

Shared Ownership Good Practice Principles

Supplementary Guidance for delivery of joint venture model



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This document sits alongside the Scottish Government Good Practice Principles for shared Ownership of Onshore Renewable Energy Developments, available at www.localenergyscotland.org/goodpractice

The guidance in this document is intended to support developers of commercial projects to deliver a joint venture structure for a shared ownership project, recognising that there are several regulatory frameworks which must be respected. The guidance in this document will support developers to engage with communities while remaining compliant with the relevant regulatory areas. There is also guidance in this document for other supporting agents in the sector to ensure their activity also remains compliant.

1 Introduction

This guidance applies only to projects which are developed and owned by a 'joint venture vehicle' which is Option 1 for shared ownership in the Good Practice Principles document.

This guidance will consider how the structure of a joint venture vehicle can impact on the regulatory issues and will then consider some of the regulatory issues developers and other supporting agents should be mindful of when considering joint venture arrangements.

The purpose of this guidance note is to provide developers and other supporting agents with some information about certain regulatory issues which may arise when discussing joint venture arrangements with communities.

This note is not intended to be legal advice and developers and other supporting agents should seek their own legal advice when considering joint venture arrangements.

This note only looks at the project vehicle aspects. It does not consider any regulatory issues relating to community level. Establishing a community group is subject to separate regulation and advice should be sought from Local Energy Scotland on this point.

This guidance provides details for projects which are led by developers inviting community involvement in a scheme. Projects which are led by community groups may be subject to different regulatory restraints and professional advice should always be sought. Local Energy Scotland can support community groups who wish to explore establishing a shared ownership project.

An overview of process and stages for other shared ownership models (split ownership and shared revenue) is available in the Process Checklist available at www.localenergyscotland.org/sharedownershipgoodpractice).

2 Background to regulatory landscape

A glossary of commonly-used terms in this document is available in Section 6.

Developers and supporting agents should be aware that there are a large number of regulatory issues involved when engaging with communities as regards potential joint venture arrangements. In addition, the regulatory landscape changes reasonably regularly so developers and supporting agents should ensure that where they have a concern as regards their ongoing activities, they seek appropriate advice at an early stage.

The main regulatory areas developers and supporting agents are likely to come across are:

1. unregulated collective investment scheme concerns which mean that certain types of legal structure of the joint venture vehicle cannot be communicated to communities;
2. the financial promotion restriction which prevents the communication to communities of certain types of investment opportunity; and
3. the so called “general prohibition” which is the restriction on carrying on regulated activities (for example buying and selling shares, advising on whether a community should invest) without either being authorised by the Financial Conduct Authority (“FCA”) or being exempt¹.

Infringing any of these restrictions is a criminal offence. Each of these restrictions are explained further below.

¹ The Financial Services & Markets Act 2000 (Regulated Activities) Order 2001

3 Legal structure of the joint venture vehicle

In this section we look at the restrictions around a Limited Liability Partnership and a Private Company Limited by Shares

Where a project is delivered through a 'joint venture vehicle', a special purpose joint venture vehicle (SPV) will need to be set up, where both the community and developer are shareholders or members (as appropriate).

The majority of joint venture vehicles involving a developer and a community entity will either be a limited liability partnership or a private company limited by shares. Each of these structures has different regulatory consequences which we consider below. There may be other legal structures a developer wishes to consider and advice should be taken as regards the regulatory implications of any other structure.

Limited Liability Partnership (“LLP”)

What is a LLP?

A LLP is a form of partnership in which some or all partners have limited liabilities.

Can a LLP be deemed a collective investment scheme?

There is a risk that a LLP structure could be an unregulated collective investment scheme, which means that if this is the case, the project cannot be communicated to a community at any stage – clearly unworkable in practical terms as the community would not be able to be involved.

Therefore, if a developer wishes to use a LLP structure, they must ensure that the scheme does not inadvertently become a collective investment scheme.

When can a LLP be deemed a collective investment scheme?

A principal characteristic of a collective investment scheme is that the participants in the LLP do not have day to day control over the management of the property, although they may have the right to be consulted or give directions².

How to avoid a LLP being deemed a collective investment scheme?

Developers should consider the following:

- for a developer to use a LLP as its joint venture vehicle, the community must have equal voting power with the developer
- the community must actually exercise that control sufficiently to be regarded as being in effective control. It is not enough simply for the LLP agreement to provide for equal voting power - in practice, the community must actually exercise their control rights; and
- the community should not delegate its rights in relation to control to any third party.

