



NUS Law Working Paper 2018/013
NUS Centre for Banking & Finance Law Working Paper 18/02

Collective Investment, Property and Coin Schemes

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[April 2018]

This paper can be downloaded without charge at the National University of Singapore, Faculty of Law Working Paper Series index: <http://law.nus.edu.sg/wps/>

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Collective Investment, Property and Coin Schemes*

Introduction

This paper sets out the decision of the UK Supreme Court in *Asset Land Plc v FCA* [2016] UKSC 17 where it was held that the land banking scheme there required authorization as a collective investment scheme. The HK definition is quite similar as is how authorisation works in practice which is that, without it, schemes can only be offered to sophisticated investors. The position in Singapore was and is different. Definitional changes were only made in 2017 to remove the concurrent requirements of pooling and external management, which kept land banking schemes outside the regulatory regime. These are not in force yet, which in Singapore means that they can be sold to the public generally (subject to consumer protection laws). Amongst other things to be discussed are how regulatory statutes should be interpreted, whether and how much deference should be given to the views of the regulators, and its ramifications for other areas like initial coin offerings.

Collective Investment Schemes

In Singapore, the Monetary Authority of Singapore has traditionally said that land banking schemes were not considered collective investment schemes and consequently outside the scope of the Securities and Futures Act (Cap 289). For example, in July 2010, MAS stated that:

Land-banking investments involve investors acquiring direct interests in real estate rather than in securities related to real estate and, as such, fall outside the scope of the SFA and FAA.¹

Being outside the collective investment scheme regime, like timeshares and club memberships, these could be sold generally to the investing public without the need to comply with the prospectus requirements of the SFA. Nor did the sales of such investments require any capital markets services licence to deal in capital markets products. These difficulties will largely be removed by an amendment to the definition of collective investment schemes introduced by the Securities and Futures (Amendment) Act 2017. This was passed in January 2017 but has not yet come into force. Amongst the changes are:

- An amended definition of “collective investment scheme” to address the land-banking problem so that it is closer to the UK definition in the Financial Services and Markets Act 2000 in that it can have the characteristic of having contributions from and profits of investors pooled (which may not initially be the case with some “land banking” schemes), *or* the property managed by a

* Hans Tjio, Professor, Faculty of Law, National University of Singapore. I would like to thank Professor Alexander Loke, Karen Man and Dominika Nestarcova for helpful suggestions and constructive comments. I would also like to thank all the participants at the *Symposium on Hedge Funds and Alternative Investment Funds in Hong Kong and Singapore* jointly organized by the Centre for Commercial and Maritime Law, City University, Hong Kong and Centre for Banking and Finance Law, NUS, and held at the School of Law, City University, Hong Kong on 20 April 2018.

¹ Lee Hanqing, ‘200 lost \$6m in land deals’ *Straits Times*, 14 May 2010.

manager for the investors (and not both as previously required under the Securities and Futures Act).²

- Amending the definition of “accredited investor” requiring that the net value of the person’s primary residence not be more than half of the total net personal assets exceeding \$2,000,000 or its equivalent in foreign currencies (which is the primary individual accredited investor test in section 4A), but with a new alternative test where a person has more than \$1,000,000 in net financial assets. Another change to be introduced by way of subsidiary legislation in the form of regulations is to allow “accredited investors” to “opt-in” before they are treated as such.

With these changes that have not come into force, “collective investment scheme” will mean:

- (a) an arrangement in respect of any property —
 - (i) under which the 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 in respect of such management;
 - (ii) under which any of the following characteristics are present —
 - (A) the property is managed as a whole by or on behalf of a manager; **or**
 - (B) the contributions of the participants and the profits or income out of which payments are to be made to them are pooled; and
 - (iii) under which either or both of the following characteristics are present:
 - (A) the effect of the arrangement is to enable the participants (whether by acquiring any right, interest, title or benefit in the property or any part of the property or otherwise) —
 - (AA) to participate in or receive profits, income, or other payments or returns arising from the acquisition, holding, management or disposal, exercise, redemption or expiry of, any right, interest, title or benefit in the property or any part of the property; or
 - (AB) to receive sums paid out of such profits, income, or other payments or returns;
 - (B) the purpose, purported purpose or purported effect of the arrangement is to enable the participants (whether by acquiring any right, interest, title or benefit in the property or any part of the property or otherwise) —
 - (BA) to participate in or receive profits, income, or other payments or returns arising from the acquisition, holding, management or disposal, exercise, redemption or expiry of, any right, interest, title or benefit in the property or any part of the property; or

² MAS Consultation Paper, P012-2014, Proposals to Enhance Regulatory Safeguards for Investors in the Capital Markets, July 2014. MAS also proposed that issuers of retail investment products be required to rate products for complexity and risks and to disclose their rating.

