position of the manager and consider whether from his point of view he is managing the property as one entity. Investors need protection if managers are not looking after their individual interests, which is likely if the managers see their role as to look after a project as a whole. There is in my view no doubt that GMX, and its predecessors, would see themselves as managing Yoni Farm as a whole, as is clear, in the case of GMX, from their actions in 2013.
178. The other question which however arises is, what if some management activities are directed at the property as a whole and others at individual plots. Is it necessary that all management is carried out as a whole, or is it enough that some is? The language is consistent with either. This is an ambiguity which could arise if there were twin investment objectives, e.g. profit from planning permission and in the meantime from agricultural activities, where only one is managed as a whole by the operator. Here it arises because, although the farm is clearly managed as one entity, some management activity is directed at the harvesting of individual plots. This is the key issue in this case.

#### Certainty

179. Certainty is clearly desirable, for the reasons advanced by Mr. Sweeting (see para. 163(f) above), but seems unlikely to be attainable, given (a) the very general concepts used in section 235, which do not lend themselves to precision e.g. day-to-day control: see Brown at [1168], and (b) the requirement to consider the effect of a scheme as it operates in practice, so that whether it is a CIS may vary over time in accordance, not with its terms, but how investors behave. It seems unlikely that certainty can be achieved without the FCA or some other body having the power to give a binding ruling on whether a scheme is a CIS, and the resources to carry out this role; even then there would be the difficulty that it might operate differently in the future. Nevertheless, if a construction of the statute promotes a degree

of certainty, that may be a point in its favour.

The [ ] **land** [ ] banking cases

180. In Sky [ ] **Land** [ ] David Richards J. said at [15]:-

"In my judgment, the test is again directed to the way in which the arrangements in fact operate, rather than requiring there to be an enforceable right of management. Equally, though, it must be a "characteristic" of the arrangements, which suggests that the participants and the operator must share the intention that in practice management of the property will be in the hands of the operator."

181. Apart from this general proposition, the decisions in those cases do not assist in resolving the issue in this case. The

issue was, as David Richards J. said in Sky [ ] **Land** [ ] at [17] what the management activities were, not whether the management was undertaken "as a whole". Having identified the relevant activities as organising planning permission or rezoning, the court in those cases did not have to consider whether they were carried out for the benefit of the scheme as a whole or for individuals - nobody suggested that there was any element

of individual management as regards planning or rezoning. In Sky [ ] **Land** [ ], all the relevant activities, the management of the agricultural enterprise having been eliminated as irrelevant to the investment

objective of the scheme, were carried out as a whole. The same was true in Asset [ ] **Land** [ ] and Chohan.

182. What D1-11 now seek to do, having identified the investment objective correctly as maximising the agricultural yield, is to designate some of the activities having that as their objective as predominant or essential and to disregard the others as remote or subordinate. While criticising Mr. Penny's approach of looking at whether the collective or individual activities are predominant, the defendants' approach differs little from it. There is nothing in the

[ ] **land** [ ] banking cases to justify this approach. They were not, as this case is, cases in which some of the relevant management activities were carried out "as a whole" and some for individuals.

#### PERG and other guidance

183. In my view, PERG does not assist D1-11 either. For ease of reference, I repeat Q.12:

**"Q.12 I run a scheme where each person owns individual properties or parts of properties in the property investment club. Each person owns property either directly, or indirectly (for example,**

through a [ ] **limited** [ ] company or a [ ] **limited** [ ]

**liability partnership of which he is the owner or through a [ ] **limited** [ ] partnership). Is this scheme likely to be a collective investment scheme?**

No, unless the properties belonging to each person, company, [ ] **limited** [ ]

liability partnership or [ ] **limited** [ ] partnership are managed as a whole by or on behalf of the operator of the scheme. So, the mere fact that the operator is managing a number of properties and achieves economies of scale in his management charges or in things such as insurance cover would not mean that the properties are being managed as a whole. Neither would the fact that the operator may be able to offer reductions in sale price because of bulk discounts negotiated with developers. This is provided the operator is managing each property on an individual basis.

**As an example, if a managing agent manages a block of flats on the basis that the only profit or income each individual flat owner obtains is what arises from the management of his property, there is no management as a whole.** However, if the managing agent managed the flats in such a way

that each individual flat owner received an income from total lettings, regardless of whether that person's flat was let or not, the properties are managed as a whole and the arrangements are likely to be a collective investment scheme." (**my emphasis**)

184.D1-11 contend (a) that the effect of the underlined sentence is that, whatever the extent of management by the operator, so long as each investor is paid the income from his property, there is no management as a whole and (b)

that this is a general proposition applicable to the  **African Land**  scheme as to any other.

