Neutral Citation Number: [2024] EWCA Civ 765

Case No: CA-2023-001864

**IN THE COURT OF APPEAL (CIVIL DIVISION)**
**ON APPEAL FROM THE HIGH COURT OF JUSTICE**
**BUSINESS AND PROPERTY COURTS OF ENGLAND AND WALES**
**KING'S BENCH DIVISION**
**LONDON CIRCUIT COMMERCIAL COURT**
**Paul Stanley KC (sitting as a Deputy High Court Judge)**
**[2023] EWHC 1686 (Comm)**

Royal Courts of Justice
Strand, London, WC2A 2LL

Date: 09/07/2024

**Before:**

**SIR GEOFFREY VOS, MASTER OF THE ROLLS**
**LORD JUSTICE LEWISON**
and
**LORD JUSTICE MALES**

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**Between:**

**1) KVB CONSULTANTS LIMITED** — **Respondents /Claimants**
**2) PAMELA CIZEK**
**3) BARRY COLEMAN**
**4) NIGEL DENNING**
**5) RICHARD DENNING**
**6) DRIVELAND ESTATES LIMITED**
**7) ARJUN KAINTH**
**8) KULDIP KAINTH**
**9) DAPHNE MORGAN**
**10) AQUARIUS LIVING LIMITED**
**11) MIRAJ PATEL**
**12) MELANIE RAYNER**
**13) DILIP SHAH**
**14) NALINA SHAH**
**15) HETUL SHAH**
**16) DR HETUL SHAH LIMITED**
**17) NEHA SHAH**
**18) DIPAK SHAH**
**19) MEERA SHAH**
**20) MAHESH SHAH**
**21) MADULABEN SHAH**
**22) SHEENA SHAH**

**23) VASANTI SHAH**
**24) BIPIN SHAH**
**25) BO SUN**
**26) SRIDHAR VENKITESWARAN**

**- and -**

**1) JACOB HOPKINS MCKENZIE LIMITED** **Defendants**
**2) HOW REFRESHING (PROPERTY MANAGEMENT) WINCHFAWR LIMITED**
**3) HOW REFRESHING (PROPERTY MANAGEMENT) HIRWAUN LIMITED**
**4) HOW REFRESHING (PROPERTY MANAGEMENT) BRYNITHEL ABERTILLERY LIMITED**
**5) HOW REFRESHING (THE BRYN) LIMITED**
**6) HOW REFRESHING (NEW TREDEGAR) LIMITED**
**7) HOW REFRESHING (SALISBURY ROAD) LIMITED**
**8) HOW REFRESHING (PORTH) LIMITED**
**9) HOW REFRESHING (KINGSLEY TERRACE) LIMITED**
**10) ANDREW HOWELL CALLEN**
**11) ALISON EVANS T/A ALISONS LEGAL PRACTICE**
**12) KESSION CAPITAL LIMITED** **Appellant/ 12th Defendant**

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**Simon Howarth KC and Lucile Taylor (**instructed by **DWF Law LLP**) for the **Appellant (the Twelfth Defendant)**

**Hugh Sims KC and Jay Jagasia (**instructed by **Acuity Law Ltd)** for the **Respondents**

Hearing date: 12 June 2024

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# Approved Judgment

This judgment was handed down remotely at 10.30am on Tuesday 9 July 2024 by circulation to the parties or their representatives by e-mail and by release to the National Archives.

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## LORD JUSTICE MALES:

1. The appellant, Kession Capital Ltd ('KCL'), the 12th defendant in this action, is a person authorised under the Financial Services and Markets Act 2000 ('FSMA') to carry on designated investment business. Pursuant to section 39 of FSMA, it entered into a contract with the 1st defendant, Jacob Hopkins McKenzie Ltd ('JHM'), appointing JHM as its appointed representative to conduct what was defined as 'Relevant Business'. I shall refer to the contract, which was described as an 'Appointed Representative Agreement', as the 'ARA'.

2. JHM then promoted and operated a series of property investment schemes in which the respondent claimants invested a combined total of about £1.7 million. When those schemes failed, the claimants lost their money, which they now seek to recover from KCL, the only active defendant in this action.

3. The issue on this appeal is whether, by appointing JHM as its appointed representative, KCL accepted responsibility for the actions of JHM in promoting and operating the investment schemes. On the claimants' application for summary judgment the judge, Paul Stanley KC sitting as a Deputy High Court Judge in the London Circuit Commercial Court, held that KCL had accepted responsibility for activities relating to their promotion and gave judgment accordingly.

4. KCL says that it did not accept such responsibility and is not liable. Although it accepted responsibility for the conduct of JHM in carrying out the business which it was permitted to carry out under the ARA, that permission did not extend to promoting or operating collective investment schemes or to advising on or arranging deals for retail clients. Accordingly, because it is now common ground that the investment schemes in question were collective investment schemes, and because all but one of the claimants were (and should have been classified as) retail clients, the actions of JHM in promoting and operating these schemes were outside the scope of the permission granted by the ARA and the responsibility which KCL accepted.

5. The appeal raises issues as to the interpretation of the ARA and the application of section 39 of FSMA, in particular as to the meaning of the terms 'business of a prescribed description' and 'part of that business' used in the section. It requires also consideration of the distinction 'between what activity may be carried on and how a permitted activity is carried on' discussed in *Anderson v Sense Networks Ltd* [2019] EWCA Civ 1395, [2019] Bus LR 1 ('*Anderson*').

## Background

6. The investment schemes in question were devised, promoted and managed by Mr Andrew Callen, acting through JHM which traded under the name 'How Refreshing'. Mr Callen was a solicitor who developed a business which initially involved attracting investment for small refurbishment property schemes. At that stage he operated through a limited partnership, Jacob Hopkins & McKenzie LLP, although by the time the ARA was concluded, he was operating through a limited company, JHM.

7. In or about 2015 Mr Callen devised a more ambitious plan for property development, which involved buying property for residential development, which would then be sold at a profit following the carrying out of development work. It appears that the

initial plan (at least in relation to the earlier refurbishment schemes) was for each property to be purchased by a special purpose vehicle ('SPV') in which the investors would own shares proportionate to the value of their investment. It is common ground that if this structure had been implemented, the schemes in question would not have been collective investment schemes. However, this structure was not implemented. Instead, the shares in the SPVs which purchased the properties were held by Mr Callen and each SPV made a declaration of bare trust, whereby the property which it had purchased would be held on trust for the investors in the scheme. The judge found, and it appears to be common ground, that this change in the proposed structure was understood by KCL by the time the ARA was concluded.

8. I will consider the legislation more fully later in this judgment. In summary, however, because the proposed investment schemes constituted regulated activity, promoting and operating them could only be carried on lawfully by a person who was either an authorised person under FSMA or an exempt person. JHM was not an authorised person and therefore needed to become exempt by becoming an appointed representative of an authorised person such as KCL. For this purpose Mr Callen approached KCL in October 2014. He had no previous knowledge of or relationship with KCL, but discovered its identity by means of a Google search. This initial approach led to the appointment of the LLP as an appointed representative of KCL, although the terms of that agreement were not in evidence. It was in any event superseded by the ARA concluded between JHM and KCL dated 30th June 2015.

9. Following the conclusion of the ARA (the terms of which I consider below), seven schemes were launched, adopting the 'bare trust' structure, in which the claimants invested:

(1) Scheme HR61 (Winchfawr) received its first investment on 3rd October 2015 and its last on 8th September 2015.

(2) Scheme HR65 (Hirwaun) received its first investment in October 2015, and its last investment in January 2018.

(3) Scheme HR66 (Brynithel) received its first investment in December 2015 and its last investment in April 2016.

