FINANCIAL CONDUCT AUTHORITY

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FINAL NOTICE

To: **Link Fund Solutions Limited**

FRN: 119197

Address: 6th Floor
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Date: 11 April 2024

1. ACTION

1.1. For the reasons given in this Final Notice, the Authority hereby requires Link Fund Solutions Limited ("Link") to pay, pursuant to section 384(1) of the Act, restitution of £298,403,919, or such lower sum as may be payable under a scheme of arrangement, to the LF Woodford Equity Income Fund ("WEIF") for the benefit of current unitholders ("Relevant Investors"). This sum reflects losses suffered by Relevant Investors as a result of contraventions by Link of Principle 2 and Principle 6 of the Principles for Businesses.

1.2. The Authority considers that, in addition, these contraventions would merit the imposition of a significant financial penalty. Had it not been for the matters outlined below, the Authority would have proposed to impose on Link, pursuant to section 206 of the Act, a financial penalty of £50,000,000 (which, in the event of settlement, could have been reduced to £35,000,000). Link has not agreed to the level of financial penalty and could have contested the amount proposed by the Authority.

1.3. Link agreed to settle the case by implementing a scheme of arrangement, under which restitution will be payable ("the Scheme"). The Scheme, which has been subject to a court-approved process including a vote by Relevant Investors, will involve the disposal by Link of substantially all of its value and, because it includes an additional significant voluntary contribution from Link's ultimate parent, Link Administration Holdings Limited ("LAHL"), will result in the payment of restitution of up to £230 million, significantly above what would otherwise be available to Link. The Authority is satisfied that the additional imposition of a financial penalty would reduce the amount of restitution available to be paid by Link. As a result, instead of imposing a financial penalty, the Authority hereby publishes a statement of Link's misconduct, pursuant to section 205 of the Act, in the form of a Final Notice.

2. SUMMARY OF REASONS

2.1. The Authority considers that Link failed to act with due skill, care and diligence in carrying out its role as Authorised Corporate Director ("ACD") of the WEIF, and thereby breached Principle 2 and Principle 6 of the Authority's Principles for Businesses.

2.2. The WEIF is an open-ended undertaking for collective investment in transferable securities ("UCITS") fund authorised by the Authority. As a UCITS fund, the WEIF was subject to a detailed regulatory framework designed to offer protection to unitholders. Investors should be able to have confidence that the UCITS they invest in will be managed in accordance with the regulatory framework. That is particularly important where funds are marketed at a range of investors, including consumers who are investing for themselves and are often heavily reliant upon those funds being managed in an appropriate way. The WEIF attracted a range of investors including consumers, as well as professional investors. The WEIF held a substantial sum of investments at the time of its suspension, with a value of just over £3.5 billion at the time.

2.3. For funds where investors expect to be able to withdraw their investments at short notice, it is particularly important that liquidity is appropriately managed to ensure that this can occur. Although there are a range of ways in which liquidity can be monitored and managed, the practices adopted must, at all times, be appropriate to the fund. In particular, investors are entitled to expect that ACDs will diligently manage liquidity to ensure that:

(a) Redemptions can be serviced in accordance with the redemption policy applicable to the relevant fund;

(b) Unitholders will be treated equally, and in particular that unitholders should not be subject to disadvantage for remaining in the fund should other unitholders redeem; and

(c) There is a prudent spread of risk in the fund.

2.4. Link was the ACD of the WEIF from the fund's inception in May 2014. However, over the period from 31 July 2018 until the WEIF was suspended on 3 June 2019, Link failed to comply with its regulatory obligations as ACD in respect of liquidity. In particular:

(a) The WEIF's liquidity profile was unreasonable and inappropriate in light of the redemption policy in the fund prospectus which allowed investors to redeem their investment within 4 days. However, Link failed to take adequate steps to deal with the problem.

(b) The metrics used to measure liquidity contemporaneously (including stress-testing) were unreasonable and inappropriate.

(c) Link failed to properly supervise Woodford Investment Management Limited ("WIM"), the investment manager of the WEIF.

(d) The WEIF held securities which were originally unquoted but later admitted to eligible markets. However, there were no arm's length market dealings in any of Sabina Estates Limited, Ombu Group, Industrial Heat, LLC and Benevolent AI (the "TISE securities"), and only one trade recorded for any of the TISE securities. The securities were valued by Link using fair value pricing ("FVP") at all stages, even after their listing. The WEIF thus held assets which remained illiquid even after listing and this increased the risks of liquidity issues arising.