185.The first reason why this argument must fail is that this is guidance for property investment clubs, which are defined as:

**"Q2. What are property investment clubs?**

In general property investment clubs, (sometimes also known as buy-to-let schemes, buy-to-let syndicates or property investment syndicates) are schemes allowing members of the public to invest in property and which possess some or all of the following characteristics:

- a pooling of resources to allow investment in, or collective management of, real property;
- much or all of the property purchased being financed by money borrowed by the members of the scheme (a typical split being 15% equity and 85% debt), with the borrowing often being arranged by the property investment club itself for members;
- the offer of educational training on the property market;
- other help given to members by the property investment club, including help with the purchase, and the sale, of the property (sometimes involving forward purchase contracts);
- the properties concerned are often newly, or not yet, built; and
- discounts are often offered, or are purported to be offered, on the price of the property (usually from the developer in recognition of a bulk purchase by club members)."

186.D1-11 contend that  **African Land**  falls within the first bullet point of this definition, and that the guidance therefore applies. I reject this. It is true that one can, by a strained interpretation, fit the scheme into this part of the definition, but nobody could sensibly see this as a property investment club. As the front page of the brochure "You invest we harvest" makes clear, it is an investment in an agricultural project.

187.Secondly, what the guidance primarily covers are buy-to-let investments, where the investor will own a property which will yield an income without the management activities having to include the constant application of sophisticated expertise, and where the investor is likely to take the main commercial decisions himself, or at least be consulted about them.

188.Thus what PERG 11 contemplates is a situation in which the operator will provide possibly extensive management services collectively, but is likely to look after the essential profit-generating activity, letting the flat, under the instructions of, or at least in consultation with, the individual owner. That, is what, in the FCA's view, is not management "as a whole".

189.That this is what PERG 11 has in mind is in my view clear from the whole tenor of the guidance, which relates to property investments, without ever suggesting that it is contemplated that the owners will delegate to a manager (let alone be obliged to delegate to a manager) all the main decisions about the property. Q.7 and Q.12 itself show what kind of management is contemplated e.g. cleaning, insurance cover. Where the main decisions are in the hands of the manager, the position is different: see Q.14.

190.In my view, D1-11 place too much weight on one sentence in the answer to Q.12. Read literally, it could bear the suggested meaning, but read as a whole, particularly with the earlier reference to "the mere fact" followed by

"economic of such in management charges" it is clear that overall management of the property is not contemplated.

191.D1-11 are perhaps on stronger ground with the informal guidance given by the FCA, especially in relation to hotels, where the investment was, typically, the income from a room for a week, with the room rotated each year so as to give a spread over time of different quality rooms.

192.Mr. Bretherton's letters say that hotel is not managed as a whole and that the rooms are managed individually, but it seems obvious that this can only be true in the sense that income from each room is segregated and paid to the individual entitled to it, which is a bookkeeping and accounting exercise. There is nothing in the Room to Invest brochure to suggest any individual treatment of investors, apart from being paid the income from their room for the year. Everything else - maintaining and cleaning the hotel, including all the rooms, (or all those that were part of the scheme, if it relates to part of the hotel only), restaurant facilities, and in the case of the Room to Invest the roof terrace and the steam bath facilities – could hardly be organised otherwise than as one operation by the operator itself or a firm engaged by it, unless (of which there is no sign in the brochure) there was a separate management company to be run by the investors and not the operators or (possibly) the operators merely leased rooms in an independently managed hotel. The same is true of the allocation of rooms to guests who have no definite wishes. It would be surprising if such a scheme was not regarded as collective, since the investors, unlike buy-to-let investors, would not be in a position to decide anything of significance, or even to be consulted. They would have no means of monitoring, for example, whether guests would be allocated first to rooms which belonged to other investors, or had not been sold to an investor and remained with the hotel operator.

193.Nevertheless, the FCA expressed the view, without further enquiry, that such schemes were not CISs, and logically it can be said that this is consistent only with D1-11's argument, that if income is paid to investors from their separate property, that is enough to take the scheme outside both section 235(3)(a) and (b). Whether Mr. Bretherton's assertions had the effect of taking the FCA's eye off the ball is unclear, but to say that such schemes are not CISs is in my view inconsistent with the FCA's argument in this case.

194.However, I do not think that this helps the defendants. It would only assist their argument if it gave rise to a presumption. It is unnecessary to decide whether PERG would give rise to a presumption, despite PERG 1.2.2 and 1.3.1 (see paras. 130-1 above), since I do not think that it contains any relevant guidance. But I do not consider that informal guidance given in response to short letters which are vague on important matters, do not frankly draw attention to obvious difficulties, and anyhow relate to different schemes, can possibly give rise to a presumption; nor is it at all persuasive. I doubt the utility of guidance being given on particular schemes without fuller details than are provided in Mr. Bretherton's letters; section 235 requires the separate consideration of several concepts, not easily undertaken where there is doubt without a comprehensive description of the proposed scheme.

#### The right test?

195.The issue, as I have said earlier, is whether the property is "managed as a whole" if all the management activities are carried out by or on behalf of the operator, but some are carried out in the interests of the body of investors and others in the interests of individual investors. As a matter of language, it could be said that the property is managed "as a whole" if the manager is responsible for its entire management, irrespective of whether all or any of it is directed at the individual interests of investors. Equally, it could be said that the property is not managed "as a whole", if there is any element at all of individual management. Given the purpose of section 235(3)(b), neither of these extreme interpretations is attractive; what must be sought is an interpretation that catches what might realistically be regarded as collective management, requiring protection for individuals' interests.