(4) Scheme HR75 (Tredegar) received all its investments in September 2016.

(5) Scheme HR71 (The Bryn/Rhigos) received its first investment in August 2016 and its second and last investment in June 2017.

(6) Scheme HR79 (Salisbury Road) received its first investment in December 2017, and its last investment in March 2019.

(7) Scheme HR81 (Porth) received all its investments between March and June 2017.

10. The schemes were promoted by JHM, who provided at least some of its promotional material to KCL for review, and KCL provided some comments on that material. Not surprisingly on an application for summary judgment where these facts were in dispute, the judge made no findings as to the detail of what material KCL saw or the

extent to which this corresponded with material seen by particular investors. His conclusion on the evidence was as follows:

> '24. The upshot is this. There is little clarity about precisely which of the financial promotions KCL approved (for any purpose), though it approved at least some. There is documentary evidence, though only from a relatively late stage, of some sort of formal approval process. But there is no direct evidence that in general, much less as a whole, KCL approved every promotion on which the claimants rely, or even that it approved all the key ones. Nor, in relation to any of the claimants, is there direct or clear evidence as to precisely which promotional statements each claimant relied on in making any particular investment.'

11. He accepted, however, that the promotion and operation of the JHM schemes was 'the *raison d'être*' of the ARA: these were the very schemes which the parties contemplated would be undertaken pursuant to the ARA.

12. With one exception (an investor who appears not to have been classified), JHM classified the investors as 'elected/elective professional investor', 'high net worth investor', 'professional client' or 'sophisticated investor'. However, many of the claimants contend that they were wrongly so classified, while KCL now asserts positively that (with one exception) they ought to have been classified as 'retail clients'.

13. In April 2016 the Supreme Court gave judgment in *Financial Conduct Authority v Asset LI Inc* [2016] UKSC 17, [2016] Bus LR 524, deciding that a property investment scheme with some similarities to the schemes promoted by JHM was a collective investment scheme within the meaning of section 235 of FSMA. This appears to have prompted some consideration whether the JHM schemes were also collective investment schemes. Although Mr Callen had said that all marketing activity for these schemes was put on hold by June 2016, the judge regarded this as unlikely as investments continued to be accepted in considerable quantity thereafter.

14. Be that as it may, a different structure was adopted for an eighth scheme ('Kingsley Terrace'), launched in 2017. We are not concerned with this scheme on this appeal. The judge declined to give summary judgment in respect of the Kingsley Terrace scheme and there is no appeal from that decision. If the claim in respect of that scheme is pursued, it will have to go to trial.

15. In the event the properties purchased were not developed. Some of the properties have been repossessed by secured lenders. Mr Callen has been made bankrupt and JHM is insolvent. The claimants have lost the money which they invested and although default judgments have been entered against other defendants, it appears that their only prospect of recovery is to sue KCL.

## The legislation

16. FSMA together with its associated subordinate legislation and the Conduct of Business Rules ('the COBS Rules') contained in the FCA Handbook represent

something of a labyrinth, at least to the general reader. In order for the issues in this appeal to be understood, it is necessary to set out some of the relevant provisions.

*The general prohibition*

17. Section 19 of FSMA contains what is known as 'the general prohibition' and introduces the concept of 'an authorised person':

> '19 **The 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.'

18. Section 23 provides that contravention of the general prohibition is a criminal offence.

19. Section 20(1) provides that an authorised person may only carry on a regulated activity in accordance with permission given by the FCA (or in some cases the PRA) or resulting from any other provision of the Act.

20. Section 21 restricts the promotion of investment activity to promotions made or approved by authorised persons:

> '21 **Restrictions on financial promotion**
>
> (1) A person ("A") must not, in the course of business, communicate an invitation or inducement to engage in investment activity.
>
> (2) But subsection (1) does not apply if–
>
> (a) A is an authorised person; or
>
> (b) the content of the communication is approved for the purposes of this section by an authorised person.'

21. Subsection (14) provides that an 'investment' includes 'any asset, right or interest'.

22. Section 55B, in Part 4A, and Schedule 6 identify various conditions which an applicant for authorisation must satisfy, while section 55E provides for the FCA to give permission 'to carry on the regulated activity or activities to which the application relates or such of them as may be specified in the permission'. Section 55E(5) enables the FCA to 'incorporate in the description of a regulated activity such limitations (for example as to circumstances in which the activity may, or may not, be carried on) as it considers appropriate'.

*The COBS Rules*

23. An authorised person must conduct investment business in accordance with the COBS Rules. These include a duty to act honestly, fairly and professionally in accordance with the best interests of its client (Rule 2.1), to ensure that communications and financial promotions are fair, clear and not misleading (Rule 4.2), and to take reasonable steps to ensure that recommended investments are suitable for the client, which includes obtaining sufficient information about the client's investment objectives, experience and knowledge, and ability to bear investment risks (Rule 9.2).

*Appointed representatives*

24. One way in which a person who is not authorised may become exempt is by becoming the appointed representative of an authorised person pursuant to section 39 of the Act, a system described by Lord Justice David Richards in *Anderson* as outsourcing the regulation of appointed representatives to authorised persons:

> '13. … Instead of being authorised by the FCA, a person may be appointed as an AR by an authorised person who thereby becomes responsible for the AR's compliance with regulatory requirements. Regulation of ARs may thus be said to be outsourced by the FCA to the relevant authorised person. It is designed to reduce the regulatory burden on both the FCA and the large number of tied agents and independent financial advisors whose activities are conducted on a relatively modest scale.'

25. Section 39, which lies at the heart of this appeal, provides as follows:

> '39 **Exemption of appointed representatives**
>
> (1) If a person (other than an authorised person)—
>
> (a) is a party to a contract with an authorised person ("his principal") which—
>
> (i) permits or requires him to carry on business of a prescribed description, and
>
> (ii) complies with such requirements as may be prescribed, and
>
> (b) is someone for whose activities in carrying on the whole or part of that business his principal has accepted responsibility in writing,
>
> he is exempt from the general prohibition in relation to any regulated activity comprised in the carrying on of that business for which his principal has accepted responsibility.
>
> …

> (2) In this Act "appointed representative" means—(a) a person who is exempt as a result of subsection (1), or …
>
> (3) The principal of an appointed representative is responsible, to the same extent as if he had expressly permitted it, for anything done or omitted by the representative in carrying on the business for which he has accepted responsibility.'

26. As explained in *Anderson* at [31], 'business of a prescribed description' refers to business which is prescribed in regulation 2 of the Financial Services and Markets Act 2000 (Appointed Representatives) Regulations 2001 (SI 2001/1217) ('the AR Regulations'). This regulation contains generic descriptions of various kinds of business activity such as 'arranging deals in investments', 'safeguarding and administering investments', and 'advising on investments'. These activities are further defined in articles 25 and 53 of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (SI 2001/544). In outline, 'arranging deals in investments' consists of 'making arrangements for another person (whether as principal or agent) to buy, sell, subscribe for or underwrite' certain kinds of investment, while 'advising on investments' consists of advising a person if the advice is given to the person in his capacity as an investor or potential investor, or agent for an investor or potential investor, and the advice concerns the merits of buying, selling, subscribing for or underwriting particular kinds of investment.

27. I consider further below what Lord Justice David Richards said in *Anderson* about the way in which this section works. The case was concerned with the meaning of the phrase 'part of that business' in section 39(1). In summary, the decision was that an authorised person ('the principal') can limit the permission given to an appointed representative to part of the business of a prescribed description for which the principal is authorised by the FCA. For the moment it is sufficient to say that Lord Justice David Richards drew a distinction in this regard between what activity may be carried on by an appointed representative and how a permitted activity is carried on. Thus the principal can limit its permission (and the corresponding responsibility which it accepts) to a particular kind of activity, but cannot avoid accepting responsibility by a stipulation as to the way in which the activity must be carried on by the appointed representative.