In setting up any sort of joint venture arrangements regarding a LLP, consideration should be given as to whether or not such arrangements amount to a collective investment scheme. Continued efforts must be taken to ensure that the regulated activity of establishing, operating or winding up an

² Section 235(2) of The Financial Services & Markets Act 2000

unregulated collective investment scheme is not unwittingly carried on without the appropriate FCA authorisation.

Also, as mentioned above, an opportunity to invest in an unregulated collective investment scheme cannot be communicated to communities even with authorisation from a FCA authorised person.

What does this mean for developers?

The key points for developers to consider are:

- if a developer wishes to use a LLP as its SPV, the community organisations must have equal voting power and must actually exercise this.
- the agreement between the developer and the community must be clear in this regard and the actual facts must support this.
- if a developer does not wish to give a community organisation such power, it cannot use a LLP as its project vehicle.

A LLP structure does not have many of the regulatory hurdles to overcome that a private limited company does, so from a regulatory perspective, a LLP is much simpler than a private company limited by shares as you will see later in this guidance.

Private company limited by shares (“Limited Company”)

We now consider another form of legal structure for joint venture arrangements with community organisations. A limited company is another common form of SPV.

Regulation of Limited Companies

Where a developer wishes to use a limited company, there are certain rules relating to non mainstream pooled investments which are relevant³.

The rules require that a FCA authorised person upholds restrictions in terms of non mainstream pooled investments, such that there can be difficulties in communicating these investment opportunities to communities.

How can a limited company avoid the restrictions regarding non mainstream pooled investments?

Assuming that the SPV carries on normal activities for a renewable energy business such as the following:

- lease and/or buy land which it will develop or construct in to either wind or hydro renewable energy schemes;
- enter into contracts with various third parties to supply the turbine, obtain planning consent, construction contracts, connect to the electricity grid etc; and
- all other relevant business activities associated with renewable energy companies.

then it is not expected to fall within the definition of being a non mainstream pooled investment.

Provided the limited company satisfies the above test regarding its normal activities and an FCA authorised person has approved a communication, an investment opportunity to invest in a limited company limited alongside a developer can be communicated to community organisations.

See section headed “Financial Promotion” for further information as regards this.

³ The Unregulated Collective Investment Schemes and Close Substitutes Instrument 2013

What does this mean for developers?

As you will see later in this guidance, a limited company has a number of regulatory issues which developers will need to take cognisance of as regards financial promotion and regulated activities.

Notwithstanding these further regulatory requirements, in the first instance developers will need to ensure that the limited company SPV they are offering the community shares in, carries on normal activities for a renewable energy business as set out above.

If developers however wish to some form of group structure, they must ensure they take separate advice.

4 Financial promotion

These rules do not apply to LLPs, only to limited company project vehicles.

At a relatively early stage in a project, as set out in the Good Practice Principles (the “Principles”), developers are expected to engage with relevant communities including having discussions with communities about the possible opportunity to invest in the project. The manner in which the developer and other supporting agents communicate with the relevant community may constitute a financial promotion which is regulated under FSMA.

The term “financial promotion” is commonly used to describe the communication of an invitation or inducement to engage in investment activity⁴ and a person (i.e. a developer or a supporting agent) may not communicate an invitation or inducement unless:

1. that person is FCA authorised (we do not expect that developers or other supporting agents will be FCA authorised);
2. the communication is approved by someone that is FCA authorised. Developers can approach any FCA authorised person to carry out this task on their behalf; or
3. the communication is covered by an exemption⁵. It is unlikely that the community organisations will fall within any potential relevant exemptions.

In terms of the project, clearly there must, at some stage in the overall process, be some form of “promotion” to the communities of the opportunity to invest and this section 4 is to assist developers and supporting agents as regards their understanding of these complex rules. For example, offers of shares in a private limited company to a community would be caught by these rules however membership of a LLP will not.

The words “invitation” and “inducement” are used above as the financial promotion regime applies to both. The guidance on this issue says that all forms of communication containing a degree of incitement will be covered and any document or other promotion (including verbal discussion) with an element of persuasion or incitement will fall within the rules⁶.

What is an “invitation”?

An “invitation” is the easier of the two words to consider as the communication must directly invite a community to take a step which will result in them engaging in investment activity. There will be some communications that a developer or other supporting agent will have with communities which would fall within this definition.

What is an “inducement”?

An “inducement” is slightly more difficult to be prescriptive about as regards what this could cover. However, the FCA guidance describes an inducement as a link in a chain where the chain is ultimately intended to lead to an agreement to engage in investment activity.

Not all links in a chain will constitute an inducement – only those which are a significant step in persuading or inciting, or seeking to persuade or incite, a community to engage in investment activity will be caught by the rules.