196.The FCA's approach is in essence a balancing exercise, or a search for the winner, even if only by a narrow margin, as between the collective and individual elements of management. The difficulty with this is that there may be, and in this case are, many and various management activities, and ascribing the correct weight to each is an arbitrary and unsatisfactory task. Further, if the conclusion is that the collective elements outweigh the individual only by a little, it does not seem right to refer to the property as being "managed as a whole". The bar is set too low.

197.D1-11's approach is essentially to isolate the supposed "core" activity at Yoni Farm, while rejecting as too remote many others of obvious importance in achieving the investment objective, without which not a grain of rice would grow. Further, it involves treating elements of management - cultivation, application of fertilizer, weed control etc - as individual management activities, because they are carried out on each plot, whereas from the manager's point of view they are just part of the management of the farm in its entirety. Another objection to this approach is that it treats segregation of income as conclusive, of itself excluding management as a whole, irrespective of how management is in fact performed.

198.Having regard to the objective of the sub-section, to protect investors where there is collective management, in my view the correct test is whether the elements of individual management, arising either from attention given by the management to the interests of individual investors, or from participation by the investors themselves in the management of the property, is substantial. If so, the management by or on behalf of the operator is not to be regarded

as management "as a whole".

199. Mr. Sweeting submits that a first instance judge should not be tempted to embroider the language of a statute, and that is surely good advice – but the language in my view leaves an ambiguity which has to be resolved. Although what I have suggested is imprecise and perhaps not very satisfactory, it is difficult to avoid the need for some quantitative and qualitative assessment of the management of the scheme, unless one takes the view, which I do not, that what is required for management as a whole is the complete absence of any element of individual management.

#### Individual and collective management in this case

200. Applying this test, I agree with Mr. Penny that GMX and its predecessors have managed Yoni Farm as an entire project, and that the element of individual management in [redacted] **African Land** [redacted] is minimal.

The terms and conditions make [redacted] **African Land** [redacted] entirely responsible for the management of the investors' plots. Investors have no control whatsoever over the management of Yoni Farm, or of their individual plots. They are not, and do not expect to be, consulted on anything. From the point of view of GMX and its predecessors, virtually anything they do is planned and carried out as a whole, even where it is carried out on individual plots. The updates (para. 93 above) provide an accurate picture. What rice is grown, and how, is entirely in the hand of the management, and fundamental decisions which may affect yield, such as what variety of rice to grow, or whether to spend available funds on irrigation or on cultivation, are taken by the management.

201. Furthermore, the only element of management which can sensibly be regarded as individual as opposed to collective, the segregation of plots for separate harvesting, while genuine, (a) has no real commercial purpose and (b) does not benefit investors; its only purpose is to attempt to take the scheme outside section 235 so as to be able to proceed without regulation. From the investors' point of view, their plots are selected at random, and there is no expectation that a particular plot will produce a higher or lower yield, even if sometimes this may happen fortuitously, as in the case of the lucky owners of 13 hectares, and the unlucky owners of 300 acres, in 2013. As the discussion with Ms. Botto (para. 109 above) illustrates, a sub-lease entitling the investor to a proportion of pooled profits, corresponding to the size of his plot, would be just as good, indeed better as the expense and delay involved in individual harvesting (see paras. 93(e), 105, 107 above) would be avoided. Therefore, in any qualitative assessment of the importance of individual management, this element of it counts for little.

202. For these reasons, in my opinion, section 235 applies to this scheme whether the right test is Mr. Penny's or mine. Whether looked at quantitatively or qualitatively, the individual element of management in this scheme is small, and the investors themselves do not participate at all in management decisions, even if in theory they could. Only if, on the proper construction of section 235(3)(b), any individual element of management is sufficient to exclude management "as a whole" does the scheme escape. That is, as a matter of language, a possible construction, and it does have the advantage of promoting certainty, since all that is then required to avoid both (a) and (b) of section 235 is to provide separate property and income. But in my view such a construction does not accord with the basic purpose of the legislation, to protect investors where this is necessary because of either pooling or collective management, and it should be rejected.

#### Conclusion

203. For these reasons I hold that the [redacted] **African Land** [redacted] scheme is and always has been a CIS.

#### The CCC Schemes

##### Overview

204. These schemes are all operated by D13, but there is no evidence from D14 or D15, the principal persons concerned with the management of D13, and therefore little direct evidence as to how they have been operated in practice, except in the case of the Australian scheme, in relation to which Mr. MacNee, the managing director of its accreditation manager, Citola Resources Pty. Ltd. ("Citola"), gave evidence.

205. The essence of each of these schemes, said by D1-8 to be based on the FCA's guidance (see para. 144-5 above), is that D13 would acquire a lease of an area of forest [redacted] **land** [redacted], which would be split into specific plots to be allocated to individual investors, who would then be entitled to the proceeds of carbon credits generated by their individual plots.