2.5. Following a request from Kent County Council ("KCC") to redeem its holding in full a decision was taken on 3 June 2019 by Link to suspend dealings in the fund. KCC was, at the time the largest single investor in the WEIF. The WEIF was subsequently put into liquidation without reopening, meaning that investors' holdings in the fund could not be redeemed. Since being suspended, the value of many of the assets held within the WEIF has reduced significantly, meaning that investors have received, or will receive, significantly less than the value of their investments at the point of suspension. The Authority considers that Link's failings: (a) materially contributed to the risk that suspension would be required; and (b) placed those investors who did not redeem prior to the point of suspension at a disadvantage. The 'first mover advantage' for those redeeming earlier was exacerbated by the failure of Link to adequately monitor how redemptions were being met by WIM and to help prevent further deterioration of liquidity. More liquid assets were sold to meet redemptions exacerbating the decline in liquidity. Link could have managed liquidity issues which arose in a number of ways, including requiring assets to be sold down equally across the liquidity profile, referred to as vertical slicing. This would have prevented a disproportionate sale of the most liquid assets. Had vertical slicing been required by Link, the WEIF's liquidity would not have deteriorated in the manner in which it did.

The WEIF's liquidity profile was unreasonable and inappropriate

2.6. The unreasonable and inappropriate liquidity profile of the WEIF permitted by Link is illustrated by the following facts and matters:

(a) Link set thresholds which would trigger action if liquidity deteriorated below what they had defined as an acceptable level. Had Link adopted reasonable and appropriate monitoring metrics (which it failed to do), some of its own triggers would have been breached in April and May 2018, and continuously from July 2018 at the very latest.

(b) Even on Link's own contemporary calculations, it was or ought to have been clear that the liquidity of the WEIF was deteriorating. Indeed, from as early as 20 November 2017, it was noted internally in Link that *"we need to now acknowledge that Woodford is in need of better management of its liquidity"*. Based on assessments conducted, had Link adopted reasonable and appropriate monitoring metrics (which it failed to do), its trigger threshold for the WEIF's most illiquid assets would have been breached in April and

May 2018 and then continuously from July 2018. By 1 September 2018 Link was referring in communications to WIM to *"the need to improve the overall liquidity profile of the fund"*.

(c) Other liquidity metrics which were not contemporaneously applied, but which the Authority has calculated as a cross-check, also show that the liquidity of the WEIF was deteriorating and imprudent.

(d) Based on assessments conducted, from 1 September 2018 onwards the WEIF would not have been able to continue to meet redemptions in stressed but plausible scenarios.

(e) The WEIF was an outlier among comparator funds. From mid-2018 until its suspension, it was less liquid than the least liquid such comparable fund in a number of respects. By way of example, from July 2018 to the time of suspension on 3 June 2019, the proportion of the WEIF's securities that were liquidable within 7 days deteriorated from 18% to 8%, which was significantly lower than the bottom ranked fund.

2.7. Despite the above, and as summarised below, Link did not take reasonable steps to adequately supervise WIM and ensure that a reasonable and appropriate liquidity framework was adopted.

Link's metrics and methodologies used to measure liquidity were unreasonable and inappropriate

2.8. In particular:

(a) Link assumed a participation rate of 100% when applying certain of its liquidity metrics. A 100% participation rate assumes that the entire volume of a security which was traded on a given day could be sold without affecting the price of that security. Link asserted that this optimistic assumption was offset by the requirement for all of the holding in that security to be sold before it could be included in the relevant liquidity time period. However, this was not the case in practice and the use of a 100% participation rate was unrealistically optimistic and it led to an unjustifiably positive assessment of the WEIF's liquidity. Had a more reasonable and appropriate participation rate been adopted, actions would have been triggered under Link's own liquidity thresholds.

(b) The liquidity thresholds were inappropriate in light of the redemption policy and metrics adopted. They were set in such a way that action would only be required when it was already too late.

(c) Link derived the data with which it calculated the WEIF's liquidity from inappropriate data sources. In particular, the data which it used reflected the total volume of shares advertised (and not necessarily traded) on one specific exchange, and not (as should have been the case) the total volume of shares traded across all exchanges on which the security is quoted.

(d) Link did not adequately stress-test the WEIF. In particular, it did not test for certain extreme but plausible scenarios. Had Link done so, it would have realised that the WEIF lacked the liquidity to withstand such scenarios.

2.9. Link's failure properly to measure the liquidity of the WEIF exposed investors to unnecessary risk and led to a difference in treatment between those investors that redeemed their unitholding and those who remained in the WEIF after November 2018. Had Link properly calculated the liquidity in the WEIF, the true scale of the liquidity problem summarised above would have been known (not least because thresholds would have been crossed). Further, had appropriate thresholds been adopted, action in relation to liquidity would have been triggered earlier. Because neither happened, the WEIF's liquidity was allowed to deteriorate, thereby materially contributing to the risk that suspension would be required and placing investors who did not redeem prior to the point of suspension at a disadvantage.

