

## PRELIMINARY ASSESSMENT OF EEA LIFE SETTLEMENT FUND RESTRUCTURING PROPOSALS

### 1. The Proposals are Unfair to Some Shareholders

Under the current rules, all shareholders in a cell have equal rights to their proportion of the proceeds of the Fund, and enjoy the same (UK) tax status on redemptions (i.e. capital gains rather than income). Under the Restructuring Proposals the “Continuing Shares” remain unaffected (apart from a 23-month lock-up period) while “Run-off Shares” incur an immediate liability to a capital gains / loss disposal and ongoing taxation as income on any future returns. Given the disagreements and uncertainty over the NAV calculation (at the Effective Date) it is not clear how these transactions will be valued and the net financial impact for the “Run-off” shareholders. There also appears to be no provision for a “Run-off” shareholder to transfer his or her shares (e.g. to a spouse) before the deemed disposal in order to mitigate the capital gains liability. The shareholder will have to fund any capital gains tax charge from other sources – the Fund should allow for a “Special Redemption” to cover this exposure. Many investors in the current Fund were specifically attracted by the capital gains (rather than income) nature of the investment and this change in tax status could have serious medium and longer term impacts. A shareholder “forced” to choose “Continuing Shares” to avoid this change would then have to incur the 23-month lock-up period and other risks associated with the Continuing option.

### 2. The Proposals are Unnecessary and Unduly Complicated

The inherent purpose of the Directors’ proposals is to manage the run-off of the existing life policies for the maximum financial benefit of all shareholders and to enable shareholders to choose when / how to redeem some or all of their holding in a managed way and/or continue all or part of their investment in an ongoing purchase of additional policies, for which purpose they have created a “New Fund” based in Ireland and propose creating a new class of “Continuing Share” to invest in the New Fund (and other permitted investments). The proposal documents contain a lot of information about the New Fund but this is not really relevant to the operation of the existing Fund. Since the Fund is also proposing to make and manage investment decisions into the New Fund and/or other investments for the “Continuing” shares then these infer additional rules and expenses for the Fund as a whole.

The same purposes could be more simply achieved under the current Fund rules by the Directors maintaining the suspension of new investment in the Fund and managing the run-off of the existing policies (by maturity and/or sale as necessary) and make compulsory redemption payments to shareholders once or twice a year as the available cash flow allows. Shareholders can then simply choose what to do with their proceeds (including to invest them directly in the New Fund, which would be able to offer a streamlined and/or discounted purchase process for such investors if it chose to do so, at its own expense). This wouldn’t require any changes to the existing Fund documents, share listings or taxation arrangements for the shareholders concerned. It would also NOT be so dependent on the accurate calculation of the NAV for redemption purposes since the eventual returns would be based on the actual cash flow over the run-off period.

The same objectives could also be achieved by a similar process under a “managed” winding up of the Fund, also allowed under the current Fund rules at the Directors’ discretion.

### 3. The Proposals are Additionally Unfair to Meteor SLS Shareholders

Investors in the Meteor Senior Life Settlement Cell have been able to choose optional (automatic) monthly redemptions (capital gains UK taxation basis) up to the equivalent of the 8% pa minimum increase in NAV assured by the Fund. Although these redemptions have been suspended since November 2011, there is nothing in the Restructuring Proposals to cover this option, or adapt it to the new quarterly redemption rules for “Continuing” shareholders. Meteor shareholders who need this stream of redemption “income” therefore have to choose “Run-off Shares” for a six-monthly (maybe) redemption stream, therefore incurring the associated taxation changes or foregoing any of the benefits of “Continuing” shares. Adopting the simpler process described under (2) above would enable all shareholders to fairly receive a series of regular redemption payments which they can then retain (for other purposes) or reinvest into the New Fund.

### 4. There Are No Financial Statements or Agreed NAV policy to use as a basis for implementing the Proposals

Although the Directors acted promptly (and necessarily) in suspending the Fund following the FSA announcements in November 2011, they subsequently failed to publish Annual Reports (or Financial Statements) within the six-month periods required under Guernsey law. They have also failed to provide the Interim Reports required under the Fund rules.

The Dec 2011 Annual Report which was eventually published in June 2013 carefully avoided the fact that the Auditors and Directors had been unable to agree on the valuation method used to calculate the NAV but the Auditors (Ernst and Young) have recently resigned, citing their disagreements over the calculation of NAV for the Dec 2011 accounts. The new auditors (Grant Thornton) have not yet had the opportunity to consider their opinion on the accounts or method of calculating NAV, and the Directors have not made any information available to shareholders of the current cash / cashflow position of the Fund, the projected cashflow of the remaining policies or an agreed method of calculating the NAV. The EEA website disclaimer still states that the NAV figures can't be used for any purpose.

The shareholder vote on the proposed restructuring is therefore taking place without any factual knowledge of the state of the Funds finances or any agreed basis for calculating the NAV or the future cashflow for the Fund, or its new “Continuing” and “Run-off” shares. It will therefore not be possible to establish a proper NAV for calculating tax liabilities (for capital gain / loss purposes) or the new share prices at the Effective Date, and on past experience this might take another year or two to resolve. Since 2012 was the first year in which the Fund had no new investment income, it is also not possible for shareholders to know whether previous increases in NAV to meet the 8-10% pa performance targets was masked by the inflow of new investment funds

It is difficult (in the absence of approved documentation) to escape a conclusion that the past (and current provisional) NAVs might have been exaggerated or possibly manipulated by the Directors in order to support the marketing of the Fund to new investors or limit requests for redemption (until the FSA announcements upset the appcart). It might therefore follow that the Restructuring Proposals have also been formulated as a further method of disguising the underlying under-performance of the fund and rolling the whole scheme over into a New Fund without the true financial situation coming to light for a few more years. The New Fund Prospectus is promising the same 8% pa minimum return rate target as the current Fund but there

is no evidence to show that this was actually sustainable under the old Fund or with the revised assumptions about future operations and life expectancy assumptions.