⁴ Section 21 of the Financial Services and Markets Act 2000

⁵ The Financial Services and Markets Act 2000 (Financial Promotion) Order 2005

⁶ Section 21 of the Financial Services and Markets Act 2000

The fact that an inducement takes place at a preliminary stage may not prevent it being a significant step and therefore developers must be mindful of these regulatory restraints when engaging with communities about investment opportunities.

How does this work in practice?

The various stages of engaging with communities are:

Early stage - education

An option for developers at any early stage to ensure that they comply with the Principles as far as possible would be to hold an education seminar/event for a community organisation to educate the community generally about shared ownership, including explaining the different forms this could take including joint venture arrangements. Such an education event may simply involve the provision of generic materials such as the shared ownership flyer available from Local Energy Scotland.

Key points for developers to consider regarding education seminars:

- Any engagement and education seminar held at this point cannot discuss any specific investment and must be general in its nature and only be on an education basis. To do this developers could use the Principles to explain the options to communities, however, they must not enter in to any discussions with any member of the community about any investment in a specific project or have any form of incitement or persuasion within any document;
- At such a seminar, communities should be advised that they must seek advice from a person authorised to give investment advice. A list of potential advisers can be provided by developers but the onus must be on the community to take the next steps and seek independent advice themselves; and
- Communities should also be advised at this stage that there may be a grant of up to £20,000 available to them from Local Energy Scotland to progress these opportunities and they should sign the form of wording set out in Part A of Appendix 2 to this document, and send this to the developer at the time they apply for the grant.

Early stage – community appointment of authorised person

Once the community has appointed a person authorised to give investment advice, the community should then confirm these details to the developer and the authorised person should confirm that they have the requisite permissions required to carry on the regulated activity of advising on investments. (Please see Part B and C of Appendix 2 of this document for suggested wording to be signed by the community and the appointed authorised person in this regard.)

Further stage – financial promotion

At a slightly later stage when a developer wishes to engage with the community about the specific opportunity, it will likely be a financial promotion, as set out above, therefore a FCA authorised person is required to approve the communication.

Developers can find detail of authorised persons on The Financial Services Register (<http://www.fca.org.uk/register>). Appointment of an authorised person will have cost implications for the overall project.

Key points for developers to consider are:

- Part of an authorised person's role is to ensure that any communication is fair, clear and not misleading and meets certain minimum standards⁷. Further rules came in to force in 2014

⁷ Conduct of Business source code

which further restricted the ability of a FCA authorised person to approve a communication⁸ which mean that a FCA authorised person cannot approve any communication unless the community confirms that, in relation to the investment being promoted (i.e. the specific investment with the developer) that they will receive regulated investment advice from an authorised person;

- The requirement to give investment advice is fairly onerous and the standard that the FCA expects in this regard is fairly high. One of the key things for developers to remember is that the firm is acting independently. The person providing investment advice must also consider alternative products for the community to invest in and prepare a comprehensive and fair analysis of other relevant investment products; and
- Other supporting agents should not get involved in communicating any information about investment opportunities to communities. This should all be developer led given that it is their project vehicle.

What does this mean for developers?

Developers must ensure that any preliminary discussions held with communities are educational only and must not contain any form of invitation or inducement. Ultimately, it would fall on the facts of what happened at an event so developers may be better to consider only using the Local Energy Scotland materials at the very initial stage.

When the developer wishes to engage with the community further than merely the educational element as outlined below, they should ensure that they have received the signed wording from the community confirming that they will receive investment advice from an authorised person and in addition, the developer should engage their own FCA authorised person to approve the financial promotion.

⁸ Policy Statement PS1414 – The FCA’s regulatory approach to crowdfunding over the internet, and the promotion of non-readily realisable securities by other media

5 Regulated activities

These rules do not apply to LLPs, only to limited company project vehicles.

In order to carry on certain activities in the UK by way of business, **such person** must be either FCA authorised or exempt⁹. There are a large number of regulated activities. The most relevant for the purposes of the joint venture arrangements envisaged by this note are as follows:

- a) arranging deals in investments; or
- b) advising on investments.

Looking at each of these regulated activities in turn:

a) Arranging deals in investments

This regulated activity comprises two separate limbs:

1. arranging (bringing about) transactions in investments¹⁰; and
2. making arrangements with a view to transactions in investments¹¹.

Arranging transactions in investments

This aspect of arranging deals in investments is narrower in scope than the second. The arrangements must be such that they bring about, or would bring about the relevant transaction. According to the FCA, a person “arranges” if its involvement in the chain of events leading to the transaction is of sufficient importance that, without such involvement, the transaction would not have taken place. This will often be true as regards the majority of developers, as they may initiate a transaction which is concluded with community organisations.