206. Assuming that the schemes operate in accordance with this description, this gives rise to two issues.

207. The first issue is whether, on the assumption that the total number or tradeable carbon credits were awarded the operator of each scheme, but they were then allocated to investors in accordance with the individually measured proportions of the total credits attributable to their individual plots, this represents "pooling" within the meaning of section 235(3)(a). In my opinion, for the reasons given later, it does not.

208. The second issue is whether, in circumstances in which the entirety of the management of the project is in the hands of D13, and in which there is neither evidence of investors having any involvement in it, nor any realistic prospect of this ever happening, there is "management as a whole" despite individual allocation of the income described above.

On this, for the same reasons as I have given in relation to the [redacted] **African Land** [redacted] scheme, there is "management as a whole" within section 235(3)(b).

209. There are also issues as to whether in fact the schemes are in fact intended to be operated in such a way as to make it possible for individual income to be allocated in accordance with the terms of the schemes. Since none of the schemes has so far generated any carbon credits, it is not entirely easy to deal with this but, for the reasons discussed below, I find that there is and always has been such an intention in the Australian reforestation scheme, but not in either of the forest preservation schemes.

210. For the reasons given earlier, I do not think that any presumption can arise from the informal guidance (paras. 144-5, 194 above); Mr. Bretherton's letter is not forthcoming on the details or extent of the individual management of the proposed scheme, and his reliance on a right of personal management unlikely in practice to be exercised by most investors as meaning that there is no management as a whole is misplaced. Anyhow, the guidance is non-committal.

#### The CCC Australia scheme

211. This scheme relates to Australian Statutory Carbon Credits ("ACCUs"), issued under the terms of the Australian Government's Carbon Farming Initiative ("CFI"), which is a carbon off-set scheme relating to reforestation.

212. The front page of the brochure refers to "Sustainable Forestry The New Asset Class" and describes "Australian Reforestation" as "an investment that brings real, ethical returns in the secure legal environment of Australia".

213. The Key Parties are D13 and D2 as Receiving Agent, and next to this the Carbon Farming Initiative is said to incentivise landowners "to return cleared, unutilised [redacted] **land** [redacted] to native woodland and earn fully registered and tradable ACCUs in the process".

214. On page 4, what is being offered is defined as a licence for a 15 year term of a ½ hectare plot within a 320 hectare area of approved [redacted] **land** [redacted] located in the Gippsland region of Victoria, qualifying under the CFI project by reason of having been cleared before 1990, at a price of £9,000 per plot, including all planting, management, maintenance, administrative and insurance costs.

215. The "preferred Project Developer", Citola, is to manage the project "from seedling propagation, planting, care, maintenance and monitoring of the woodland through to accreditation and the issue of tradable ACCUs", and including all establishment and management costs and fees including insurance.

216. The predicted minimum return is 49% rising to 365% depending on which option is selected.

217. Page 7 gives more detail about Citola:

"Each State will maintain a list of ROEs (Registered Off-set Entities) operating within its territory on the basis of "an approved and verified methodology" to fulfil the sustainable forestry and CFI aims ...

[D12] has teamed up with Citola Resources, a leading carbon expert in carbon forestry and reforestation in Australia. Citola Resources already has full ROE status and approved projects across the country ... this means that [it] will be able to deal directly with the regulator to achieve 'Eligible Off-set Project'

status for your [redacted] **land** [redacted] and obtain the necessary 'Certificate of Entitlement' to ACCUs ... we believe Citola Resources, as a leading ROE, will maximise your carbon credit yield."

218. Investors are offered the option of choosing another ROE to manage the  land , in which event the initial investment is reduced to £6,950 per plot, but there is no evidence that any investor has done this.

219. Page 9 describes the management process in some detail, stating that it includes intensive weed control, selective fertiliser applications, pruning to maximise consistent form and tree growth, remedial design to optimise plantation structure and efficiency and "pro-active/reactive plantation inputs".

220. Monitoring and verification are also described. Monitoring was to take place about 7 times in the first year and 4 times in the next 2 years to check on general tree health and vigour and various other matters. Prior to the application for ACCUs, the project and on-site carbon yield was to be independently verified.

221. Page 11 states that the 15-year licence over each plot will provide that "the beneficial interest in the Forestry Property Rights will vest with the investor for the duration of the Project" and that such rights "give investors the exclusive right to plant, maintain and own all parts of the trees on their plot including the Carbon Sequestration Benefits".

222. Page 12 states that the exit options available to investors were forward sale, "make your own arrangements to sell ACCUs in your own account" and retaining them for the full life of the project and obtaining the long-term value.

223. As regards the second of these options, each investor is stated to be eligible to obtain an Australian National Registry of Emissions Unit ("ANREU") account to receive their own certificate of entitlement, enabling them to dispose, sell or transfer ACCUs within in Australia or into a foreign registry account.

224. For those taking the third route, retention for the full period of the project, the annualised return over 15 years is projected to be between 14.8% and 24.3%.

225. On this basis, investors are urged to participate in a truly ethical and environmentally friendly project, which will deliver on sustainability, environment protection and carbon reduction, and represents a premium forestry investment. The risk warnings include a warranty by the purchaser that he is aware that the project is not regulated by the FCA and is not a collective investment scheme, and that he will therefore have no recourse to statutory or regulatory protections.