Link's failure to properly to supervise WIM

2.10. Link communicated to WIM as early as November 2017 that the WEIF's liquidity profile was becoming unbalanced and that action needed to be taken. However, it continued to deteriorate, with there being a lack of "vertical slicing" of the portfolio as redemptions continued. Subsequently:

(a) Link imposed liquidity limits in May 2018 as a backstop position to prevent the portfolio from deteriorating any further. However, those limits came to be treated (by both Link and WIM) as an acceptable framework within which the WEIF was to be run, rather than urging the fund to rebalance the portfolio away from the inappropriate and unreasonable liquidity profile described above.

(b) In October 2018, Link approved a change in the liquidity monitoring framework, at WIM's instigation. That change was approved despite the fact that:

a. Metrics which had hitherto been part of the monitoring programme and which were identifying, and were likely to continue (and did in fact continue) to identify, breaches of liquidity thresholds, were abandoned.

b. The new monitoring framework was less prudent (in the sense that it did not identify the liquidity profile as breaching thresholds, whereas the previous framework did), but the relevant thresholds were not adjusted downwards to take this into account.

(c) From September 2018 onwards, Link repeatedly communicated to WIM that there was a need to improve the overall liquidity profile of the WEIF. However, Link failed to ensure that the necessary actions were taken.

2.11. The failure to take appropriate steps to control WIM and ensure that the liquidity in the WEIF was properly managed meant that the unreasonable and inappropriate liquidity profile of WEIF was not corrected.

TISE Securities

2.12. Although ACDs are not usually expected to be involved in an underlying asset's corporate actions, including listing on exchange, Link failed to give consideration to the potential implications for the WEIF's liquidity profile where businesses which the WEIF had holdings in announced an intention to convert from unlisted status to becoming listed on an exchange. This included four businesses whose assets were held by the WEIF, which announced that they intended to list relevant securities on the International Stock Exchange, a stock exchange headquartered in Guernsey ("TISE"). Details of the process by which this happened are set out below;

(a) The WEIF invested in a number of companies that were unquoted ("Unquoted Securities"), which meant that the relevant securities they issued were not listed and traded on an exchange. Between October 2014 and October 2015, the WEIF invested in the TISE securities, which were all Unquoted Securities, prior to subsequent listing.

(b) In August 2017, WIM entered a moratorium on any further investments in Unquoted Securities, as the WEIF was approaching the 10% limit on Unquoted Securities, permitted under COLL 5.2.8R (the "10% limit"). By the end of November 2017, the percentage of Unquoted Securities held by the WEIF stood at 9.82%.

(c) Unknown to Link, WIM notified each of the TISE companies about the issues arising from the funding moratorium as well as the WEIF nearing the 10% limit. WIM was unable to provide further funding to the TISE companies unless the securities held by the WEIF were listed, which meant they would no longer be covered by the 10% limit. Subsequently, each of these four companies listed shares in their companies on TISE.

(d) Notwithstanding their listing, prior to the suspension of the WEIF on 3 June 2019, there were no arm's length market dealings in any of the TISE securities, and only one trade recorded for any of the securities. Link did not change its treatment of the TISE securities from a liquidity perspective, being aware that the relevant listings were likely to be, at most, thinly traded. However, Link failed to give sufficient consideration to the potential implication of the WEIF holding what it knew would be illiquid assets, in addition to those within the 10% limit. By not adequately considering the implications of the various listing on TISE, Link failed to sufficiently recognise the risks of increased levels of illiquid assets being held within the Fund. This increased the risks of liquidity issues arising.

2.13. The Authority's operational objectives include securing an appropriate degree of protection for consumers and protecting and enhancing the integrity of the UK financial system. Link's failings threatened these objectives, resulting in significant losses to investors and an adverse impact on confidence in the fund management sector.

2.14. Link (with the support of a voluntary contribution from its ultimate parent company, LAHL) has voluntarily agreed to contribute, without admission of liability, up to £230 million towards restitution for investors who held investments in the WEIF at the point of suspension on 3 June 2019. The Authority is satisfied that imposition of a penalty would reduce the amount of restitution available and, on the basis of the contribution made, does not seek to apply or enforce the penalty that would otherwise have been imposed. But for the restitution issues, the Authority would have imposed a financial penalty on Link in the amount of £35,000,000 pursuant to section 206 of the Act, for breaches of:

(a) Principle 2 (skill, care and diligence); and

(b) Principle 6 (fair treatment of customers).