28. Rule 12 of the FCA's Supervision Handbook ('SUP 12') deals with the supervision of appointed representatives by their principals. Among other things, before making the appointment, an authorised person must 'establish on reasonable grounds' that a prospective representative's activities 'do not, or would not, result in undue risk of harm to consumers or market integrity' and that the authorised person has 'adequate controls' over the prospective representative's regulated activities. Once the representative is appointed, the principal is subject to a continuing duty to take reasonable steps to ensure that the representative does not carry on regulated activities in breach of the general prohibition.

*Collective investment schemes*

29. Collective investment schemes are subject to what the judge described as 'notoriously stringent regulatory requirements' which it is unnecessary to set out. They are defined in section 235 of FSMA:

> ‘235 **Collective investment schemes**
>
> (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.
>
> (4) If arrangements provide for such pooling as is mentioned in subsection (3)(a) in relation to separate parts of the property, the arrangements are not to be regarded as constituting a single collective investment scheme unless the participants are entitled to exchange rights in one part for rights in another.
>
> (5) The Treasury may by order provide that arrangements do not amount to a collective investment scheme–
>
> (a) in specified circumstances; or
>
> (b) if the arrangements fall within a specified category of arrangement.’

30. Subject to exceptions not applicable in this case, section 238 prohibits an authorised person from communicating an invitation or inducement to participate in a collective investment scheme, while section 240 prohibits an authorised person from approving for the purposes of section 21 the content of a communication relating to a collective investment scheme if that person would be prohibited by section 238 from effecting the communication himself. Section 241 provides that a contravention of these prohibitions gives rise to an action for damages.

31. There is no doubt, and it is common ground, that the property investment schemes promoted and operated by JHM were collective investment schemes. Under the schemes as implemented, investors were to receive profits from the disposal of the properties; they had no day-to-day control over the management of the properties;

their contributions were pooled; and the properties were managed as a whole by JHM as the operator of the schemes.

32. It is difficult now to understand how anybody aware of the definition in section 235 could have thought that these schemes were not collective investment schemes as there defined. However, the evidence in the court below was that Mr Callen believed that they were not, at any rate until the Supreme Court decided the *FCA v Asset* case in April 2016, a case which emphasised the need to focus on the reality of how the 'arrangements' were to be operated. Accordingly the judge proceeded on the basis that it was at least arguable that Mr Callen acted honestly, that is to say that he believed that the schemes were not collective investment schemes.

*Retail clients*

33. The COBS Rules distinguish between different kinds of client. The default category is a '*retail client*', defined in rule 3.4.1 as 'a *client* who is not a *professional client* or an *eligible counterparty*'. '*Professional clients*' are defined in rule 3.5 to include '*per se professional clients*' and '*elective professional clients*'. Again in outline, '*per se professional clients*' consist of entities required to be authorised or regulated to operate in the financial markets, while a firm may only treat a client as an '*elective professional client*' if appropriate procedures are carried out to ensure that the client has a level of financial sophistication and understands that by so electing it will not have the benefit of the same degree of investor protection as afforded to retail clients:

> '3.5.3 A *firm* may treat a *client* other than a local public authority or municipality as an *elective professional client* if it complies with (1) and (3) and, where applicable, (2):
>
> (1) the firm undertakes an adequate assessment of the expertise, experience and knowledge of the *client* that gives reasonable assurance, in light of the nature of the transactions or services envisaged, that the *client* is capable of making his own investment decisions and understanding the risks involved (the "qualitative test");
>
> …
>
> (3) the following procedure is followed:
>
> (a) the *client* must state in writing to the *firm* that it wishes to be treated as a *professional client* either generally or in respect of a particular service or transaction or type of transaction or product;
>
> (b) the *firm* must give the *client* a clear written warning of the protections and investor compensation rights the *client* may lose; and
>
> (c) the *client* must state in writing, in a separate document from the contract, that it is aware of the consequences of losing such protections.'

34. The third category of client consists of eligible counterparties, dealt with in rule 3.6. Again, a client may be a '*per se eligible counterparty*' or an '*elective eligible counterparty*'. For present purposes it is sufficient to say that an eligible counterparty is either a particular kind of entity or a professional client which requests categorisation as an eligible counterparty. Rule 3.7 provides that a professional client or eligible counterparty may request re-categorisation as a client that benefits from a higher degree of protection.

## KCL's authorisation

35. KCL is and was at the material time authorised by the FCA to conduct investment business. Its authorisation stated that it was 'for specific activities and product types'. The authorisation in evidence appears to have been printed from the FCA Register on 7th October 2022. The authorisation as it stood at the date of the ARA was not in evidence.

36. The authorisation identifies the activities for which KCL is authorised, the types of customer with which it is authorised to deal, and the types of investment for which it is authorised. For example, it is currently authorised for the activity of 'Arranging (bringing about) deals in investments', for all three categories of client, with a list of investment types which include 'rights to or interests in investments (Contractually Based Investments)', 'Rights to or interests in investments (Security)', 'Share', 'Unit' and 'Warrant'. A 'limitation' is specified that:

> 'Rights to or interest in (both): Investment activity in "rights to or interests in investments (security)" and "rights to or interests in investments (contractually based investments)" is limited to the investment types granted for this activity.'

37. It is agreed, however, that this particular limitation is of no relevance to the present case.

38. KCL is also authorised for the activity of 'Advising on investments', for the same investment types and with the same limitation. In this case, however, the customer types include eligible counterparties and professional clients, but not retail clients.

39. In the court below there was an issue whether KCL's authorisation included authorisation to advise on or arrange investment in collective investment schemes. The judge recorded KCL's evidence that:

> '25. … CISs are the subject of notoriously stringent regulatory requirements, and KCL did not have the necessary authorisations to operate them, promote them, or approve their promotion.'

40. In this court, however, it became common ground that KCL was authorised to advise on and arrange investment in such schemes. That is because the term 'unit' in the list of authorised investment types includes units in a collective investment scheme (see section 237(2) of FSMA).

## The Appointed Representative Agreement

41. The ARA between KCL ('the Appointor') and JHM (the 'AR') dated 30th June 2015 contained the following introductory recitals:

> '(A) The Appointor carries on the business of financial services and regulated activities including managing, promoting, dealing, advising and arranging in financial instruments. The Appointor is authorised and regulated by the FCA (Firm Reference Number: 582160) in the conduct of designated investment whose permissions are detailed on the fca.org.uk website.
>
> (B) The AR has agreed to advise on and arrange deals in designated investments for professional clients and eligible counterparties. The AR will not advise on and arrange deals for retail clients or US resident clients. The Appointor has agreed that the AR should do so as its appointed representative under section 39 of FSMA.
>
> (C) The AR has agreed to act as the Appointor's appointed representative in accordance with the provisions of section 39 of FSMA and the terms of this agreement.'