(BB) to receive sums paid out of such profits, income, or other payments or returns, whether or not –

(I) the arrangement provides for the participants to receive any benefit other than those set out in sub-paragraph (BA) or (BB) in the event that the purpose, purported purpose or purported effect is not realized; or

(II) the purpose, purported purpose or purported effect is realized; or

(b) an arrangement which is an arrangement, or is of a class or description of arrangements, specified by the Authority as a collective investment scheme by notice published in the *Gazette*,

but does not include –

(i) an arrangement operated by a person otherwise than by way of business;

(ii) an arrangement under which each of the participants carries on a business other than investment business and enters into the arrangements solely incidental to that other business;

(iii) an arrangement under which each of the participants is a related corporation of the person operating the arrangement;

(iv) an arrangement made by or on behalf of a corporation solely for the benefit of persons each of whom is either a bona fide director, former director, consultant, adviser, employee or former employee of that corporation or a related corporation of that corporation, or a spouse, widow, widower or a child, adopted child or step-child below the age of 18 of such director, former director, employee or former employee;³

(iva) an arrangement made by or on behalf of 2 or more corporations solely for the benefit of persons each of whom is either a bona fide director, former director, consultant, adviser, employee or former employee of any of those corporations or a related corporation of any of those corporations, or a spouse, widow, widower or a child, adopted child or step-child below the age of 18 of such director, former director, employee or former employee;⁴

(v) a franchise;

(vi) an arrangement under which money is taken by a solicitor from his customer, or as a stakeholder, acting in his professional capacity in the ordinary course of his practice;

(vii) an arrangement made by any co-operative society registered under the Co-operative Societies Act (Cap. 62) in accordance with the objects thereof for the benefit of its members;

(viii) an arrangement made for the purposes of any chit fund permitted to operate under the Chit Funds Act (Cap. 39);

³ Subparagraph (iv) was amended by the Securities and Futures (Amendment) Act 2003.

⁴ Subparagraph (iva) was inserted by the Securities and Futures (Amendment) Act 2003.

- (ix) an arrangement arising out of a policy of life insurance;
- (x) **a closed-end fund constituted either as an entity or trust;**
- (xi) an arrangement under which the whole amount of each participant's contribution is a deposit as defined in section 4B of the Banking Act (Cap. 19);
- (xia) an arrangements under which -
 - (A) the predominant purpose is to enable the participants to share in the use or enjoyment of property or to make its use or enjoyment available gratuitously to others; and
 - (B) the property does not consist of any of the following:
 - (BA) an currency of any country or territory,
 - (BB) an capital markets product;
 - (BC) policy as defined in the First Schedule to the Insurance Act (Cap. 142);
 - (BD) anydeposit as defined in section 4B of the Banking Act (Cap. 19);
 - (BE) any credit facilities as defined in section 2(1) of the Banking Act (Cap. 19);
- (xii) an arrangement which is an arrangement, or is of a class or description of arrangements, specified by the Authority as not constituting a collective investment scheme by notice published in the *Gazette*;

The definition that was first introduced in 2002 with the Securities and Futures Act is much tighter than the previous definition of 'interests' in the Companies Act, which used alternative criteria that involved more open-ended terms like 'common enterprise' and 'investment contract'. Although these terms were not fully tested in the local courts,⁵ the width of it can be seen in the US, where in the leading case of *SEC v Howey*,⁶ it was held that an arrangement created by a land sale contract, warranty deed and service contract for a citrus grove development with contracts for cultivation, marketing and remitting of net proceeds was considered a security.⁷ Registration of the offered securities was required and the offer was prohibited as there was no registration statement. It is the element of it being an investment contract whereby a person invests money in a common enterprise and expects to make a profit, predominantly

⁵ Cf *PP v 888.com (S) Pte Ltd* (PS 3383/99), where the District Court found that a franchise arrangement created an interest under the then Companies Act s 107. However, a specific exclusion for franchises was added to s 107 by the Companies (Amendment) Act 1998.

⁶ 328 US 293 (1946), referred to in *Australian Softwoods Forests Pty Ltd v A-G (NSW)* (1981) 148 CLR 121, cf *Australian Securities Commission v United Tree Farmers Pty Ltd* [1997] FCA 479 (Finn J).

⁷ See L Loss and J Seligman, *Fundamentals of Securities Regulations* (Aspen Publishers, 5thed, 2004) at 246 *et seq.*

through the efforts of a promoter or third party,⁸ which renders offers of such securities registrable, even if the underlying asset that is managed is not a security itself, and the units issued are non-redeemable.

By contrast, the definition of collective investment scheme, which is somewhat similar to the definition in Schedule 1 of Hong Kong's Securities and Futures Ordinance, as well as the meaning of 'collective investment schemes' under the UK's Financial Services and Markets Act 2000, has concurrent requirements that require delegation to a manager **or** pooling of monetary contributions and profits (thus effectively excluding timeshares and club memberships),⁹ and the sharing of what appears to be profits in *pecuniary* form ('the profits or income from which payments are to be made to them are pooled' and 'profits, income, or other payments or returns') rather than 'profits, rent or interest' as was the case in the definition of 'interests' under the now repealed section 107 of the Companies Act). The long list of exclusions also relate to schemes that generate such financial returns. But it does appear from the beginning that the authorities wanted to really only regulate unit trusts as CISs, which is why there was a problem when the first REITs actually desired classification as a CIS in 2001/2 (as opposed to being completely unregulated even when sold to retail investors) as these were in effect closed-end trusts and excluded by the part highlighted in the definition.

That regulatory mindset linking CIS to open-end unit trusts has created a great deal of difficulty but could, however, have been maintained in other ways. In the UK, the Financial Services and Markets Act 2000 essentially forbids the public offering of unit or trading trusts that are not open-ended in nature, and these can only be marketed privately and to sophisticated investors.¹⁰ Closed-end companies are treated as shares, and closed-end trusts cannot be authorised or offered to the public.¹¹ But redemption there was given a wider meaning – and it is stated under section 243(11) of the Financial Services and Markets Act 2000 in relation to the redemption formula in section 243(10):

But a scheme shall be treated as complying with subsection (10) if it requires the manager to ensure that a participant is able to sell his units on an investment exchange at a price not significantly different from that mentioned in that subsection.