Supporting agents are different in that they may have no direct effect on the transaction taking place, although many of them do play a significant role in the overall project which is sufficiently important. However, they are not able to directly influence a transaction occurring, therefore in the majority of circumstances, supporting agents are not likely to be carrying on item 1.

Making arrangements with a view to transactions in investments

This second aspect is wider in scope and is aimed at ongoing arrangements and those designed to facilitate others entering into transactions. The FCA’s guidance on this point is that it is the intention of the arranger that is important here. Both the developer and the majority of supporting agents will typically be carrying on this regulated activity.

There is an exemption from this regulated activity where a deal is arranged with or through an authorised person¹², which excludes any deal that is entered into on the advice of an authorised person.

⁹ The Financial Services and Markets Act 2000 (Regulated Activities) Order 2001

¹⁰ Article 25(1) of The Financial Services and Markets Act 2000 (Regulated Activities) Order 2001

¹¹ Article 25(2) of The Financial Services and Markets Act 2000 (Regulated Activities) Order 2001

¹² Article 29 of The Financial Services and Markets Act 2000 (Regulated Activities) Order 2001

In the joint venture arrangements set out in this guidance note, community organisations are expected to receive investment advice from an authorised person meaning the developers and other supporting agents could rely on this exemption.

What does this mean for developers?

Developers and other supporting agents should tell community organisations from the outset that they must get investment advice from a person authorised to give investment advice, and they may choose to do so as follows:

- make it clear to community organisations in all literature and at all meetings that they are not providing investment advice. Developers should thereafter ensure that communities obtain such investment advice; or
- including clear statements on their own websites that they are not providing investment advice.

Supporting organisations should not receive any reward or fee or other advantage arising out of them making the arrangements. Developers should also ensure that it is clearly stated on all communications or other literature that developers have made this fact clear to communities.

Developers should not receive any form of payment linked to the actual deal happening e.g. it should not receive a commission payment or the like for the joint venture deal occurring.

b) Advising on investments

This regulated activity consists of advising the community on the merits of becoming involved in the joint venture vehicle¹³.

Developers and other supporting agents should not engage in any form of advice to communities as regards any investment opportunity.

They should all refer community organisations to the appropriate authorised person as set out above. The PERG Guidance relating to advice on investments says that giving a community generic advice (for example, invest in Japan rather than Europe) is allowed as is giving information.

The giving of specific advice (for example, listings or company news) is not permitted.

Developers and supporting agents should be aware that notwithstanding the above, the context in which something is communicated may affect its character and what appears to be a permissible statement may actually be deemed as constituting advice on investments, e.g. if a developer gives information on share price against the background that, when he does so, that will be a good time to purchase, this will constitute advising on investments.

To ensure that a developer or other supporting agent does not inadvertently provide investment advice, it should not engage at all with the communities about the merits of any investment opportunity. This is for the community's appointed authorised person to do.

What does this mean for developers?

Developers should ensure that communities obtain independent investment advice. They should also ensure that it is clear on all communications or other literature that developers have made this clear to communities.

¹³ Article 53 of The Financial Services and Markets Act 2000 (Regulated Activities) Order 2001

6 Glossary

<p>“Exempt”</p>	<p>Means a person who is exempt from the general prohibition under the Financial Services and Markets Act 2000, in respect of the activities it carries on. Exempt persons can therefore carry on regulated activities without authorisation from the Financial Conduct Authority. The glossary to the FCA Handbook sets out the full definition of this term. When considering this term in the context of financial services, reference should be made to the FCA Handbook glossary definition of exempt person.</p>
<p>“FCA”</p>	<p>Means The Financial Conduct Authority</p>
<p>“General Prohibition”</p>	<p>Means the prohibition imposed by section 19 of the The Financial Services & Markets Act 2000 (The general prohibition) which states that no person may carry on a regulated activity in the United Kingdom, or purport to do so, unless he is:</p> <p>(a) an authorised person; or</p> <p>(b) an exempt person.</p>
<p>“Inducement”</p>	<p>Means a link in a chain where the chain is intended to lead ultimately to an agreement to engage in investment activity. But this does not mean that all the links in the chain will be an inducement or that every inducement will be one to engage in investment activity. Only those that are a significant step in persuading or inciting or seeking to persuade or incite a recipient to engage in investment activity will be inducements under section 21. The FCA takes the view that the mere fact that a communication may be made at a preliminary stage does not, itself, prevent that communication from being a significant step.</p>
<p>“Invitation”</p>	<p>Means something which directly invites a person to take a step which will result in his engaging in investment activity. It follows that the invitation must cause the engaging in investment activity.</p>
<p>“Non-mainstream Pooled Investments”</p>	<p>Means pooled investments or ‘funds’ characterised by unusual, speculative or complex assets, product structures, investment strategies and/or terms and features. They are units in unregulated collective investment schemes (UCIS); securities issued by certain special purpose vehicles (SPVs); units in qualified investor schemes (QIS); and traded life policy investments (TLPs). Note that not all pooled investments meet the statutory criteria for a ‘collective investment scheme’; pooled investment special purpose vehicles, notably, do not generally amount to a collective investment scheme.</p>
<p>“PERG Guidance”</p>	<p>Means The Perimeter Guidance Manual</p>
<p>“Regulated Activities”</p>	<p>Means those activities which cannot be carried on without regulation as set out in section 22 of the Financial Services & Markets Act</p>