42. By clause 1 of the ARA:

> '1.1 The Appointor appoints the AR as its appointed representative to carry on the Relevant Business on behalf of the Appointor from the date of this Agreement and the AR agrees to carry on the Relevant Business on behalf of the Appointor and to comply with the provisions of this Agreement.
>
> …
>
> 1.3 In accordance with section 39 of FSMA, the AR acknowledges that it does not have permission to carry on any regulated activity in its own right and is therefore not an authorised person under FSMA. However, the AR is exempt from the general prohibition in relation to any regulated activity comprised in the carrying on of the Relevant Business for which the Appointor has accepted responsibility.
>
> 1.4 In accordance with section 39 of FSMA and the FCA Handbook, the Appointor may impose restrictions:
>
> a) on the AR preventing the AR from procuring or attempting to procure persons to enter into investment agreements;
>
> b) as to the types of investment and investment activity in relation to which the AR may act, even if those activities and/or investments form part of the Relevant Business;

> c) on the AR preventing the AR from becoming an appointed representative of any other person. …'

43. 'Relevant Business' was defined as follows (for ease of reference I have added paragraph numbers which were not contained in the ARA itself):

> '(1) Relevant Business means regulated activities which the AR is permitted to carry out under this Agreement which are subject to the limitations of the Appointor's part IV permission as detailed in Schedule 5. For the avoidance of doubt, the AR is not permitted to carry out any investment management activities.
>
> (2) The AR is permitted to market and promote its services, arrange business and give advice.
>
> (3) The AR will conduct business with professional clients, elective professional clients and eligible counterparties.
>
> (4) The AR is not permitted to conduct any business with retail clients.
>
> (5) The Appointor acknowledges that the AR will offer advisory and arranging services to third party investors with regard to residential Property investment. There is no pooling of capital and no CIS.'

44. Schedule 5 of the ARA set out, under the heading 'Limitations of the Appointor's part IVA permissions', a list of the activities for which KCL was authorised. These included 'Advising on investments' and 'Arranging (bringing about) deals in investments' as in KCL's authorisation by the FCA, save that the customer types listed under the latter activity were limited to eligible counterparties and professional clients, and did not include retail clients. Neither party was able to tell us whether retail clients had been included on the list of customer types for this activity on the authorisation as it stood at the date of the ARA. There appear to be two possibilities: either KCL was not authorised to arrange deals for retail clients in 2015 or, if it was, a decision was made by somebody not to include this in Schedule 5 of the ARA.

45. Schedule 5 also contained the following provision which, obviously, did not record the extent of the FCA's authorisation of KCL, but was intended to take effect as a term of the contract between KCL and JHM:

> 'For the avoidance of doubt the AR cannot:
>
> - conduct any investment management activities; or
> - conduct business with US resident citizens; or
> - directly hold client money; or
> - operate a collective investment scheme; or

- market or promote a fund that is an Alternative Investment Fund without the consent of its manager and Appointor; or

- give advice to retail clients'

46. Clause 6 of the ARA contains KCL's acceptance of responsibility:

> '6.1 The Appointor hereby accepts responsibility for all the AR's and the Individuals' activities in carrying on the Relevant Business under this Agreement.'

47. The 'Individuals' referred to were 'those persons for whom the Appointor will apply for approved person status to perform a controlled function that it is intended will appear on the FCA's register as approved persons of the Appointor and will be operating within the AR'. Primarily, this was Mr Callen.

48. The ARA also included terms requiring JHM to provide KCL with any documents in the nature of a prospectus, offering or information memorandum relating to the issue of or subscription for investments at least 72 hours prior to their release, and entitling KCL to withhold consent to the publication of such documents or to require amendments.

49. In return for lending its authorisation to JHM in this way, and accepting responsibility, KCL was to be paid a monthly fee, together with all reasonable costs and expenses.

**The judgment**

50. The claimants put their case against KCL in three ways, summarised by the judge as follows:

> '39. Mr Sims put the claimants' case under three broad headings: (a) as a claim based on breach of the rules in the FCA's Supervision handbook, SUP 12 (the "Supervision Claim"), (b) on the ground that KCL had unlawfully approved promotions so as to become liable to the claimants under section 241 of the Act, and (c) on the basis of section 39(3) of the Act, alone or in conjunction with the Conduct of Business Rules (COBS) or provisions of the Act relating to promotions. The issues I must decide, therefore, are whether KCL has a real prospect (more than barely or merely arguable, not fanciful) of successfully defending itself against those claims at trial.'

51. The judge decided that the first two of these claims (breach of the supervision rules and unlawful approval of promotions) were not suitable for summary judgment, because they involved issues of disputed fact. There is no challenge to those conclusions. We are concerned only with the third of these claims, the section 39 claim. As to this, the claimants' case was that JHM had been appointed to carry on the Relevant Business, and that its activities in promoting the various schemes, which were exactly what the parties had envisaged it would do, fell within the scope of the

responsibility accepted by KCL, so that KCL was liable for breaches of the COBS Rules by JHM in promoting these schemes.

52. KCL submitted that the case on section 39 was flawed: collective investment schemes were excluded from the definition of 'Relevant Business', and therefore not something for which it had accepted responsibility; similarly, the terms of the ARA prohibited JHM from dealing with retail clients. Whatever was done, therefore, was outside the terms of KCL's acceptance of responsibility, and therefore not subject to section 39.

53. The judge dealt separately with schemes 1 to 7 on the one hand and scheme 8 on the other. As I have said, his decision not to give summary judgment on scheme 8, to which different considerations applied, has not been challenged. His reasoning in relation to schemes 1 to 7 was as follows.

54. So far as KCL's first submission was concerned, the judge drew a distinction between operating and promoting/marketing a collective investment scheme. Operating such a scheme was not a prescribed category of business activity specified in the AR Regulations. Accordingly permission to operate such a scheme was outside the scope of section 39: even if it purported to do so, an authorised person could neither give permission to an appointed representative to operate such a scheme nor accept liability for such operation pursuant to the section. The operation of a collective investment scheme by an appointed representative would therefore be subject to the general prohibition in section 19, and thus unlawful, but the principal would not be responsible. This did not mean that an authorised person who purported to appoint an appointed representative to operate such a scheme would necessarily escape liability. There might be liability at common law on the basis of participation in a joint enterprise, but that would not arise under section 39 and was not the basis on which the claimants had pleaded their case.

55. On the other hand, the promotion and marketing of a collective investment scheme was a prescribed category of investment business within the scope of section 39. The judge rejected the submission that the promotion and marketing of such schemes was excluded from the definition of 'Relevant Business'. On the contrary, when the ARA was interpreted against the relevant background, it was beyond doubt that the parties intended the marketing of the very schemes which JHM had marketed to be 'Relevant Business': they were the '*raison d'être*' of the agreement. Accordingly KCL had accepted responsibility for JHM's activities in marketing the schemes, and those activities were unlawful under sections 238 and 241 of FSMA.

56. The judge accepted KCL's submission that arranging deals with retail clients was prohibited by the ARA. He held, however, applying the distinction in *Anderson*, that 'specifying the characteristics of those investors who may be appropriate candidates for an investment' was a 'how' and not a 'what': it was 'an instruction which is directed at how the appointed representative should carry on the business, not part of the definition of the business':

> '54. … It would strip section 39 of much of its intended effect if a mistake about the categorisation of a client deprived the appointed representative of exemption, and the client of protection. The line between "how" and "what" is drawn not by

> considering the way a particular limitation is expressed. Skilful drafting can easily express instructions about an agent's conduct ("do not market to retail clients") or legal categorisation ("market only if the investment is suitable") as if they were limitations on authority ("you may market only to professional clients for whom the investment is suitable") or on the scope of the business ("relevant business is marketing suitable investments to professional clients"). What matters is the commercial activity ("marketing") and its substance.'

## The appeal

57. Mr Simon Howarth KC for KCL advances two grounds of appeal. The first is that on its true construction the ARA prohibited JHM from conducting collective investment scheme business, with the consequence that KCL neither gave permission nor accepted responsibility for the conduct of such business by JHM pursuant to section 39. The second is that the ARA prohibited the promotion of the schemes to retail clients, this being a prohibition which restricts what can be done, not how it can be done.