The position in the UK, which the Securities and Futures Act collective investment scheme regime modelled itself on, was therefore both stricter and more flexible at the same time. A closed-end trust, though still considered a collective investment scheme as defined in the UK, would not be authorised as

⁸ The fact that the return of each investor depends on their own efforts does not undermine the existence of a common enterprise, particularly in the case of vertical or pyramid schemes. In such schemes, there may not be any pooling as it may involve only one promoter and one investor.

⁹ See MAS, FAQs on Offers of Shares, Debentures and CIS, 1 April 2014, on 'scope of collective investment schemes'.

¹⁰ The table of promotions which are permitted to be made were set out in the Financial Services (Promotion of Unregulated Schemes) Regulations 1991, now Part III of the FSMA (Promotions of Collective Investment Schemes) (Exemption) Regulations 2001.

¹¹ In the UK, investment trusts are really investment companies regulated in the same way we regulated such companies under the now deleted Companies Act (Cap 50) s 355. These are closed-end companies that are precluded from, for example, holding too much of their investments in any one company, and with more liberal distribution rules than applicable to industrial companies. In addition, the Listing Rules of the London Stock Exchange require certain additional disclosure by investment companies.

such, the consequence of which is that it cannot be offered to the public but only to a set of sophisticated investors. However, the meaning of redeemability is wider than is usually understood, and permits that requirement to be met by a listing on the exchange. This could then allow the UK Financial Conduct Authority to treat the trust or company as open-ended¹², which would then permit its authorisation and offer to the public.

In Singapore, however, closed-end trusts or companies were kept out of the definition of collective investment schemes altogether. While the latter is regulated when it offers shares to the public, the former was outside the regulatory reach of the Securities and Futures Act entirely, and could be offered to the public completely unregulated (and not to just accredited investors as in the UK). This created some difficulties, particularly with the introduction of REITs into the capital markets. In Singapore, these are structured as trusts, and due to the illiquid nature of the underlying assets, the units that are issued or sold to investors are in effect not redeemable (the trust deeds generally state that they cannot be redeemed while the REIT is listed on an exchange). Given the exclusion of closed-end funds from the definition of a collective investment scheme, they should have fallen outside the regulatory regime, and would not have required MAS's approval as a collective investment scheme before they could be sold to the public. However, most issuers of REITs, and the investment bankers associated with them, in fact wanted the regulatory safeguards as that increased investor confidence in the units being sold or marketed to the public.¹³

What then happened was that the definition of "closed-end fund", itself excepted from the CIS definition, was seen to exclude these REITs, and this has progressively been amended since the mid-2000s so that it now reads:

"closed-end fund" means an arrangement referred to in paragraph (a) or (b) of the definition of "collective investment scheme" under which units that are issued are exclusively or primarily non-redeemable at the election of the holders of units, but does not include —

- (a) an arrangement referred to in paragraph (a) of that definition —
 - (i) which is a trust;
 - (ii) which invests primarily in real estate and real estate-related assets specified by the Authority in the Code on Collective Investment Schemes; and
 - (iii) all or any units of which are listed for quotation on a securities exchange; or

But there is a new subsection (aa) with the SFAA 2017 that will effectively say that all funds operating for economic gain will not be seen to be closed-end and hence will be collective investment schemes which

¹² MAS and ACRA are closely studying the adoption of an open-ended investment company ('OEIC') regime as well as a Singapore Variable Capital Company ("SVCC") for investment funds.

¹³ This provides arguably an example of a bonding argument to enhance reputation.

was actually introduced in a 2013 amendment to the CIS definition by the Securities and Futures (Closed-End Fund) (Excluded Arrangements) Notification 2013. This means that the CIS exclusion for "closed-end fund" is itself subject to further exclusion if the fund is carrying on an active business (as opposed to holding investments passively). Specifically, MAS has now prescribed the following criteria to determine whether a closed-end fund is deemed to be a CIS (which operated prospectively from July 1 2013):

- all or most of the units issued under the arrangement cannot be redeemed at the election of the holders of the units;
- the entity operates in accordance with an investment policy under which investments are made for the purpose of giving participants in the arrangement the benefit of the results of the investments, and not for the purpose of operating a business; and
- the arrangement has certain prescribed characteristics.

What now seems to have happened is that the CIS exclusion for closed-end funds highlighted above does not really exist anymore except for some passive funds. This actually brings us to the position in HK where the SFC has made clear that it does not matter whether a CIS is open or closed-ended.¹⁴

Land Banking

However, land banking is still a problem as the earlier highlighted "or" has not replaced "and" and so pooling and external management are both required before something is a CIS. Again, if it is not a CIS, as land banking currently is not, it can be sold generally to retail investors. But would the recent change be enough to bring land banking schemes within the CIS fold given that in 2010 MAS thought that "(l)and-banking investments involve investors acquiring direct interests in real estate"? What is the position in the UK and HK?

In a recent decision in *Asset Land Investment Plc v FCA*¹⁵, the UK Supreme Court unanimously upheld the decisions of the courts below in finding an archetypal land banking scheme in the UK (where individual plots are sold to investors despite the land being restricted and on the understanding that a developer would be found to buy up the plots as a whole) as falling within the meaning of a collective investment scheme in section 235 of the Financial Services and Markets Act 2000. This meant that Asset Land was operating a regulated activity which required authorisation under section 19 of the same Act. Asset Land had represented that they would seek planning permission to rezone the land for residential use during the sales process. In subsequent written documentation, such as the contract of sale, however, there was a representations clause which attempted to wipe out any prior misrepresentations. A letter would also be sent prior to the payment of the initial deposit which stated that Asset Land was not responsible for pursuing re-zoning or planning permission (this also appeared as a disclaimer in the contract of sale). At first instance, Smith J held that the non-reliance clause only covered statements of fact and not of future intention. The Court of Appeal did not address this point but instead held that the definition of collective investment scheme ('CIS') captured 'arrangements' which did not have to be formal nor legally binding, and in particular that there was no need for a mutual understanding. Such an arrangement arose at the

¹⁴ HKSFC, Frequently Asked Questions, "What is a collective investment scheme".