226. The detailed terms and conditions provided that, within 28 days of receipt of a duly completed application form, the investor would receive confirmation of the Plot(s) allocated to them by way of a Licence Certificate, and the terms and conditions also included the following:-

### "3. LICENCE ...

(iii) The Licence Covenant Registration will take place no later than 18 months from the date recorded on the Licence Certificate providing Investors the exclusive right plant, maintain and own all Carbon Sequestration rights in accordance with the CFI Act 1996;

(iv) upon payment of the Management and Accreditation Fee, the Investor irrevocably and unconditionally agrees to the Project Developer being solely responsible for Project on behalf of the Investor for the term of the Licence in accordance with Part 10 of the CC (CFI) Act 2011;

(v) Ownership of seedlings, harvest, machinery and any intellectual property rights developed and maintained by the Project Developer remain with the Project Developer and Landholder during the Licence Term. The Plots) remains the property of the Landholder;

(vi) The Investor is unconditionally the sole beneficial owner of any ACCUs issued on the Investor's Plot(s);

(vii) The Company reserves the right to defer the date for performance of, or issue of the ACCUs units, or to terminate this Licence, if it is prevented from, or delayed in, carrying on its activities by acts, events, omissions or accidents, beyond its reasonable control, including (without limitation) strikes, lockouts or other industrial disputes (whether involving the workforce involved in the project or any other party), failure of a utility service or transport network, act of God, war, riot, civil commotion, malicious damage, compliance with any law or governmental order, rule, regulation or direction, accident, breakdown of plant or machinery, fire, flood, storm, crop failure or default of suppliers or subcontractors;

(viii) the Investor accepts that the Licence issued over the Plot(s) for exclusive purpose and use of the Project;

(ix) the Investor hereby acknowledges that the Company shall be entitled in its absolute discretion to allocate the Plot(s) within the Licensed Area on behalf of the Investor provided the total area of the Plot(s) is not reduced; and ...".

There are also various disclaimers, including that D12 had no specialist knowledge and could not guarantee that the price paid for the licence represented market value or that the projections set out in the document would be realised.

227. The "Project Developer" is defined as Citola Resources Pty Ltd, and the Landowner as Forestry

**Land**  Resources Pty Ltd, a subsidiary of Citola.

228. "Licence" is defined as "the issue of a licence over the ACCUs that will be produced from 1/2 hectare plot(s) granted to the Investor for the term in accordance with the terms and conditions set out in this Offer".

229. In my view, the FCA is right to say that, although some parts of the brochures do suggest that investors will acquire a 15-year licence over the half hectare plot, on a careful reading of the terms and conditions (3(v) and (vi) above), the plot remains the property of the D13 and the investor is merely the beneficial owner of "any ACCUs issued on (his) Plot(s)". This leaves open the method of attributing ACCUs, to individual plots, and in particular whether it will be rateable according to the size of the plot or in accordance with the measurements of the trees on each individual plot.

230. An informal meeting was held between Ms. Durham and Mr. Edwards of the FCA and Mr. Christopher MacNee and Mr. Murray of Citola on 21<sup>st</sup> August 2013. Ms. Durham made a note of the meeting, but did not send it to Citola.

231. Mr. MacNee said that Mr. Haddow had approached Citola in October 2011 to provide forestry services in connection

with the proposed scheme under the CFI: Citola was to acquire the  **land**  through its subsidiary and to provide forestry services for A\$10,000 per hectare, including registration of the property as forest and later registration of the carbon credits when the planted trees reached a certain level of maturity, usually after 2-3 years.

232. This led to a contract being entered into on 24<sup>th</sup> January 2012, which had been negotiated with Ms. Hargous. This specified what Citola was to do, and the milestones to be reached before payments were made. The project was divided into two phases, the first consisting of a plantable area of 130 hectares; planting had been completed on Good Friday 2013. Phase I comprised 130 plantable hectares divided into 260 half hectare plots, each of approximately 20 x 30 metres. Phase II would be 234 plantable hectares, divided into 468 half hectare plots.

233. As to the investors' option to appoint their own project developer, Mr. MacNee and Mr. Murray both said that this was possible in theory, but would be very difficult, and would necessitate allocation of plots to those investors round the periphery.

234. The FCA's note states as follows:-

**"CM said ... that the calculation of the CCs generated per plot was based upon the amount of carbon sequestered across the whole site and divided by the number of plots. It was not feasible to measure the CCs generated by individual plots." (my emphasis)**

235. Mr. MacNee said that D12 owed Citola some A\$350,000.

236. Mr. MacNee then provided the FCA with a short statement summarising what he had told them, and stating that the project development and management being conducted to the highest professional standard, that there had been several project reports; Citola was a public company, and a government contractor including in relation to the provision of carbon offsets.

237. Mr. MacNee also answered a request from Ms. Hargous for "clarification that the project has not been developed as a collective scheme" in the following terms is:-

"7. Within three years (between one and half to two years from the project being established – Easter 2013 – and depending on growth rates of the trees, an accredited

group will verify and register the project with the authorities under the current legislation namely the Carbon Farming Initiative (CFI).