58. There is no challenge to the judge's conclusion that, if KCL did accept responsibility for the activities of JHM, the judge was right to order summary judgment in the claimants' favour.

### Ground 1 – collective investment schemes

*Submissions*

59. Ground 1 raises a question of interpretation of the ARA: does it on its true construction prohibit the promotion and marketing of collective investment schemes? Mr Howarth submitted that the distinction drawn by the judge between operating and promoting/marketing such schemes was too fine a distinction. In the case of an agreement which, although not entirely informal, was not professionally drafted, it was too subtle to read the ARA as permitting the marketing but not the operation of such schemes. Rather, the better reading of the ARA was that JHM was not permitted to have anything to do with collective investment schemes.

*Analysis and conclusion*

60. I would reject this submission. The distinction between the promoting and marketing on the one hand and the operation on the other hand of a collective investment scheme is recognised in the legislation. Section 235, which defines collective investment schemes, refers expressly to the 'operator' of such a scheme, and that term is defined in section 237(2). However, the activities listed in the AR Regulations (i.e. the 'business of a prescribed description' referred to in section 39(1)) do not include the operation of a collective investment scheme, although they do include arranging and advising on investment in such a scheme.

61. Turning to the ARA, the definition of 'Relevant Business' states in its fifth paragraph that the appointed representative will offer advisory and arranging services to third-party investors with regard to residential property investment. That was of course

exactly what was intended. I agree with the judge that the further sentence that 'There is no pooling of capital and no CIS' is to be read as a statement of the parties' understanding of the position, and not as a limitation on the permission granted by the remainder of the definition. That understanding was mistaken, but this does not alter the effect of the final sentence. As in *Street v Mountford* [1985] 1 AC 809, where the parties described their agreement as a licence when on its true analysis it was a lease, the label which the parties attached to the proposed transactions cannot detract from the reality of what was agreed.

62. The business which the appointed representative was permitted to conduct was as set out in Schedule 5 of the ARA. The permissions were identified by reference to the specified activities which, by virtue of the inclusion of 'units', included permission to advise on and arrange deals in collective investment schemes.

63. The concluding paragraph of Schedule 5 then makes the position clear: 'For the avoidance of doubt the AR cannot … operate a collective investment scheme'. This clarifies, in case it were necessary, that the permission granted to advise on and arrange deals in collective investment schemes does not include permission to operate them. Thus KCL did not give permission to JHM to operate a collective investment scheme and did not accept responsibility for the operation by JHM of such a scheme. But this does not negative or detract from the permission granted in the earlier parts of Schedule 5 to advise on and arrange deals in such schemes. Rather, it reflects the distinction between operating and advising/arranging which exists in the legislation.

64. I do not regard this as an unduly subtle interpretation of the parties' agreement. On the contrary it gives effect to its clear language. It is not possible to read the ARA as a blanket prohibition on the appointed representative having anything to do with collective investment schemes, at any rate once the significance of the term 'Unit' is understood. As this was a contract, even if not professionally drafted, to be entered into by parties who (given its purpose and subject matter) could reasonably be expected to have some understanding of the regulatory background, the parties can be taken to have understood that the inclusion of the term 'Unit' in Schedule 5 meant that the permission granted to JHM did include permission to advise on and arrange deals in collective investment schemes.

65. I would therefore reject ground 1 of this appeal.

**Ground 2 – retail clients**

*The nature of the issue*

66. The nature of the issue arising on ground 2 is different. A preliminary question is whether the ARA prohibits the appointed representative from giving advice to or arranging deals for retail clients. As to this, the position is clear: introductory recital (B) states that the appointed representative will not advise on and arrange deals for retail clients; the fourth paragraph of the definition of 'Relevant Business' spells out that the appointed representative is not permitted to conduct any business with retail clients; the customer types identified for each category of business activity in Schedule 5 include other customer types but not retail clients; and the final bullet point in the concluding 'For the avoidance of doubt' paragraph of Schedule 5 again makes clear that the appointed representative cannot give advice to retail clients.

67. Taken together these provisions make clear that the ARA does indeed prohibit JHM from giving advice to or arranging deals for retail clients. The real question, however, is whether such a limitation on the scope of the permission given to JHM by KCL is permitted by section 39 of FSMA – in *Anderson* terms, whether it is an effective limitation as to *what* activity may be carried on or an ineffective limitation which seeks impermissibly to prescribe *how* the permitted activity (e.g. of arranging deals) is carried on; or in terms of section 39 itself, whether the business of a prescribed description (e.g. arranging deals) for which KCL is authorised can be divided into two parts, one consisting of arranging deals for professional clients and eligible counterparties, and the other consisting of arranging deals for retail clients.

*The authorities*

68. Before considering this question further it is necessary to deal with the authorities which culminated in this court's decision in *Anderson*.

69. *Martin v Britannia Life Ltd* [2000] Lloyd's Rep PN 412 concerned the scope of a financial consultant's authority. The consultant was authorised to give advice 'as to the sale of investments issued by any member of' a group of insurance companies operating under the Financial Services Act 1986. He was, therefore, an appointed representative of an authorised person for the purpose of section 44 of the 1986 Act. Section 44(6) dealt with the principal's responsibility for the actions of the appointed representative in materially the same terms as section 39(3) of FSMA. Mr Justice Jonathan Parker described the concept of 'investment advice' in these terms:

> '5.2.5 … In my judgment it is neither appropriate in the context of the 1986 Act, nor for that matter would it be realistic, to seek to limit the concept of "investment advice" by reference to the extent to which the advice relates to the "merits" (i.e. to the advantages or disadvantages) of a particular "investment" as defined; and if that be accepted, it seems to me that it must follow that the concept of "investment advice" will comprehend all financial advice given to a prospective client with a view to or in connection with the purchase, sale or surrender of an "investment", including advice as to any associated or ancillary transaction notwithstanding that such transaction may not fall within the definition of "investment business" for the purposes of the 1986 Act.
>
> ...
>
> 5.2.12 In my judgment, just as "investment advice" extends beyond advice as to the merits or otherwise of a particular "investment" as a product (see paragraph 5.2.5 above), Mr Sherman's authorised activities under the 1990 Agreement (which, as I pointed out earlier, mirror the provisions of section 44(3) of the 1986 Act) similarly so extended. If anything, the provisions of section 44(3) serve to reinforce my conclusion as to the width of the concept of "investment advice". An activity consisting of "giving advice … about entering into investment agreements" seems to me to involve much more than advising

> as to the terms of a particular investment agreement, without regard to the question whether it is appropriate for the client to enter into such an agreement, given his particular financial situation. Similarly, the activity of "procuring or endeavouring to procure [clients] to enter into investment agreements …" seems to me to extend beyond stressing the advantages of a particular product and to include advising or recommending that it is appropriate for the client to purchase a particular product.'

70. The effect of this decision is summarised in *Jackson and Powell on Professional Liability*, 8th ed (2017), para 15-027, in terms which were approved in *Anderson* at [47] (see now the 9th ed (2021)):

> ' … while the terms of an appointed representative's express authority might be limited to providing investment advice to customers in relation to particular products of his principal, conduct that is incidental to the provision of that advice (such as soliciting the customers, identifying the financial and personal circumstances of the particular customer, assisting in any application that the customer might choose to make) will still fall within the actual authority of that representative … [in *Martin's* case] the advice was inherently bound up with and incidental to the advice given by him in relation to other investments.'

71. Although concerned with legislation which is not identical, this approach supports taking a broad view of what is included in the various categories of regulated activity with which section 39 is concerned.