¹⁵ [2016] UKSC 17.

point the oral representations were made, even if that arrangement ended or was varied by the subsequent documentation.

At its core, a CIS is a ‘collective investment where there is pooling of (a) contributions *and* income/profits and/or (b) collective management’.¹⁶ More specifically, section 235 states that participants in the scheme must not have day to day control over the management of the property, and that the property must be managed as a whole by or on behalf of the operator of the scheme. Although the definition was challenged with respect to its various constituent parts, the main argument raised by Asset Land in the Supreme Court was that the relevant property here was the individual plots of land, over which the investors had control, and not the sites as a whole. This was rejected by Lord Carnwath who held that an arrangement did not have to be viewed objectively just from the operator's viewpoint; that the relevant property for consideration was the entire site rather than each individual plot aggregated together as in the case of a block of flats; and that management concerned the operation of the scheme rather than looking after the individual plots as a managing agent would. Earlier in the judgment, he had approved of Smith J's approach¹⁷, that management activity was seen as context specific to the scheme – here it involved the promise to obtain planning permission, and then to find a developer for the entire site.

Lord Sumption preferred a narrower approach, even though he also agreed with Lord Carnwath (the other 3 judges agreed with both). He goes through the history of collective investment scheme regulation and draws the distinction between unregulated activity involving sales of physical property like land, and regulated schemes involving not just land sales themselves (even with subsequent professional services provided to rezone the land, which would not be a Financial Services and Markets Act 2000 regulated activity) but arrangements which fall within the definition of a collective investment scheme. He found this present in Asset Land but only on the basis that the scheme was a collective investment scheme at the point it was constituted (and not just later on because of the parties' actions) because although the investors legally owned their own plots, the judge below had found that their dominion was illusory as they could not sell their plots individually as this would have defeated the purpose of the scheme even as planned (value would be lost throughout by all the parties).

As we have seen, Singapore will amend its definition of collective investment scheme to look more like section 235 of the Financial Services and Markets Act 2000 in that pooling and collective management have become alternative requirements as in the UK (as opposed to the previous situation where both are required, which was the reason MAS provided for not being able to regulate land banking previously as funds might not be pooled as such even if the scheme was wholly managed by the scheme manager). This would be consistent with Lord Sumption's analysis of the collective investment scheme regime in the UK, where he thought that pooling and having someone else manage the property covered the same mischief where an operator manages other people's money – they were ‘functionally equivalent’.¹⁸

¹⁶ *Financial Conduct Authority v Capital Alternatives Ltd* [2015] EWCA Civ 284 (appeal to the SC denied). See further H Tjio, ‘The Not So Collective Investment Scheme’ [2015] LMCLQ 451.

¹⁷ Smith J in *Asset Land* [2013] EWHC 178, following David Richards J in *In re Sky Land Consultants plc* [2010] EWHC 399.

¹⁸ *Supra* fn 15 at [98].

MAS has also said that collective investment schemes that require authorisation will be restricted to investments in securities or other assets that are liquid, such as precious metals, or which have stable income, such as completed real estate.¹⁹ That will continue to distinguish regulated CISs from unregulated schemes involving timeshares and club memberships which are only subject to consumer protection rules. But given the slightly more liberal philosophical bent with regulators in Singapore, it may be that the position in HK is still stricter even with a similar CIS wording. The SFC has said that all property funds are largely included and it is really only the sale of individual units without more that is outside the CIS definition. In 2013, the attempted Apex Horizon hotel room sale by Cheung Kong (Holdings) had to be withdrawn (with 360 buyers refunded their deposits) as the SFC saw that as an unauthorised CIS given that the operator continued to allocate guests to the rooms.²⁰ Day to day management was still in the operator's hands, and not the individual buyers. It may, however, be that the views of specific regulators should generally prevail regardless of how similar the definitions are.

Statutory interpretation

The more modern approach to contractual interpretation is highly purposive or contextual, and intended to accord with "business common sense".²¹ It may be that we have to go one full circle for statutory interpretation where regulators have tried to give certainty by providing greater guidance through more precise drafting but now find that every phrase is the subject of close scrutiny by persons trying to avoid regulation. A few things in the recent cases suggest that the courts have reacted to this.

The first time the English Court of Appeal considered the CIS definition was in *Financial Services Authority v Fradley*²² where in setting aside a summary judgment holding that a horse-betting scheme was a CIS, Arden LJ warned that although the definition was "open-textured" and having a "wide meaning", "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."²³

Although the Supreme Court in *Asset Land* at [6] referred to Arden LJ's statement, it did not address it. However, the Court of Appeal in *Capital Alternatives*²⁴ did not think their approach in any way detracted from the warnings proffered by Arden LJ. At first instance in *Capital Alternatives*, Strauss QC had presaged the issue by asking "should section 235 be construed strictly, in the event of ambiguity, in favour of the person who might be subject to a criminal sanction?"²⁵ He then referred to the decision of Warren J in *re*

¹⁹ See MAS Consultation Paper, P012-2014, Proposals to Enhance Regulatory Safeguards for Investors in the Capital Markets, July 2014, to address, amongst other things land banking.