8. Each owner of plot(s) or rights holder, can them, should he or she decide, open a carbon registry account – ANREU (Australian National Register of Emission Units) in their own name to hold the Australian Carbon Credit Units (ACCUs) generated on their plot(s).

9. The Company (RPL) will also open an ANREU account.

**10. Once the project is registered under the CFI as explained above, the carbon yields of each plot are measured on an annual basis (by measuring the growth of the trees). This should be in accordance with the models and methodology used at the time and based on specific growth and carbon sequestration rates of tree species in each individual and specific plot. We have endeavoured to plant each plot identical i.e. with same number of tree species, remembering that this is not a monoculture plantation but plots of bio-diverse plantings and hence creates further plot uniqueness.**

**11. Once measured the ACCUs are deposited into the ANREU account of the plot owner or if the owner is not able to open an ANREU account into the account of the RPL which will then distribute them on behalf of the plot(s) owner.**

12. From this account the owner can sell his credits to regulated traders or companies (or based on proposed legislation not yet approved to the government through their Direct Action plan).

13. The plot owner has the right to sell his plot(s) at anytime at fair market rates.

14. The project is designed to a 15 year life cycle (based on growth rates of trees in the region)." (**my emphasis**)

238. Accordingly Mr. MacNee gave evidence against a background in which there was a difference between what he was recorded as having told the FCA on the important question of the individual measurement of the yield from each plot, and what he says in paras. 10-12 of his response to Ms. Hargous. In cross-examination, he said that what he had told the FCA had not been correct.

239. The agreement between D13 and Citola dated 24<sup>th</sup> January 2012 is described as an Agreement for the Provision General Services: Asset Management Agreement.

240. Carbon Sequestration Rights are defined as "the exclusive economic rights to economic benefits associated with the carbon sequestered by the trees as recognised under or provided for in the Act" (i.e. the 2011 Act).

241. Citola's Services are defined in Schedule 2 and 3: it is unnecessary to go into detail, these schedules demonstrate that Citola has the entire management of the project.

242. Clause 2.2(a) provides that Citola's subsidiary, the landholder, will grant Citola "exclusive Carbon Sequestration Rights over the Planted Area for the purposes of the Project".

243. Clause 2.2(b) provides that D13 will have the exclusive right to all ACCUs subject to payment to Citola as specified in the agreement.

244. Clause 2.2(c) provides that Citola will transfer all ACCUs to D13's ANREU account for the term of the project.

245. Clause 2.2(d) provides that Citola will provide to D13 plot certificates for each plot at the appropriate stage (as defined) in the implementation of the project.

246. Schedule 2 item 5 repeats clause 2.2, and further provides that Citola will design the project according to the Reforestation – Environmental Planting methodology developed and approved by the Australian Department of Climate Change and Energy Efficiency, as a "Single Project Proponent", and that it would provide copies of Project Reports at the end of each Reporting Period.

247. There are project reports dated June 2012 and February 2013, and these demonstrate, (if any further demonstration is

needed) that the project is managed in its entirety by Citola on behalf of D13.

248. In his oral evidence, Mr. MacNee provided a very interesting description of the methods used to develop a project of this kind, and the stage which it must reach before ACCUs can be applied for, a stage which has so far not been reached. The important point for the purposes of this case is that I am satisfied by Mr. MacNee's evidence that Mr. Haddow and Ms. Hargous explained to him, his brother and co-director and Mr. Murray that it would be necessary to ensure that each investor received the proportion of ACCUs which represented the performance of his own individual plot, and that this would be measured by the foresters who:-

"would get as close as possible to the real calculation of their particular acreage ... [so that investors] ... would receive the carbon credit equivalent to what their holdings would be ... they would get that, not pro rata, but..pretty close to what it should be based on growth rates."

249. Mr. MacNee said that it was not possible to take measurements until somewhere between 18 months and 3 years after planting, and that the trees were still too thin. When the time came, one of Citola's duties would be to provide it with a report, which would enable D13 to divide up the ACCUs in accordance with the performance of each plot.

250. Mr. MacNee's evidence that it is possible to measure the individual plots' entitlement to carbon credits is supported by the evidence of Mr. McKendrick that he had had experience of a carbon sequestration scheme in which this was done, and that it was an important element of such schemes.

251. Although Citola might be said to have some interest in the outcome of this case, since recovery of what is owed to it might well be less likely if the scheme is held to be a CIS, Mr. MacNee was a transparently honest witness, and I accept his evidence that, despite the absence from the terms and conditions of any provision defining how the ACCUs attributable to individual plots were to be ascertained, this was and remains the intention in the Australian CCC scheme.

#### The elements of a CIS

##### Arrangements

252. I find that there are arrangements, in accordance with the terms of the brochure, relating to property, from which investors are intended to derive profit.

