# ‘This may become one of the few Ponzi schemes where victims get most of their money back’

Failed fractional ownership schemes present considerable challenges for IPs. **Stephen Hunt** and **Matthew Brown** share their experiences of the Qualia Group

**MB:** In 2020, the Qualia Group owned 13 care homes, with contracts in place to acquire two more, when the Care Quality Commission launched an investigation into the group’s funding model. The investigation resulted in the CQC refusing to agree the registration of new homes and prohibiting the acquisition of new homes. A cash flow crisis followed, and administrators were urgently appointed. More than £53 million had been taken from investors worldwide for the 793 rooms in the care homes. Investors were promised annual returns of 8–10% and a repayment of 100–115% per cent of their initial investment after five years.

> **There were few controls in place, with undisclosed HMRC debts exceeding £1 million. Most of the available cash had been used to pay Mr Forster’s personal defence costs in the FCA claim**

A month after their appointment, the administrators agreed a sale of the care homes’ freeholds to a newco group controlled by Robin Forster, who ran Qualia Care Developments and Qualia Care Properties before both companies entered administration. The plan was for the newco group to continue making payments to investors and gradually recover the losses incurred by the insolvent companies over time.

However, the sale to Mr Forster raised concerns among investors, prompting them to appoint Stephen as joint administrator to investigate the transaction.

**SH:** I accepted the appointment as joint administrator with a limited remit. As it turned out, it was not long before the administration ended, and I became the sole liquidator. The assignment progressed from an investigation into a disputed sale to working with creditors to reverse it.

**MB:** The FCA issued proceedings against Mr Forster[1] and found that he was operating an unregulated collective investment scheme (UCIS). The instalments promised to investors under the sale agreement had ceased and action needed to be taken.

In August 2022, Stephen took control of the newco group and its operator, though the battle for control of the operator through a creditor administration application was fiercely contested. The operator submitted evidence from another IP arguing that administration was not appropriate, along with accounting evidence claiming that the operator was viable and solvent. Just days before the hearing, all directors offered to resign and assign their shares, ensuring the operator would come under Stephen’s control. The offer was accepted.

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**SH:** It became apparent within two weeks of my instructing Healthcare Management

### Fractional ownership schemes

The SRA and others have long flagged the potential problems inherent in fractional ownership schemes. See, for example, the 2020 Warning Report[2], which links to a thematic review.

Under a fractional ownership scheme, a promotor raises money by selling long leases of rooms within a care home, hotel, student accommodation or any property that can be split into fractional interests. The investments might be used to finance the purchase or redevelopment of the site. Rent will be a peppercorn or similar.

At the same time, a sublease is granted by the investor back to the promotor. Rent is usually 8–12% of the capital sum paid per annum. This is the investor’s ‘guaranteed’ annual return.

The promotor and investor often enter into options so that after a few years the investor can require the promotor to buy back the leases, and the promotor can do likewise. The premium is often 110% or 115% of the capital paid.

Finally, the promotor (as a tenant under the sublease) enters into an operating agreement for the room with an operator. Income then flows back up the structure to the investor.

Examples of failed fractional ownership schemes include the Qualia scheme (£53m invested)[3], Park First airport parking scheme (£230m invested)[4], Carlauren (£75 million invested)[5] and Northern Powerhouse Developments (£80 million invested)[6].

### Collective investment schemes

Depending on their structure, a fractional ownership scheme can be a collective investment scheme (CIS). Typically, this happens where profits are pooled to pay investors. A CIS is defined by s235 of the Financial Services and Markets Act 2000 (FSMA) and is a regulated activity in the UK. Section 19 of the FSMA prohibits the promotion, establishment or operation of a CIS by any person who is unauthorised or exempt from authorisation. Section 382 of the Act allows the court, on the application of the FCA, to make restitution orders against those concerned.

*Stephen Hunt and Matthew Brown*

Solutions (HCMS), an experienced CQC-approved operator, to take over the head office functions and that the business was insolvent. There were few controls in place, with undisclosed HMRC debts exceeding £1 million. Most of the available cash had been used to pay Mr Forster's personal defence costs in the FCA claim. It was clear that the business had been a Ponzi scheme, but I established that a trading administration could be viable. I moved the operator into administration so that trade could continue.

Initial forecasts indicated losses for a few months before the business would turn a profit and achieve positive cash flow. My trading plan streamlined operations by eliminating head office functions, closing one care home and negotiating higher residential fees. The key obstacles to success were no indemnity for losses, a lack of suitable assets to secure borrowing for working capital, rising heating bills because of the Ukraine war and very limited cash reserves. I approached another IP to act as a potential conflict joint administrator, and he turned me down.

We engaged with local authorities, recognising that the care homes housed over 600 residents and employed a similar number of staff. The loss of any care home would be disastrous for both residents and their families while putting additional pressure on local services. Adopting a proactive approach to negotiations, we determined that preserving services at break-even levels would justify keeping some care homes open. The local authorities responded positively, offering contracts on better terms. By eliminating losses, the more profitable care homes could support the overall business, which provided the platform for a potential rescue.