²⁰ E Yiu, P Sito and J Ng, "Cheung Kong's sales of Apex Horizon hotel suites cancelled over investment breach" South China Morning Post, 13 May 2013.

²¹ *Fons Hf v Corporal Ltd* [2014] EWCA Civ 304 at [16], noted H Tjio (2014) 73 CLJ 303.

²² *Financial Services Authority v Fradley* [2005] EWCA Civ 1183; [2006] 2 BCLC 616 at [33].

²³ *Ibid* at [32], where Arden LJ also highlighted the fact that Fradley had no legally qualified representative.

²⁴ See *supra* fn.16, [78].

²⁵ *Financial Conduct Authority v Capital Alternatives Ltd* [2014] EWHC 144 (Ch) at [46].

*Digital Satellite Warranty Cover Limited*²⁶ which in turn relied on the judgement of Sir Brown-Wilkinson V-C in *in re Lo-Line Electric Motors Ltd*,²⁷ where it was held that the main purpose for the Company Directors Disqualification Act 1986 was the protection of the public, and this was an “interpretative factor” that weighed against the “principle against doubtful penalisation”.²⁸ Clarke LJ fully endorsed this on appeal in *Capital Alternatives* where he thought that “it was not necessary to adopt a restrictive construction because FMSA contains penal sanctions.”²⁹

Given that there are also civil consequences in finding that an arrangement is a collective investment scheme, as in *Asset Land* where interim payments were ordered to compensate investors for their loss under section 382 of the Financial Services and Markets Act 2000³⁰, this could be seen as a similar protected interest that balances out Arden LJ’s concerns. Indeed, Gloster LJ in *Asset Land* had acknowledged the *Digital Satellite* decision, and that a “competing public interest (such as consumer protection under FSMA) was in play”³¹, but thought that the Court of Appeal did not have to address the issue in that case. Nevertheless, Clarke LJ’s determination not to be swayed by arguments as to the penal nature of the provisions in *Capital Alternatives* shows that the court was determined to adopt a neutral approach to interpretation even where there are criminal consequences lurking in the background.

There is no need to be apologetic about this as modern statutes, unlike some broadly drafted legislation in the past, appear more didactic and, being the product of consultation, take into account stakeholder interests. A narrow construction is not necessary with “detailed statutory codes”³² or where the affected person is “chancing one’s arm”³³. However, adopting a seemingly neutral approach in light of possible penal sanctions means that the courts may have drawn a line in the sand. That slight change in judicial thinking may be significant, for although Arden LJ in *Fradley*³⁴ found that the participants did not have day to day control in the horse betting scheme, she refused to uphold summary judgment on grounds that the parties may not have been jointly operating the scheme and that issue had to go to trial as to whether it was a single “arrangement” as such. But it is not clear if the shift in court thinking towards seeing land banking as CISs is simply a matter of evolving statutory interpretation or goes further into the realms of deference to administrative agencies.

²⁶ [2011] EWHC 122; [2011] Bus LR 981 (Ch) (Warren J), upheld by the Court of Appeal [2011] EWCA 1413; [2012] Bus LR 990.

²⁷ [1988] Ch 477.

²⁸ F Bennion, *Bennion on Statutory Interpretation: A Code*, 5th edn (London: LexisNexis, 2008), Part XVII, 828.

²⁹ See *supra* fn. 16, [79].

³⁰ Pursuant to the Senior Courts Act 1981, s. 32 and Civil Procedure Rules, r. 25.7. The procedural challenges to the interim payment order were dismissed by Clarke LJ in *Capital Alternatives*, *supra* fn. 16, [105]-[107].

³¹ *Asset Land* [2014] EWCA Civ 435, Note 1.

³² *Bennion*, *supra* fn.28, 829.

³³ *Bennion*, *supra* fn.28, 830.

³⁴ See *supra* fn.22, [32]-[33].

Administrative deference

The FCA, and its predecessor the Financial Services Authority, has by all accounts been very interventionist since the Global Financial Crisis,³⁵ and “its bona fides cannot be questioned”.³⁶ However, for this to work, courts may have to give regulators (at least the more qualified ones) some leeway, and there are growing signs of this. In *Capital Alternatives*, Clarke LJ thought that “Courts are reluctant to disturb a settled interpretation and the practice based on it, and there was a powerful presumption that the meaning that had been given to a phrase in issue by a regulatory body was the correct one”.³⁷ This added a further gloss to the speech of Lord Phillips in *Bloomsbury International Ltd v Sea Fish Authority*³⁸ that Clarke LJ relied on where his Lordship only stated that there is “a powerful presumption that the meaning that has customarily been given to the phrase in issue is the correct one”.³⁹ After a detailed examination of various guidance letters of the FCA that were referred to by defence counsel, however, Clarke LJ thought that they concerned different structures from the one under consideration there.⁴⁰ In *Asset Land*,⁴¹ Gloster LJ may have gone even further in finding helpful a paper published by the Financial Markets Law Committee dated July 2008, “Issue 86 – Operating a Collective Investment Scheme”, which had said that the definition of “arrangements” is very wide and intended to be so, and which in that case guided her in finding such an arrangement that resulted in the establishment of a collective investment scheme. The Supreme Court while referring to this paper did not comment on it and it may be that the approach in the UK is still more conservative as opposed to other developed legal jurisdictions. This is also likely to be the case in Singapore and HK. In the case of the latter, it was said in a securities licensing appeal from the Securities and Futures Appeals Tribunal in *Ng Chiu Mui v Securities and Futures Commission*⁴² that:

³⁵ In *Asset Land*, *supra* fn.31, [38]-[39], Gloster LJ noted that the FSA was actually aware in early 2007 of the operator selling land to UK investors. After representations from its City solicitor, the FSA terminated investigations in November 2008 with a “no-action letter”, but later appointed investigators under the Financial Services and Markets Act 2000, s. 168(3) when complaints against the operator continued to file in.