72. *Ovcharenko v Investuk Ltd* [2017] EWHC 2114 (QB) was concerned with an appointed representative agreement, entered into pursuant to section 39 of FSMA, under which the representative was permitted to carry on three categories of designated business: (a) arranging and bringing about deals and investments for clients, (b) making arrangements with a view to transactions and investment, and (c) advising on the investments. However, the agreement also provided that the representative 'will not, for the duration of this agreement, carry out any activity in breach of section 39 or of any other applicable law'. The claimants alleged that the representative had recommended an investment without carrying out adequate due diligence and had made misleading statements. They sought to hold the principal liable under section 39 as having accepted responsibility for the representative's conduct.

73. His Honour Judge Waksman QC rejected the principal's attempt to avoid liability in reliance on limitations in the appointed representative's authority, viewing this as contrary to section 39's purpose of protecting investors:

> '32. I, therefore, turn to the logically first question which is whether there is, in any event, a real, as opposed to a fanciful, defence. The argument made on behalf of D2 [the principal] runs thus. What D1 [the appointed representative] is alleged to

have done was to give investment advice. While it is true that this was firmly encompassed by the permitted services in the authorised representative agreement, there was a problem for D1 because the client agreement expressly stated that whatever else it did it must never communicate an inducement to invest with the client or arrange a deal, or provide any investment advice. That, says D2, is what is alleged against D1 and if that is right, it has not only exceeded the terms of the client agreement but it has, in fact, exceeded the terms of implied limitation on the permission under the authorised representation agreement. That being so, D2 cannot, in any event, be liable for the defaults of D1.

33. I regard that proposition as wholly unarguable for the following reasons. First of all, as would be expected, the whole point of section 39(3) is to ensure a safeguard for clients who deal with authorised representatives but who would not otherwise be permitted to carry out regulated activities, so that they have a long stop liability target which is the party which granted permission to the authorised representative in the first place. In my judgment, section 39(3) is a clear and separate statutory route to liability. It does no more and no less than enable the claimant, without law [sc. more], to render the second defendant liable where there have been defaults on the part of the authorised representative in the carrying out of the business and which responsibility had been accepted. The business for which responsibility had been accepted encompasses the services set out in clause 3 of the authorised representative agreement. It matters not whether, as between the client, the authorised representative was not entitled to proffer those services. That is an entirely separate matter.

34. In seeking to rebut that conclusion, Mr Marquand has relied upon certain other provisions within the authorised representative agreement. I have recited them. He relies on paragraph 4.3 which is simply a promise by D1 to D2 that it will not do anything outside clause 3 and, in fact, it did not but also would not act in a manner which would breach any requirement or limitation applied including what had been incorporated into that permission.

35. All that does is regulate the position *inter se* between D1 and D2. It says nothing about the scope of the liability of D2 to the claimants under section 39(3). The same point can be made in respect of clause 4.7 which says, "The representative will not carry out any activity in breach of section 19 of FSMA which limits the activities that can be undertaken or of any other applicable law or regulation". Again, that is a promise made *inter se*.

> 36. The reason for those promises is obvious. D2 will be, as it were, on the hook to the claimants as in respect of the defaults of D1 and if those defaults have arisen because D1 has exceeded what it was entitled to do or has broken the law in any way, then that gives a right of recourse which sounds in damages on the part of D2 against D1. If Mr Marquand was correct, it would follow that any time there was any default on the part of an authorised representative, for example, by being in breach of COBS, that very default will automatically take the authorised representative not only outside the scope of the authorised representative agreement but will take D2 outside the scope of section 39(3), in which case its purpose as a failsafe protection for the client will be rendered nugatory; that is an impossible construction and I reject it.'

74. On this analysis, it is necessary to distinguish between limitations on the scope of the appointed representative's permission to conduct certain kinds of business and obligations undertaken as between the principal and the appointed representative which do not affect the scope of that permission or limit the responsibility accepted by the principal. In applying that distinction, the investor protection purpose of section 39 must be kept firmly in mind. As Judge Waksman put it, 'the whole point' of the section is to give the investor a remedy against the principal for misconduct by the appointed representative. That purpose would be defeated if the principal could circumscribe the scope of the representative's permission, and thus its acceptance of responsibility, to exclude responsibility for such misconduct.

75. In *Anderson* the principal was authorised by the FCA to carry on various categories of investment business described in the generic terms of the AR Regulations. It appointed the incongruously named Midas Financial Services (Scotland) Ltd as its appointed representative, on terms which limited Midas's authorisation to the sale of specified products using a 'Company Agency', the effect of which was that Midas was only authorised to sell the products of companies with which the principal had a relationship. Instead of doing so, Midas advised investors to put their money in what turned out to be a Ponzi scheme. The investors argued that because Midas was authorised in generic terms to give advice on and arrange deals in investments, the principal's responsibility under section 39 extended to advice given on, and deals arranged in, any type of investment falling within the principal's authorisation and that the term requiring the use of a Company Agency was ineffective to limit the responsibility which the principal had accepted pursuant to section 39(3). The claim failed. This court (Lord Justices David Richards and Hamblen and Mr Justice Snowden) held that the principal had given permission, and accepted responsibility, only for that part of its business of advising on investments which was carried on with the use of a Company Agency.

76. Lord Justice David Richards explained the way in which section 39 is intended to work in a passage which, despite its length, is worth citing in full:

> '30. Section 39(3) imposes liability on the authorised person (Sense, in this case) for the acts or omissions of the AR "in carrying on the business for which he (i.e. the authorised

person) has accepted responsibility". The quoted words define the extent of the authorised person's liability.

31. Those words refer back to section 39(1) which, for these purposes, contains three critical steps. First, there must be a contract (the AR Agreement) between the authorised person and the AR which "permits or requires him [the AR] to carry on *business of a prescribed description*". As Mr Sims[1] rightly submits, that is a reference to one or more of the businesses prescribed in generic terms in regulation 2 of the AR Regulations.

32. Second, the AR must be someone "for whose activities in carrying on *the whole or part of that business* [the authorised person] has accepted responsibility *in writing*". There are a number of points that arise. The acceptance of responsibility must be in writing, normally but not necessarily in the AR Agreement. In order to determine the extent of the acceptance of responsibility it will be necessary to refer to the terms of the document by which the authorised person accepts responsibility. The words "that business" refer back to "business of a prescribed description" in section 39(1)(a), which the authorised person permits or requires the AR to carry on. The words "the whole or part" demonstrate that the acceptance of responsibility need not relate to all activity that could fall within a generic type of business described in the AR Regulations and specified in the AR Agreement. The acceptance of responsibility may relate to part only of such business, as stated in the written acceptance of responsibility.

33. Third, if paragraphs (a) and (b) of section 39(1) are satisfied, the AR "is exempt from the general prohibition in relation to any regulated activity comprised in the carrying on of *that business for which his principal has accepted responsibility*". The italicised words refer back to paragraph (b), requiring identification of "the whole or part of that business" for which responsibility is accepted. These words of exemption do not need to repeat "the whole or part of" because paragraph (b) permits the authorised person to accept responsibility for part of a generic type of business and they are, therefore, necessarily encompassed within the italicised words.

34. The scheme of section 39(1) is thus clear. An AR is an exempt person only to the extent that an authorised person has accepted responsibility for the business to be carried on by the AR. If an authorised person has accepted responsibility for only part of a category of business, the AR will be exempt only in respect of that part. This makes sense. Acceptance of

[1] Counsel for the claimants in *Anderson*, as in this case.

responsibility is the equivalent of authorisation and is essential to the enjoyment of exempt status by the AR. The AR will be subject to the general prohibition as regards any activity falling outside the business, or part of the business, for which the authorised person has accepted responsibility.