##### The property

253. I find that the property, for the purposes of this scheme, is the whole of the forest area; that is what Citola is managing, and investors are intended to benefit from the overall management of the project, including for example "permanent" areas, not owned by investors, but set aside for the purposes of research and experiments, and not only from their own individual plots.

##### Day-to-day control over management

254. As with  **African Land** , although in theory investors can, in accordance with the terms and conditions, take control over the day to day management, and Mr. MacNee evidence suggests that this would not be unusual, there is no evidence that it has in fact happened.

##### Pooling

255. As I have already said, this has its ordinary meaning, and the question is whether the profits are to be combined for the common benefit. The factual position is that the ACCUs, if any, will be awarded to D13, and will then be divided between investors in accordance with the performance of their individual plots.

256. Mr. Penny submits that, whatever the ultimate division, the award of the total number of ACCUs attributable to the forest area to D13 means that the profits are pooled, as well as the contributions which, it is to be inferred, have been pooled in order to meet the expenses of the scheme. I do not accept this. If the operator is to distribute the ACCUs, it obtains no benefit, whether common or combined or otherwise, as it has no beneficial interest. If they are then distributed between the investors in accordance with the yield of performance of their own individual plots, there is still no common or combined benefit. Therefore, in my opinion, there is no pooling if the ACCUs are not divided rateably in accordance with the areas of investors' plots, but in accordance with the amount of carbon benefit generated by each plot individually, section 235(3)(a) is not engaged.

257.Mr. Penny also submits that section 235(3)(a) is satisfied because any refunds due under the terms and conditions could not be made except out of the proceeds of contributions; that may be so, but the payment of a refund would not be a payment of profits or income, and so would not fall within section 235(3)(a).

#### Management as a whole

258.Finally, there is again "management as a whole". I find that section 235(3)(b) is satisfied, for all the reasons given in relation to [redacted] **African Land** [redacted]. The property (whether it is the whole forest or just the totality of plots allocated to investors so far) is clearly being managed in its entirety by Citola on behalf of D13, the terms and conditions do not provide for any input into management by investors, or consultation with investors, and there is no evidence of any such management or consultation in practice.

259.As in the case of [redacted] **African Land** [redacted], it is true that trees are planted on each plot, but the decision what to plant (according to Mr. MacNee an identical mixture of different trees on each plot) is that of the management, and I do not regard this as an element of individual management. There is again only the allocation of profit to individual plots. As in the case of [redacted] **African Land** [redacted], this has no economic purpose, since there is no difference at the outset between the expected yield of one plot as against another, and the sole or main purpose is to allow the promoters and operators of the scheme to be unauthorised persons.

#### Conclusion

260.I conclude that the Australian CCC Scheme is and always has been managed as a whole by Citola on behalf of D13.

#### The CCC Sierra Leone and Brazilian schemes

261.It is unnecessary to set out the content of the brochures for these schemes in great detail. The benefits of it are described in broadly the same terms as the Australian scheme. In each case D13 is the operator and there is a separate "project developer/accreditation specialist", Eco Securities Group plc ("Eco").

262.However, Eco, a subsidiary of JP Morgan, objected and was swiftly replaced by Climate Care Global [redacted] **Limited** [redacted] ("CCG") of which D15 was a director, and which has been struck off the register. The evidence suggests that CCG is so named so as to resemble a former subsidiary of JP Morgan with a reputation in the field, and that has neither the standing nor, probably (having regard to the lack of progress in both schemes), the expertise of Citola.

263.In each case, the main features of the scheme are as follows:-

(a) Carbon credit potential generated through Reducing Emissions from Deforestation and Forest Degradation in Developing Countries ("REDD") Scheme.

(b) Ethical carbon off-setting generating VER (voluntary emissions reductions) carbon credits, which can be traded.

(c) Investors buy sub-leases of one hectare plot(s), for a term of 45 years.

(d) Investors have the option to appoint own manager with a reduction in price.

(e) Full money back guarantee (not including accreditation fees) if the [redacted]

**land** [redacted] is not granted carbon credits within three years of the investment.

(f) The terms and conditions provide that on payment of the accreditation fee (i.e. unless appointing their own manager) investors "irrevocably and unconditionally agree to D13

being solely responsible for managing the [ ] **land** [ ] and the Carbon Credit Accreditation Process" on their behalf.

(g) The terms and conditions refer to the sublease as "your legal ownership over the [ ] **land** [ ]".

(h) By the terms and conditions, D13 is to procure that investors will receive their "Carbon Credit Allocation" within three years, and Carbon Credit is defined as –

"...the number of carbon credits attributed to an investor's plot in accordance with the Accreditation Agency (which is Eco Securities or CCG)".

264. There is nothing in the brochures, or in the terms and conditions, for either of these schemes to make it clear whether the carbon credits attributable to each plot were to be separately measured, or were to be a proportion, referable to the area of the plot, of the whole of the forest's allocation. It is the evidence of Ms. Hargous that it was her (and by

implication that of her colleagues) understanding that satellite imagery for each plot of [ ]

**land** [ ] could be used to determine tree heights and types, so as to give each plot of [ ]

**land** [ ] a carbon credit value. I accept her evidence as to what she understood, which is consistent with the evidence relating to the CCC Australia scheme. However, the evidence to which I refer below suggests that this is not what D13 or CCG ever intended to provide or did provide.