³⁶ Smith J in *Asset Land*, *supra* fn.17, [51], when rejecting the argument to set aside the claims on the basis that the FSA was in abuse of process in going back on its subsequent letter of 19 September 2012 stating that they would not take the pre-November 2008 sales into consideration, *ibid*.

³⁷ See *supra* fn.16, [68].

³⁸ *Bloomsbury International Ltd v Sea Fish Authority* [2011] UKSC 25; [2011] 1 WLR 1546 at [55] – [59].

³⁹ *Ibid*, [58].

⁴⁰ See *supra* fn.16, [33]-[68]. Clarke LJ thought that the guidance was “rather guarded” (at [66]) and “vague on important matters” (at [67]). The Financial Services and Markets Act 2000, s. 157 provides that the FCA may give guidance consisting of such information and advice as it considers appropriate with respect to, amongst other things, the operation of the Act and any rules promulgated under it.

⁴¹ See *supra* fn.31, [51]. But see M Bundle, J Perkins and N Minervini, “Collective investment schemes: a missed opportunity” (2012) JIBFL 219, 222, suggesting that the paper actually “highlighted many of the uncertainties discussed” in that article.

⁴² [2010] HKCA 150 at [26]-[27].

It was submitted that the SFC's interpretation was the correct one and the Tribunal was wrong to have dismissed that interpretation as well as the footnoted commentary in the consultation paper presented to the Bills Committee as "straws in the interpretative wind".

But the SFC's view can be of no relevance as a matter of law unless it is a tool of statutory interpretation. Since Mr Grossman accepts that it is not such a tool, the Tribunal's approach plainly was correct.

By contrast, in the context of judicial review, courts in the US,⁴³ Canada⁴⁴ and to a lesser extent in Australia,⁴⁵ accord regulators a zone of discretion in the exercise of their administrative powers. The role of the court is to ensure that they stay within that zone, but not to attempt to second-guess their intentions.⁴⁶ It may be that this is the only way that financial markets can properly be regulated given the pace at which things change and the fact that the various participants in the market are actively trying to avoid regulation. While the tide may have turned when it comes to seeing whether an investment arrangement involving underlying land or real property is a collective investment scheme, this may not be because courts are prepared to defer to the regulatory expertise of the FCA/SFC/MAS. Rather, there has now evolved enough formal material to aid the courts in statutory interpretation when a land banking matter comes up against highly technical objections raised by those with less of a stake in its proper regulation. It is not clear if that is the case with cryptocurrency and initial coin offerings due to their more nascent nature. Further, regulators themselves are ambivalent about how and how far to regulate what are in effect virtual property schemes given their possibly greater contribution to the economy.

Cryptocurrency and ICOs

In 2017, the Singapore International Commercial Court⁴⁷ heard the first cryptocurrency case to come to the courts in Singapore involving its most widely known, "Bitcoin". Bitcoin first started out as an alternative to fiat currency in 2008 as a means of exchange but appears to be traded as a commodity or store of value today with a great deal of speculation in what appears to be of little intrinsic value, which may explain its volatility. Regulations concerning cryptocurrency appear to be moving along the same lines, *ie* from it being a form of currency to a kind of security. In *B2C2 Ltd v Quoine Pte Ltd*⁴⁸ (*B2C2*),

⁴³ *Chevron USA Inc v National Resources Defence Council, Inc* 467 US 837 (1984). Intervention by the courts is also constrained by the lack of capacity: see eg, *Gustafson v Alloyd Co, Inc* 513 US 561 (1995). There is, however, a difference between regulatory guidance carrying a greater force of law and those that are less formal: *Christensen v Harris County* 529 US 576 (2000).

⁴⁴ *United Brotherhood of Carpenters and Joiners of America, Local 579 v Bradco Construction Ltd* [1993] 2 SCR 316, 335; *Pezim v British Columbia (Superintendent of Brokers)* [1994] 2 SCR 557, 591-592. The amount of deference may depend on the standing of the regulator in question.

⁴⁵ See eg, *Corporation of the City of Enfield v Development Assessment Commission* (2000) 169 ALR 400 and now *Minister for Immigration and Citizenship v SZMDS* [2010] HCA 16.

⁴⁶ HP Monaghan, "Marbury and the Administrative State" (1983) 83 *Columbia LR* 1, 32-33.

⁴⁷ Andrew Godwin, Ian Ramsay and Miranda Webster, "International Commercial Courts: The Singapore Experience" (December 31, 2017) forthcoming in (2017) 18 *Melbourne Journal of International Law*. Available at SSRN: <https://ssrn.com/abstract=3095059>

⁴⁸ [2017] SGHC(I) 11.

Thorley IJ dismissed an application for summary judgment pursuant to O 14 of the Rules of Court⁴⁹ for breach of contract and breach of trust against a Singapore incorporated company operating a currency exchange platform which enabled third parties to trade Bitcoin and Ethereum for other virtual currencies or for fiat currencies such as the Singapore or US dollars.