To a large extent therefore the Restructuring Proposals are a “Pig in a Poke” and inferior to a simple run-off of the existing Fund as described under (2) above.

#### **5. The Proposals Unnecessarily Jeopardise the Taxation Basis and Listed Share Basis for Some Shareholders**

This has largely been covered under (1) above. The present shares are listed (but suspended) on the Channel Island Stock Exchange and the Fund is treated as a “Reporting Fund” by the UK HMRC. Under the Restructuring Proposals the existing shares would be delisted (immediately) without any assurance that the new shares would be accepted for listing. The Proposals state that Run-off Shares would NOT be accepted as a Reporting Fund by HMRC (changing the status of any proceeds from capital gain to income). There is also no assurance that the Continuing Shares would be accepted as a Reporting Fund by HMRC.

These risks and potential consequences need not apply under the simpler run-down plan described in (2) above.

#### **6. The Board is Using the “threat” of Liquidation as an Alternative to The Proposals**

The EEA (and Meteor) documents for the voting on the Restructuring Proposals state that the likely outcome of shareholders NOT approving the Resolutions by the requisite quorum / majorities would (probably) result in a decision by the Directors to appoint a liquidator, implying that this might be a more expensive and less fruitful solution than the Restructuring Proposals. This view is not substantiated by any further information and evidence and appears to be simple scaremongering. The assets of the existing Fund are the current cash balances plus the future stream of premium payments and maturity receipts from the remaining life policies. Simply running these down (by maturity and/or sale) for the maximum financial benefit of the Fund over time is the same process and result whether carried out by the Directors or a liquidator. In either case, the Fund would not be bearing any costs of managing new investments or subscriptions or the associated advisory and certain other fees / charges. A liquidator shouldn't cost more than a similar number of Directors and support staff, and wouldn't need an Independent auditor. There would be full transparency for the shareholders (and any other creditors), and the whole process would be under the supervision of the appropriate Regulator and Court in Guernsey.

#### **7. The Performance of the Current Board in Developing and Managing the Suspension and These Proposals Has Been Inadequate.**

In addition to the inadequate financial reporting described in (4) above, the Directors have also failed to share any information or consult with shareholders (or Meteor) during the development of the Restructuring Proposals and have now sprung them on the shareholders with minimum notice and a collection of draft documents. There appears to be no opportunity to submit amendments or alternative resolutions to the Class Meeting or EGM and the Directors will not have “final” documents available until the meetings. The Directors have also neglected to properly understand or explain the Guernsey Regulatory process related to the Restructuring Proposals and the need to firstly publish overdue accounts and to obtain shareholder approval before submitting the proposals for Regulatory approval. This has either added unnecessary delay to the whole process or has just been a series of tactics to delay

the process while the Fund continues to run under suspension. It raises questions as to whether the current Directors are suitable to manage the running down of the existing fund for the maximum benefit of all shareholders, and to manage the proposed Continuing Shares and New Fund on a more transparent and competent basis

## 8. Risk / Return Factors

Strangely, the list of Risk Factors in the draft offering documents does NOT include the risk of suspension of the Funds due to adverse announcements and publicity by significant Regulators (e.g. the UK FSA) or media commentators, regardless of whether these announcements are reasonable or not. Once bitten should be twice shy ...

Investors must also be alert to the current real risk of a serious devaluation or collapse in confidence for the US dollar v/v other currencies and commodities. The current and proposed Funds are both based on the US markets and currency and are therefore at increased risk at this time, especially now that the Fund is unhedged and likely to remain so for the near future. Since the Fund returns of 8-10% pa now appear to have been overstated (or artificially achieved) and higher risk now appears to be in place then investors should now be considering an accelerated redemption of their investment regardless of what has occurred with the Fund since November 2011. Within this context, investors should choose an option that leads to earlier (and safer) redemption rather than later (and riskier).

## 9. Conclusions

The Proposed Restructuring appears to be unduly complex and unnecessary and will result in significant extra risks and / or taxation disadvantages for various shareholders.

The performance of the Directors in communicating the ongoing financial position of the Fund and the development of the proposals has been woefully inadequate and their competence to manage the ongoing affairs of the Fund under any scenario must be in question.

The short notice, nature and content of the proposed meetings and resolutions is disappointing and smacks of trying to railroad shareholders into the only proposals that the Directors appear to have considered. They seem to be more focussed on ensuring an ongoing market for their New Fund than necessarily serving the best interests of existing shareholders in the simplest and most effective way.

The additional risks that these investments still carry the "toxic" label so firmly implanted by the FSA announcement, plus the additional risks of exposure to a weak (and devaluing) US Dollar (unhedged), together with questions around the quality and sustainability of the 8-10% growth targets suggests that a path towards earlier and faster redemption of the current investment is the better and more flexible way to go.

The Proposals should be rejected by shareholders and an alternative approach to winding down the existing fund (as soon as possible) by the Directors or a liquidator under current Fund rules should be adopted. The New Fund will still be available for any shareholder that wishes to continue investing in a Life Settlements Fund run by the Directors under similar terms to the current Fund (but clearly separated from it).