265. If the schemes had proceeded on the basis of the brochures, with the intention of measuring individually the carbon credit values of each plot, I would have held that the scheme did not involve the pooling of profits or income, as and when earned, but did involve management "as a whole", and was therefore a CIS, for all the reasons given earlier in relation to the other schemes.

266. However, the evidence as to the progress of the Sierra Leone project is as follows:-

(a) The evidence as to D13's ownership of [ ] **land** [ ] is unsatisfactory. Mr. McKendrick's evidence is that he was involved in obtaining options to lease in 2010, which were assigned to D13 in December 2010, and there is an agreement and undertaking dated 28<sup>th</sup> September 2010 between the Paramount Chief of the relevant area and "Agri Capital" of Freetown, Sierra Leone, for a lease of 50,000 acres of virgin

forest [ ] **land** [ ] for a rent to be agreed, followed by three leases dated between June and September 2012, all of which (despite the evidence as to

assignment) are in the name of [ ] **African Land Limited** [ ].

(b) There is no clear evidence as to the progress of attempts to obtain carbon credit accreditation. Communications with investors have been to the effect that documents have been submitted, but that accreditation was still some time in the future. The APX VCS Registry, which is the registry through which transfers of VCUs would be effected, has provided evidence that an account was opened by D15 in mid-2012, with the Sierra Leone project listed as a new project, but no documents were submitted and the account

was closed on 3<sup>rd</sup> December 2012; a document issued by Co2balance UK [ ]

**Limited** [ ], a project developer, shows that it had prepared a feasibility study, and estimated that obtaining registration for the project would cost in excess of £150,000.

(c) The feasibility study and project development study prepared by CCG say that

conservation of forest [redacted] **land** [redacted] would be achieved by activities on non-forest [redacted] **land** [redacted], including the creation of a protected area, working with communities to identify sustainable and used practices and planting community wood lots for fuel wood and construction materials. Similarly, a Co2balance proposal suggests four key activities, namely forest patrols, improved forest management, biomass pellet production using waste residue from rice production and reforestation of degraded areas. It is difficult to see how the income from any of these could be allocated otherwise than by pooling.

(d) The witness statement of Mr. Barrington, an investor, evidences a meeting with D14 on 6<sup>th</sup> November 2012, referred to in a contemporaneous email to another witness, Mr. Skeels, a chartered management accountant who has been conducting research and analysis in the area of alternative investments for some years. At that meeting, D14 said that the yield of 400 carbon credits per hectare suggested in the brochures would not be achieved, and that he proposed –

"...that no more than 10% of the forest be sold to investors, i.e. 5000ha. They will use the credits attaching to the 90% to fulfil their obligations to investors..."

267. The evidence as to the Brazil scheme is virtually non-existent. There is a brief feasibility study prepared by CCG, again referring to other activities, which would not be capable of being related to individual plots. There is no evidence of any [redacted] **land** [redacted] having been leased or otherwise acquired, enabling D13 to fulfil its promise to sub-lease to investors. Ms. Hargous says in her witness statement that she was told in January 2012 that the scheme was not viable, and several investors have been told this, but there have been no refunds.

268. It is difficult to know, from the sparse evidence available, what has been going on in either scheme but in relation to both the starting point, as in the Australia scheme, is that there is no provision for measurement of carbon benefit on individual plots. However, unlike in the Australia scheme, there is no evidence at all that consideration has been given to establishing a method for measuring the carbon credit value of each plot individually, or for appointing a firm, such as Citola, that would be able to achieve this.

269. Further, an internal email sent by D14 on 4<sup>th</sup> May 2012 suggests that it was never contemplated that there would be individual measurement:-

"If the costs of letting one client do this are approved or covered, then the individual accreditation is done on one hectare at a time to take into account the divide of [redacted] **land** [redacted] then yet it can be done! Those costs would probably be in the region of Â£1m.

Surely it is easier to sell the product you have, not one that is tailored to every single client. ... If we went down that route we would have to register each plot as a separate accreditation."

Although this refers to the cost of seeking individual accreditation rather than the cost of individual measurement of the carbon credit value of each plot, it suggests that D13 had no intention of incurring what would no doubt be the considerable cost of carrying out the latter in these vast areas.

270. Therefore, I find on the balance of probabilities that the intention of D13 (but not of Ms. Hargous) at the time these schemes were promoted and thereafter was that the accreditation manager/specialist should seek one allocation of VCUs for each of the schemes, if they ever got that far, which would be shared rateably between investors in accordance with the size of their plots. It follows that, on any view, on the proper construction of section 235 the intention of the operator of both these schemes was both to pool profit/income and to manage them as a whole.

### Conclusion

271. For these reasons I hold that there is both pooling within section 235(a) and management as a whole within section 235(3)(b) in both these schemes.

### **Overall conclusion**



272.I declare that all the schemes under consideration are, and have been since their inception, collective investment schemes within the meaning of FSMA section 235.

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