The plaintiff was an electronic market maker incorporated in England providing liquidity on the exchange platform by buying and selling virtual currencies at the prices it quoted for virtual currency pairs. It agreed to a set of terms and conditions available on the defendant exchange platform's website. On 19 April 2017, the plaintiff placed 12,617 Bitcoin and Ethereum orders of which only 15 were filled. Eight of the orders were buy or sell orders transacted at a price of around 0.04 Bitcoin for one Ethereum. Seven others were sell orders that were effected at an exchange rate of around ten Bitcoin for one Ethereum. These were filled after a technical glitch had hit the defendant exchange and it was unable to perform its market price updates. All the orders on the relevant order book were not available so that no true market price could be set. However, because of the glitch, the plaintiff's price was the only one available on the defendant's platform and this was matched by the computer system with Bitcoin held by forced sale customers. This meant that the plaintiff was credited with a large number of Bitcoin with the exchanged amount of Ethereum debited. The forced sold customers had their accounts correspondingly debited and credited. The plaintiff stood to gain almost 250 times the amount of Bitcoin that the pre-glitch exchange rate of Bitcoin for Ethereum would have given them. The defendant exchange platform tried to unilaterally reverse the transaction on the following day. They contended that the risk disclosure document contained a term that allowed them to do that which Thorley IJ thought raised an arguable defence. He thus refused to grant summary judgment. Another reason for this was founded on the doctrine of unilateral mistake which the judge acknowledged was less developed where computers were concerned. In *Chwee Kin Keong v Digilandmall.com Pte Ltd*⁵⁰ ("*Digilandmall*"), it was held that there needed to be a sufficiently important or fundamental mistake as to a term of the contract and that the party seeking to enforce the contract must have had actual knowledge of the mistake. Here, Thorley IJ thought that a more thorough investigation of the facts behind the setting of the high offer price was needed in order to assess the state of the plaintiff's knowledge and so summary judgment was not apposite. He also thought that the law of unilateral mistake could properly be revisited at trial when all the facts had been fully established.

What this case shows is that the lack of regulation can lead to overreaching behavior that courts will find very difficult to deal with utilizing common law techniques. The trade-off is acceptable so long as there are real benefits to the economy.

MAS statement on tokens

While the financial products that were exchanged in *B2C2* involved cryptocurrency rather than capital markets products, many in fact overlap, particularly later incarnations of these financial instruments. Indeed many initial coin offerings (ICOs) are today offered in exchange for cryptocurrency, so it is the virtual being built on the virtual. ICO issuers usually are or concern putative technology companies with no immediate working product. They are in this sense very much like a fund that says that it has not

⁴⁹ Cap 322, R 5, 2014 Rev Ed.

⁵⁰ [2005] 1 SLR(R) 502.

identified what companies to invest in which in *Exeter Group Limited v ASC*⁵¹ was found to be insufficient disclosure for there to be a public offering in Australia. Consequently, most ICOs avoid prospectus disclosure. The basis for this was a statement made by the MAS about two years ago and Singapore has since become the second or third largest ICO jurisdiction. Out of the worldwide 211 ICOs in 2017, 20% of that was in Singapore raising about US\$790 million according to the Association of Cryptocurrency Enterprises and Startups, Singapore.

In November 2017, however, MAS issued a Guide to Digital Token Offerings. This stated that “digital tokens that constitute capital markets products” will have to comply with the offering requirements of the Securities and Futures Act,⁵² including the need to prepare a prospectus, although the offerors can avail themselves of the exclusions and exemptions there. This statement concerned offers of digital tokens in the primary market that represent underlying securities or derivatives contracts, for which a great deal of concern has been voiced recently in terms of their financial risks,⁵³ as well as link to illegal activity.⁵⁴

The Swiss Financial Market Supervisory Authority (FINMA) suggests that there are essentially three types of such tokens, payment tokens, utility tokens and asset tokens⁵⁵. However, it also suggested that these categories are not mutually exclusive and can be in the form of a hybrid. If it has some characteristics of a capital markets product, that should be enough to require its regulation. Even utility tokens should be caught by CIS definition where the purpose of the scheme is to obtain economic benefits. But there has been no sign of that thus far in Singapore, perhaps because the CIS definition has not been changed. In contrast, although the more recent MAS statement sounds similar to what the SEC has been saying, the latter has in fact been enforcing extant securities laws in that regard. The *SEC v Howey* case discussed at the start of this paper was used by the SEC in Munchee’s restaurant review application MUN token to argue that it was a security due to the expectations of return even though it was argued that it was a utility token to be used within Munchee’s system and not to fund it. Perhaps this was because “investment contract” can be interpreted more widely than a CIS. We have, however, seen that the use of the phrase “arrangement” in the CIS definition can be equally wide. In HK, the SFC has used the CIS regime to stop

⁵¹ [1998] 16 ACLC 1,382. It is unlikely that the common law imposed a duty to disclose; although some cases supported the position that if anything is said it cannot be misleading: *New Brunswick and Canada Railway and Land Co v Muggerridge* (1860) 1 DR & SM 363. There were also judicial statements that refer to the duty of ‘utmost candour and honesty’ on the part of promoters who invite members of the public to invest in a company: *Central Railway of Venezuela v Kisch* (1867) LR 2 HL 99 at 113 *per* Lord Chelmsford. This could be seen as the “Golden Rule” that did not create a firm foothold: editorial note on “R v Kysant: A New Golden Rule for Prospectuses” (1932) 45 *Harv LR* 1078. The old Companies Act s 4(3) stated that “a statement included in a prospectus or statement in lieu of prospectus shall be deemed to be untrue if it is misleading in the form and context in which it is included.”

⁵² Cap 289.