**MB:** While Stephen concentrated on managing the business, I developed an exit strategy centred around the support of investors. The majority of the Qualia Group's investors held 125-year leases in the company's care home rooms, and many had been badly burned by other fractional investment scams. They were supportive of Stephen's actions but understandably protective of their own property interests.

**SH:** By Christmas 2022, we had completed three months of trading but the losses were greater than anticipated, with the short-term forecast indicating we would run out of money by the end of February 2023. With no access to capital, we had few options. I sought advice from an experienced IP at another firm about deferring the monthly PAYE payments for the spring, which would allow us to build up capital. He advised me on how to approach the conversation and I subsequently wrote to HMRC to explain my decision. The strategy worked, and we eventually became cash-positive.

> **"The portfolio, once valued at £7 million under the best-case scenario, is now likely to sell for over £25 million for the benefit of investors, HMRC and trade creditors"**

**MB:** Our objective was to sell the freeholds for maximum value and distribute the proceeds to investors, less agreed costs. The problem was that the freeholds were essentially worthless with the leases in place. Without any leases, the freeholds would have significant value, which could be returned

Test solution: the loss-making St Mary's home was used as a trial for the proposals, with an original valuation of £1.3 million

Barrier to realisations: the freeholds were essentially worthless with the investors' leases in place

> **Following the hearing, 45 investors voluntarily surrendered their leases and the court executed three more**

to investors as a consequence of their giving up their leases. The question was, if we explained the situation, would the support of the majority persuade the minority?

We explored the provisions of the Financial Services and Markets Act 2000 (FSMA), which might allow the unwinding of the UCIS upon repayment of the amount invested. Given the business's insolvency, this was not feasible, but we became confident that a workaround was possible. We engaged Ruth Bala, an experienced FSMA specialist counsel, to advise on the technical solution and also instructed Eleanor Temple KC.

We consulted creditors about our proposed solution, which received a cautious response. Undeterred, we pressed ahead with a plan to test the solution on a single loss-making home, called St Mary's. We obtained a valuation of £1.3 million for the property, assuming it was sold as a going concern and free of the leases, and we sent a proposal to the St Mary's investors. We then held a 'town hall' meeting to answer their questions.

**SH:** The investors at the 'town hall' were not hostile but they also were not enthusiastic. However, there was enough support to proceed with the application. I instructed Peter Fenwick and Colliers to begin marketing St Mary's ahead of the application. At the same time, my team worked hard to locate and speak with all the investors, which was especially challenging for investors in different jurisdictions, to explain our proposal. By the final hearing, all 58 investors were involved, with all but two supporting the proposals. None were against.

**MB:** The court process was complex, but we ultimately obtained the orders sought. Following the hearing, 45 investors voluntarily surrendered their leases and the court executed three more. This enabled St Mary's to be sold for £2.275 million – nearly £1 million more than expected. The net proceeds were quickly distributed to investors.

**SH:** At the time of writing, we have made proposals to investors for all remaining trading care homes. The responses have been overwhelmingly in favour, with no votes against. The portfolio, once valued at £7 million under the best-case scenario, is now likely to sell for over £25 million for the benefit of investors, HMRC and trade creditors. Thanks to HCMS and care home staff, all care homes are now rated 'good' by the CQC, which has significantly increased the value of the freeholds. The operator is now generating over £1 million in profit. HMRC will receive about £10 million in tax from the administration trading period in addition to the full repayment of their £1.3 million preferential claim. Valuable local services have been rescued and jobs have been saved.

**MB:** We are hopeful that with the overwhelming support of investors and further court applications, we will realise the full value in the remaining homes. If achieved, this may become one of the few Ponzi schemes where victims get the majority of their money back, and it is largely because of the support and dedication of a huge number of stakeholders, not all of whom have been mentioned in this article, and by building trust with investors over time.

The problem with failed fractional ownership schemes has been evident for years. Could the rescue of Qualia Group offer a solution to failed schemes where property interests have been granted? We think so, but only if those involved recognise that the economic interest in the properties is with the investors and not with the freehold-owning companies that insolvency practitioners are appointed over. Of course, most importantly, the solution must be heavily supported by the investors themselves.

1 *The FCA v. Robin Scott Forster and others [2023] EWHC 1973 (Ch)*

2 www.sra.org.uk/solicitors/guidance/investment-schemes-including-conveyancing

3 www.fca.org.uk/news/press-releases/financial-watchdog-wins-civil-case-against ponzi-like-care-home-investment-scheme #:~:text=The%20High%20Court%20has%20 ruled,to%20pay%20back%20to%20investors

4 www.fca.org.uk/news/news-stories/park-first-limited-information-investors

5 www.gov.uk/sfo-cases/carlauren-group

6 www.gov.uk/sfo-cases/northern-powerhouse-development group-and-mbi-group

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