PRIVATE EYE

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In the City

Your money or your life

GUERNSEY'S already scandal-soiled reputation for regulation looks set to take another beating over yet one more regulatory failure – this time regarding EEA Life Settlements Fund, which sold investments in life insurance policies acquired from ageing and/or seriously ill Americans.

The traded life insurance investment model relies on the policyholder dying before the fund has paid too many premiums, enabling it to make a quick profit on a death benefit higher than the price of purchasing the policy. Ethical investment it is not, as it is a bet on when a policyholder dies!

Some 4,000 individual and institutional investors are estimated to have $800m locked up in the Guernsey-based and run EEA Life Settlements Fund, invested between 2006 and late 2011, when sales and redemptions were suspended. Redemptions resumed last year after a restructuring approved by the Guernsey Financial Services Commission (GFSC). The total number of individual investors, via insurance companies and other investment platforms, as distinct from shareholders could be as high as 20,000.

The 2011 suspension followed a warning from the UK regulator, the FSA, that investments in traded life insurance policies were "high-risk, toxic products" and not suitable for retail investors. No such warning had come from EEA's regulator, the GFSC, or the then Channel Islands Stock Exchange (now rebranded the Channel Islands Securities Exchange), on which fund units were listed. The sale of such investments to retail investors was later banned by the FSA last year.

The EEA fund was suspended within two days of the FSA's warning – due, it is suspected, to a wave of redemption requests. Subsequently auditor Ernst & Young resigned in 2013 after raising concerns that the life insurance policy portfolio was overvalued by $100m. Custodian BNP Paribas has indicated it wishes to resign but cannot without a replacement.

The FSA's successor, the FCA, last September advised UK retail investors in the EEA fund to consider complaining and seeking compensation against their advisers, via the Financial Ombudsman Service and the Financial Services Compensation Scheme, for mis-selling. Three months ago it was announced that the policy portfolio was to be revalued on a different basis. Last week it was disclosed that the net asset value had fallen from $862m in August 2014 to $602m, including cash of $128m. In 2012 that net asset value number was just over $1bn.

Next month should see a cash repayment to those fund investors who opted to switch into run-off shares as part of the restructuring. However, a similar expected distribution in December was not made. Some $14m was previously distributed last June. A smaller $4m payment has also been made to some of those holding the alternative continuation shares. If that June payment is not made, pressure will increase on the GFSC.

The latest figures suggest investors could face a major loss, even though the remaining life policies have a face value of $1.1bn. However, there is scepticism about these valuations, as well as about the quality of some of the remaining high value policies. Other traded life insurance funds have been hit by phoney policies where the policyholders were not as ill as they made out, meaning payout could be long delayed or never made.

Benefits from the life policies that paid out in the year to March were $122m, against an expected $201m. So maybe the dead policyholders are having the last laugh on those who sought to profit from their early demise.

The 2011 FSA warning was inevitable, given the losses suffered by investors in Keydata, largely as a result of the fraud organised by the missing (and believed dead) David Elias. Keydata was shut down in 2009.

Eye 1257 detailed back in 2010 the dangers inherent in the "death bonds" business already exposed by US regulators. Soon afterwards the FSA quietly started closing down those peddling investment in traded life policies.

The fund continued to be listed by the CISX and managed from Guernsey, watched over by the GFSC. The fund units were only delisted last year. The new CISE refused to relist them after the restructuring.

The EEA fund managers are FCA-authorised and the marketing of the EEA fund was handled by FSA/FCA-registered individuals and independent financial advisers. Not surprisingly, some 500 EEA investors are considering legal action against the FCA.

But surely that fire would be better concentrated on Guernsey and the failed fund regulators there? The EEA Investors Group has had meetings and conversations with the GFSC, but these have so far produced no satisfactory response other than that it is aware of the problem.

The problem with EEA Life Settlements is that it may face a cash crisis, with no more new money from investors coming in and only maturities to fund future premiums, along with dwindling cash reserves. But with the 400 remaining policyholders living longer, premiums are costing more and payouts on death are therefore less than projected. A perfect actuarial storm, and far from the low-risk, 8-10 percent-a-year return that was projected back in the day.

EEA Life Settlements is part of the EEA investment group run by stockbroker and fund manager Simon Shaw – previously also involved with carbon credits and assorted clean energy funds. Another of his less successful ventures was Sun Biofuels, which was looking to produce oil from jatropha seeds in Tanzania and Mozambique. It ran out of money before a crop was produced and collapsed in 2011 with a deficit for creditors of £12m. Shaw was a director.

The Sun Biofuels shares were held by the AIM-listed renewable energy investment fund Trading Emissions (investment advisor Simon Shaw). Loss-making Trading Emissions' shares have fallen heavily since 2008 and the fund is to be wound down.

Shaw is now the sole shareholder of EEA Holdings, renamed Melquart, which owns the FCA-regulated EEA fund managers and marketed the life settlements fund. Shaw was paid dividends of £2m for 2013.

EEA investors have been lobbying since last October for the GFSC to either appoint an administrator or liquidator and/or investigate, alleging that the fund has been "mismanaged and misrepresented" – something EEA rejects. "We urgently need to know how much money we will get back and over what period," the EEA Investors Group told the GFSC.

This is not something that bothered the policyholders who sold the anticipated future payout for cash now, leaving EEA to pay the premiums and hope they died sooner rather than later. What a way to make money! One more reason the GFSC should have been all over EEA Life Settlements fund from the start.