⁵³ See, eg, Dirk A Zetsche, Ross P Buckley, Douglas W Arner and Linus Föhr, “The ICO Gold Rush: It’s a Scam, It’s a Bubble, It’s a Super Challenge for Regulators” (January 9, 2018). University of Luxembourg Law Working Paper No. 11/2017. Available at SSRN: <https://ssrn.com/abstract=3072298>.

⁵⁴ Sean Foley, Jonathan R Karlsen and Tālis J Putniņš, “Sex, Drugs, and Bitcoin: How Much Illegal Activity Is Financed Through Cryptocurrencies?” (January 15, 2018). Available at SSRN: <https://ssrn.com/abstract=3102645>.

⁵⁵ Guidelines for enquiries regarding the regulatory framework for initial coin offerings (ICOs), Swiss Financial Market Supervisory Authority FINMA, 16 February 2018

the token offering of Black Cell Technology Limited, although it appears that not only was the ICO proceeds to be used to fund development of a mobile application, but the token itself could be redeemed for equity in Black Cell subsequently.⁵⁶ That later characteristic made the securities link unavoidable in this primary offering.

If the secondary market rules had applied to the defendant exchange in *B2C2*, however, it would have been seen as a person providing a platform on which digital tokens are traded and may have been seen as operating an organised market. A person who establishes or operates an organised market, or holds himself out as operating an organised market, must be approved by the MAS as an approved exchange or recognised by the MAS as a recognised market operator, unless otherwise exempted. The plaintiff, being a market maker, may then have required a capital markets services licence to deal in securities or capital markets product, which is a regulated activity under the Securities and Futures Act. Again, however, it is unlikely that Bitcoin and Ethereum, unlike more recent generations of cryptocurrency, would have been seen as a capital markets product as opposed to a currency or payment system. It would be quite different with the Bitcoin futures contract now traded on the Chicago Board Options Exchange which if it had a presence in Singapore would currently be seen as a “futures contract” under the Securities and Futures Act and with the coming into effect of the Securities and Futures (Amendment) Act 2017, a “derivatives contract”.

MAS is currently conducting public consultation on a proposed Payment Services Bill that will empower it to impose anti-moneylaundering or combating the financing of terrorism requirements on such intermediaries.⁵⁷ This will be based on the idea that at some stage, fiat currency will have to be exchanged for virtual currency, or *vice versa*, at intermediaries that buy, sell or exchange virtual currency. More recently MAS confirmed that “(t)he key risks MAS is monitoring in the crypto world are in the areas of financial stability, money laundering, investor protection and market functioning”.⁵⁸

Conclusion

While it may appear that MAS seemingly only reacts to overreaching behaviour in the financial markets after they occur, this may in fact be the correct way for regulators to act. The market should be allowed to function as much as possible, and only where it has failed, and subsequently failed to adjust to find its own solutions and remedies, should regulators then step in to correct the problem. This is not an excuse for the libertarian refrain that ‘this time is different’;⁵⁹ far from it. Regulators have to act in a temperate way, always looking closely at empirical evidence, and challenging their own views. Although said in an infinitely different context, they may well have to constantly remind themselves of ‘the spirit which is not

⁵⁶ HKSFC, “SFC’s regulatory action halts ICO to Hong Kong public” 19 March 2018.

⁵⁷ See MAS Consultation Paper P021-2017 on Proposed Payment Systems Bill (November 2017).

⁵⁸ Ravi Menon, MD of MAS, “Crypto Tokens: The Good, The Bad, and The Ugly” Money20/20, 15 March 2018.

⁵⁹ C Reinhart and K Rogoff, *This Time Is Different: Eight Centuries of Financial Folly* (Princeton University Press, 2009). Mark Carney, Governor of the Bank of England called this phrase ‘the four most expensive words in the English language’: remarks at The Harvard Club UK Southwark Cathedral dinner, 21 September 2015.

too sure that it is right'.⁶⁰ The statement by Ravi Menon, MD of MAS on 15 March 2018 is in this vein.⁶¹ There he said that, "MAS assesses that the nature and scale of crypto token activities in Singapore do not currently pose a significant risk to financial stability. But this situation could change, and so we are closely watching this space".

From an academic perspective, it appears that regulators are concerned but "politicians like looser regulation".⁶² One reason for this may be that they fear missing out on the next big growth story, particularly given the slowdown in economic growth alongside recovery in bank bonuses since the Global Financial Crisis. The young are struggling for jobs all over the world as retirement ages have been pushed back. Another explanation is that there has been a fundamental shift in long-term business cycles so that the world's economy has been unable to start afresh partly due to the failure of states to address the over-financialisation of their economies. The problem is that these investments in technology, or more accurately in the hope that technology will lead to tangible growth, may not work.⁶³ Even if they do not pose financial stability risks, the investors, many who may well be from that younger generation, should see that the world does not need more than 1500 cryptocurrencies when there are fewer than 200 real currencies. Still, the jury is out on whether they should be regulated as securities, which is unlike the case with land banking, where there is almost universal recognition now that the starting point is that they are collective investment schemes.

⁶⁰ Learned Hand, 'I am an American Day' (Central Park, New York City, 21 May 1944).

⁶¹ *Supra* fn. 58.

⁶² Peter Boone and Simon Johnson, *The Future of Finance* (LSE, 2010) at 246.

⁶³ P Mason, *Postcapitalism, A Guide to Our Future* (Farrar, Straus and Giroux, 2015) referring to 50-60 year Kondratieff cycles, and the contradictions within present technological innovation which prevents it from starting the 5th long wave when growth in the previous waves was precipitated by technological change.