35. I have up to this point focused on the construction of section 39(1), but that is critical because section 39(1) defines the scope of section 39(3). The responsibility, and hence potential liability, of an authorised person under section 39(3) is limited to the acts or omissions of the AR "in carrying on the business for which [the authorised person] has accepted responsibility". Those words take one back to section 39(1), and specifically to section 39(1)(b). Again, the structure of the section is clear. As the quid pro quo for accepting responsibility for the activities of an AR in carrying on the whole or part of a prescribed business, and thereby exempting the AR from obtaining its own authorisation, the authorised person becomes personally liable to third parties for the AR's acts or omissions in the course of those activities. Exemption and liability under section 39(3) are co-extensive.

36. In my judgment, Mr Sims' submission that the authorised person necessarily must accept responsibility for the whole of a generic description of business, provided it falls within its own FCA authorisation, cannot be reconciled with the terms of section 39. As the judge said at [133],

> "There is no indication in the wording of section 39, or in the case-law, that indicates that the business for which responsibility is accepted is to be determined not by reference to the contract, but by reference to the authorisations granted to the principal which are to be found in the Financial Services register".

37. Mr Sims submits that the purpose of the words "the whole or part of that business" is to enable an AR to have agreements under section 39 with more than one authorised person. They cater for the situation where more than one authorised person has accepted responsibility for the business to be carried on by an AR and each authorised person is itself authorised for only one or some but not all of the businesses to be carried on by the AR. An authorised person cannot accept responsibility for a business for which it does not have authorisation from the FCA. While I accept that the words "the whole or part of" facilitate the involvement of more than one authorised person with the same AR, I do not see the basis for restricting the clear and unqualified words of section 39(1) to this situation. The purpose of section 39(1) is to confer exempt status on persons in a manner which will fulfil the underlying regulatory and protective purposes of the legislation. It may make perfect

sense to limit an AR to a partial exemption, having regard to the breadth and depth of the expertise of that AR or indeed of the authorised person. If, as Mr Sims submits, the legislative intention is to make an authorised person responsible for all the activities of an AR that fall within the authorised person's own authorisation, it is inexplicable that section 39(1) is not drafted in clear terms to have that effect. For my part, I find it impossible to spell it out of section 39(1) as it is in fact drafted.

38. Mr Sims further submitted that the words "part of" enabled an authorised person, as a matter of contract, to "delegate" part of its own statutory licence to an AR. For example, an authorised person with authority to conduct general insurance intermediation and mortgage intermediation could delegate only one of those to a particular AR. Mr Sims submitted that this would prescribe the scope of AR's statutory exemption under section 39(1) and would be relevant to the internal relationship between the authorised person and the AR, but it would have no impact on the liability of the authorised person for the activities of the AR under section 39(3). It will be apparent from what I have already said that this appears to me to be an impossible construction. Not only is the extent of the authorised person's responsibility defined by the acceptance in writing required by section 39(1)(b), which in terms refers to "the whole or part of that business" but, for the reasons given above, the acceptance of responsibility under section 39(1) and the imposition of liability under section 39(3) are co-extensive.

39. Mr Sims submitted that this construction deprives the words "as if" in the phrase "is responsible, to the same extent as if he had expressly permitted it" of any legal meaning. I address below the purpose of these words but, in short, they recognise that at common law giving authority for an activity will not necessarily impose liability on the principal for all actionable acts or omissions of the agent that may occur in relation to the conduct of that activity, particularly as regards tortious liability. These words overcome those difficulties.

40. A further submission made by Mr Sims was that, even if statutory responsibility may be restricted to only part of a business, liability cannot be excluded by reference to a failure properly to conduct that business. I agree with that, but I do not agree with Mr Sims' next submission that it is impossible to distinguish between "what" and "how", so that the only sensible answer is to define the authorised person's responsibility by reference to its authority to conduct business of a prescribed, generic description. In my view, it will be a rare case which presents any difficulty in distinguishing between what activity may be carried on and how a permitted activity is carried on.'

77. For the purpose of this appeal, I would draw attention to four points.

78. First, the appointed representative's exemption and the principal's responsibility are co-extensive.

79. Second, the permission given to the appointed representative, and the corresponding acceptance of responsibility by the principal, may be limited to the carrying on of only part of the generic business for which the principal is authorised.

80. Third, it was in this context that Lord Justice David Richards drew a distinction between 'what' and 'how'. The point of the distinction was to enable the principal's acceptance of responsibility to be limited to certain kinds of business (the 'what', i.e. 'what activity may be carried on'), while preventing the principal from drafting its way out of responsibility by limiting its permission by reference to the way in which the permitted business was to be carried on (the 'how', i.e. 'how a permitted activity is carried on'). For example, a grant of permission which is conditional on the business being carried on properly will be ineffective to limit the principal's responsibility to investors. If I may say so, the distinction between 'what' and 'how' sheds valuable light on section 39, although it is always necessary to ensure that such a striking phrase does not come to replace the statutory language. The statutory language refers to 'part of that business', i.e. part of the business of a prescribed description which the principal is authorised to conduct.

81. Fourth, it is significant that Lord Justice David Richards referred to 'the underlying regulatory and protective purposes of the legislation'.

*The rival submissions in outline*

82. Mr Howarth for KCL submitted that the prohibition in the ARA on dealing with retail clients was a prohibition as to what business could be conducted by the appointed representative, not a prohibition on how the permitted business could be conducted. A restriction as to the status of the client was no different from the restriction in *Anderson* as to the status of the providers whose products could be sold to clients. Just as in *Anderson* it made commercial sense for the principal to accept responsibility limited to the sale of particular investment products whose sale it would be able to supervise, so here it made commercial sense for the principal to trust the appointed representative to deal with professional clients, but not with retail clients who would be entitled to a higher degree of investor protection requiring more onerous supervision. Moreover, KCL was not itself authorised by the FCA to advise on or arrange deals for retail clients, and was therefore entitled to impose the same limitation on the permission which it gave to an appointed representative under section 39. It could not grant a permission to deal with retail clients which it did not itself have.

83. Mr Hugh Sims KC for the claimants submitted that the classification of clients is concerned with how the business is carried on and does not form part of the description of a business activity for the purposes of section 39. Such classification requires an evaluative and qualitative assessment under COBS rule 3.5 very similar to the assessment of suitability of an investment under rule 9.2, which is undoubtedly concerned with how the business is carried on. It would be odd if the classification of clients were to be regarded differently. The prohibition on dealing with retail clients

in the ARA operates as a stipulation between the parties, but does not affect the scope of the permission given to JHM for the purposes of section 39, or the scope of the responsibility accepted by KCL.

84. Although this issue arises on an application for summary judgment, neither party submitted that we are not in a position to decide it one way or the other.

*Analysis and conclusion*

85. The critical question concerns the meaning of 'business of a prescribed description' in subsection (1)(a) of section 39 and 'the whole or part of that business' in subsection (1)(b). These expressions must be interpreted having regard to the purposes of the section, which include providing investors who deal with appointed representatives with a remedy against the principal whose grant of permission to carry on investment business has enabled the appointed representative to operate in the financial services sector. That statutory purpose applies regardless of whether the relationship between the principal and its representative is akin to a genuine agency or, as in this case, the principal is effectively lending its authorisation to enable the representative to operate in return for a fee.

86. Dealing first with the meaning of 'business of a prescribed description' in subsection (1)(a), *Anderson* explains at [32] that this is a reference to one or more of the businesses prescribed in generic terms in regulation 2 of the AR Regulations. This regulation refers to certain kinds of activity. It follows, in my judgment, that the 'description' of the business in subsection (1)(a) refers to the activity in question, in this case 'Advising on investments' and 'Arranging deals in investments'. Those generic descriptions are not defined by reference to the classification of the clients to whom advice may be given or for whom deals may be arranged. They do not distinguish, as descriptions of activities, between giving advice to or arranging deals for professional clients and eligible counterparties on the one hand and retail clients on the other.