Appendix 1

Do and Don't...

Do:

Developers	Other supporting agents
<ul style="list-style-type: none"> • Developers should decide at as early a stage as possible what the legal structure of their joint venture vehicle will be as this could impact on the regulatory issue they need to consider; • If legal structure changes, developers need to be mindful of this; • If choosing a LLP, communities must have equal rights and must exercise them; • If choosing a limited company, Developers should engage a FCA authorised person at an early stage to approve any communication going to communities as regards investment opportunities; • Ensure that the risks of any investment are made clear to community organisations from as early a stage as possible and that the wording is in plain English so it is easily understandable by the community. The risks should be as prominent as any rewards; • If choosing a limited company, create a script or form of wording that could be used for the education event to ensure that this does not stray into being a financial promotion. By being clear from the outset with members of staff working for a developer, they should ensure that they do not fall foul of these rules; • Developers should be the one that promotes and/or makes the community aware of any investment opportunity. 	<ul style="list-style-type: none"> • If legal structure changes, supporting agents need to be mindful of this as it could impact on regulatory constraints; • Supporting agents should ensure that they tell communities from the outset that they must get investment advice from a third party authorised to give investment advice. They should tell communities that they are not advising on any investment and all literature, meetings, websites etc should make clear reference to that. It is better to say it as many times as possible; • If supporting agents are at any meetings where they believe a financial promotion is taking place which is not regulatory compliant, they should decline to discuss these opportunities and they should make it clear why they are taking this stance; • Supporting agents should assist developers by making it clear to communities that the developer is under certain regulatory constraints and is unable to discuss certain points about the deal to ensure that expectations of communities are managed.

Don't:

Developers	Other supporting agents
<ul style="list-style-type: none"> • If using a LLP, communities cannot have any less rights than developer; • If choosing a limited company, developers should not have any discussions or provide communities with any literature about investment opportunities without it being approved by a FCA authorised person; • Avoid using any language which may be seen as trying to persuade the community to invest eg. refrain from discussing the pro's of any investment or the benefits that a community could gain by becoming a joint venture partner; and • Developers should not provide a community with any literature or other information about an investment opportunity without the community having confirmed that they will receive authorised investment advice. 	<ul style="list-style-type: none"> • Developers are to lead on joint venture arrangements and provide all information to communities about these opportunities (except for the Local Energy Scotland leaflet). Supporting agents should not be involved in this process and should not distribute any promotional material to communities; • Avoid using any language which may be seen as trying to persuade the community to invest e.g. refrain from discussing the pro's of any investment or the benefits that a community could gain by becoming a joint venture partner; and • If choosing a limited company, supporting agents should not receive a reward, fee or any other advantage from arranging the deal.

Appendix 2

Part A

We [insert name of community organisation] confirm that in relation to the investment being promoted by [insert name of Developer], we shall receive regulated investment advice from an authorised person.

.....
Signed for and on behalf of
[insert name of community organisation]

Part B

We [insert name of community organisation] confirm that we have appointed [insert name of authorised person], being an authorised person to provide [insert name of community organisation] with regulated investment advice as regards the investment being promoted by [insert name of Developer].

.....
Signed for and on behalf of
[insert name of community organisation]

Part C

[TO BE TYPED ON HEADED PAPER OF AUTHORISED PERSON]

We [insert name of authorised person] confirm that we are authorised to provide regulated investment advice as regards shares which is the investment being promoted by [insert name of Developer]. We confirm that we have been appointed to provide [insert name of community organisation] with regulated investment advice as regards the investment being promoted by [insert name of Developer]. We enclose our Scope of Permission Notice.