87. The question then arises whether, for the purpose of subsection (1)(b), the business of 'Advising on investments' and 'Arranging deals in investments' can be divided into two parts, one of which consists of advising and arranging deals for retail clients while the other consists of advising and arranging deals for other types of customer, enabling an authorised person to give permission limited to the latter part of the business. In my judgment that is not a sensible reading of what is meant by 'part of that business' in subsection (1)(b).

88. First, the type of business which an appointed representative is permitted to conduct is distinct from the question of for whom that business is undertaken. The issue in the present case is not comparable to the issue in *Anderson*.

89. Second, deciding whether a client is a professional client or eligible counterparty requires an assessment which has a great deal in common with the assessment of suitability which must be carried out before an investment can be recommended to a client regardless of the client's status. It is common ground that an assessment of suitability is concerned with how the business is conducted, so that if an appointed representative recommends an unsuitable investment, the principal is responsible. That responsibility cannot be avoided by a contract term purporting to limit the

permission given to the appointed representative to recommending investments which are suitable for the investor. Similarly, in *Anderson* terms, the decision whether a client should be classified as a professional client or eligible counterparty forms part of the way in which the business activity in question is carried on. If a client is mistakenly classified as a professional client or eligible counterparty, the principal should be responsible for the representative's error.

90. To limit the appointed representative's authority to dealing with professional clients and eligible counterparties necessarily involves the principal entrusting to the appointed representative the decision about how a prospective client should be classified, just as it entrusts to the representative the decision whether an investment is suitable for an investor. It makes no legal or commercial sense to say that the principal entrusts that decision to the representative when the representative gets it right, but not when it gets it wrong. That would be close to the kind of avoidance of responsibility by clever drafting which was ruled out in *Ovcharenko* and *Anderson*.

91. Third, to interpret the term 'part of that business' in subsection (1)(b) as enabling a principal to grant permission, and to accept responsibility, limited to providing advice to or arranging deals for professional clients and eligible counterparties only would be contrary to the purpose of investor protection which underlies section 39. It would mean, as Mr Sims pointed out, that a professional investor dealing with an appointed representative would have a higher degree of protection than a retail client or indeed a retail client who was misclassified as a professional investor. It would have the consequence in the present case that the one claimant who was correctly classified as a professional investor would have a remedy against KCL, while the other claimants who should have been classified as retail clients but were wrongly classified as professional investors would not. That would make little sense.

92. For these reasons I would hold that the stipulation in the ARA that JHM should deal only with professional clients and eligible counterparties operated as a contractual term as between JHM and KCL, but did not affect the scope of the permission given by KCL, or the responsibility which it accepted, for the purposes of section 39 of FSMA.

93. The only point which has caused me to doubt this conclusion is whether it means that KCL was giving permission to JHM to do something, i.e. to deal with retail clients, which it was not itself authorised to do having regard to the terms of its own authorisation by the FCA. That may be so, but it does not in my judgment detract from the interpretation of section 39 which I regard as correct and which gives sensible effect to the statutory purpose of investor protection. The maxim '*nemo dat*' has a venerable history, but I do not think it applies in the circumstances of this case.

94. Thus, on the assumption that KCL's own authorisation does not authorise it to deal with retail clients, the responsibility is on KCL to ensure in its own dealings that it deals only with investors who are correctly classified as professional clients and eligible counterparties, and a retail client investor to whom it gives advice, or for whom it arranges a deal, will be protected. Similarly, on the appointment of JHM as an appointed representative, the onus is on KCL to supervise the activities and systems of its representative and KCL's responsibility as principal will be engaged in the event that a retail client is wrongly classified as a professional client. As it is KCL which has enabled JHM to promote and market its investment schemes, in the course

of which and as part of that activity JHM will inevitably have to decide how investors should be classified, this is a fair outcome. An interpretation of section 39 which places responsibility on the principal except in cases where there is a clear demarcation between different parts of its business, and the representative is appointed only in respect of a clearly demarcated part of that business, is in accordance with the statutory objectives.

95. I would therefore reject ground 2.

**Conclusion**

96. For these reasons I would dismiss the appeal.

**LORD JUSTICE LEWISON:**

97. I agree with my colleagues that ground 1 fails. I have more difficulty with ground 2. Part of my difficulty is, as Lord Justice Males has said, the legislation is something of a labyrinth. I do not consider that the limited argument on the overall scheme of the Act that was possible on an application for summary judgment has given me Ariadne's thread to steer my way confidently through. Since mine is a minority judgment, and makes no difference to the outcome of the appeal, I can explain my difficulty shortly.

98. Section 39 applies to an agreement with an "authorised person". An "authorised person" is defined by section 31. The relevant part of the definition is:

> "a person who has a Part 4A permission to carry on one or more regulated activities;"

99. A Part 4A permission is permission given under Part 4A. The FCA's power to grant permission is in section 55E. The relevant parts of that section provide:

> "(2) The FCA may give permission for the applicant to carry on the regulated activity or activities to which the application relates or such of them as may be specified in the permission.
> …
>
> (4) If it gives permission, the FCA must specify the permitted regulated activity or activities, described in such manner as the FCA considers appropriate.
>
> (5) The FCA may—
>
> (a) incorporate in the description of a regulated activity such limitations (for example as to circumstances in which the activity may, or may not, be carried on) as it considers appropriate;
>
> (b) specify a narrower or wider description of regulated activity than that to which the application relates;

> (c) give permission for the carrying on of a regulated activity which is not included among those to which the application relates and is not a PRA-regulated activity."

100. I consider that it is at least arguable that a person is not an authorised person except to the extent that his carrying on of regulated activities is authorised by the FCA (or the PRA). For example if a person is only authorised to arrange deals in investments he is not an authorised person as regards safeguarding or administering investments. It seems to me, therefore, that if an ARA purports to appoint a representative to carry on business which the principal is not authorised to carry on, that agreement is not, to that extent, an agreement with "an authorised person".

101. The terms of KCL's authorisation do not appear to have received any attention in the court below. It was something that this court drew attention to in the course of argument; and consequently neither side deployed fully developed arguments in relation to its significance.

102. In the present case, KCL's authorisation in relation to advising on investments does not authorise it to advise retail clients. Since the FCA is empowered to grant permission for such of the regulated activities as may be specified in the permission (describing them), and has done so in relation to advising on investments, I would regard the exclusion of retail clients as falling on the "what" rather than the "how" side of the line. I do not think that, for this purpose, it matters that the regulated activities are described in general and generic terms in the AR Regulations. Section 39 (1) (b) specifically permits a contract to cover a business which is only part of that generic description. On the face of it, it seems to me that KCL was not an "authorised person" as regards advising retail clients on investments.

103. How to distinguish between retail clients and others is covered by COBS. COBS, I would accept, is part of "how" to carry out regulated activities but that does not overcome what I regard (in the absence of further argument) as the fundamental point that KCL was not authorised to advise such clients.

104. In short, at this stage of the case, despite the strong consumer orientated arguments which militate in favour of the conclusion to which my colleagues have come, I would not be prepared to enter judgment summarily on this part of the case.

**SIR GEOFFREY VOS, MR**

105. I understand the concerns expressed by Lord Justice Lewison in relation to the second ground of appeal. Nonetheless, I am persuaded that Lord Justice Males is right in his analysis of both the first and second grounds of appeal. Accordingly, I agree with him that the appeal should be dismissed on both grounds.