2.15. The Authority considers that these contraventions have resulted in unfair treatment and consequent losses being incurred by investors in the WEIF who did not redeem their investments before its suspension on 3 June 2019. This is because Link allowed redemptions to be made by realising more liquid assets, leaving those who continued to hold investments in the WEIF at the time of its suspension with an unfairly disproportionate share of less liquid assets whose previously recorded values in certain cases could not ultimately be realised upon sale. The Authority considers that these losses can most appropriately be assessed by calculating the additional amounts which those who remained invested in the WEIF at the time of its suspension would have received had the proceeds of the sale of assets from November 2018 to the time of suspension been divided equally between all investors (rather than being used only to meet redemptions). Using this approach, the Authority has calculated that those invested in the WEIF at the time of suspension would have received an additional £298,403,919.

2.16. The Authority considers that it would be just to require Link to pay this sum of money as restitution to the WEIF (which will thereby benefit the Relevant Investors). However, this sum significantly exceeds the assets available to Link. As a result, for the purposes of settling this action, Link agreed to propose the Scheme, pursuant to the terms of the Companies Act 2006, to Relevant Investors. Under the terms of the Scheme, Link has agreed to pay all its available assets to the WEIF, together with a contribution by LAHL of approximately £60 million. This will result in restitution of up to £230 million being paid to Relevant Investors. The Scheme was subject to a vote by Relevant Investors (in which 93.7% of those voting voted in favour) and to sanction by the High Court. The Authority therefore requires Link to pay restitution in the sum of £298,403,919, or such lesser sum as may be payable under the terms of the Scheme.

2.17. The Authority acknowledges the cooperation shown by LAHL and Link and the substantial contribution that LAHL has voluntarily agreed to provide towards restitution. For the avoidance of doubt, no criticism is made of anyone except Link in this Notice.

3. DEFINITIONS

3.1. The definitions below are used in this Notice:

"the Act" means the Financial Services and Markets Act 2000;

"ACD" means an Authorised Corporate Director of a fund;

"ADTV" means the Average Daily Traded Volume of a security, which is the average number of shares traded per day on an exchange over a certain period of time;

"AFM" means Authorised Fund Manager;

"AUM" means assets under management, which is a total value of a fund's assets;
"the Authority" means the body corporate previously known as the Financial Services Authority and renamed on 1 April 2013 as the Financial Conduct Authority;

"Benevolent" means BenevolentAI Limited;

"COLL" means the Collective Investment Schemes sourcebook, part of the Handbook;

"DEPP" means the Decision Procedures and Penalties Manual, part of the Handbook;

"EG" means the Authority's Enforcement Guide;

"Full Allocation Approach" means a liquidity risk monitoring approach in which a security was assigned to a time bucket based upon the number of days it was expected to take to dispose of all shares held by the fund in that security;

"FVP" means Fair Value Pricing, a means of estimating the value of an asset where no market value is readily ascertainable;

"Handbook" means the collection of regulatory rules, manuals and guidance issued by the Authority as in force during the Relevant Period;

"IOSCO" means the International Organization of Securities Commissions, an association of national securities and financial regulators from over 100 countries;

"Industrial Heat" means Industrial Heat, LLC;

"KCC" means Kent County Council;

"KIID" means Key Investor Information Document;

"LAHL" means Link Administration Holdings Limited;

"Large Cap" means securities with a market capitalisation of greater than or equal to US$10 billion;

"Linear Allocation Approach" means a liquidity risk monitoring approach in which a security was assigned to numerous time buckets based upon the number of shares in the security that were expected to be disposed of each day;

"Link" means Link Fund Solutions Limited, known until 6 November 2017 as Capita Financial Managers Limited (FRN 119197);

"Mid Cap" means securities with a market capitalisation of between US$1 billion and US$10 billion

"NAV" means Net Asset Value, the value of a fund's assets minus its liabilities;

"NEX" means the NEX Exchange Growth Market (which has since been renamed as Acquis Stock Exchange), a stock exchange headquartered in England;

“Ombu” means Ombu Group;

“Participation Rate” means an estimate of the percentage of ADTV of a security that the WEIF could sell in one day without having a significant impact on the price of that security;

“Principle” means one of the Principles for Businesses, rules set out in the section of the Handbook entitled “Principles for Businesses” (PRIN);

“RCR” means the Redemption Coverage Ratio, a ratio based on Link’s liquidity metrics which measured the ability of the WEIF to meet redemption requests;

“Relevant Investors” means those persons beneficially holding units in the WEIF at the time of its suspension on 3 June 2019 (or their assignees);

“the Relevant Period” means the period from 1 May 2017 to 3 June 2019;

“Sabina” means Sabina Estates Limited;

“the Scheme” means the scheme of arrangement, proposed by Link under the terms of the Companies Act 2006 and sanctioned by the High Court on 9 February 2024;

“Small Cap” means securities with a market capitalisation of less than or equal to US$1 billion;

“the Statistical Model” means the statistical model used by the Authority to assess the liquidity of the WEIF over the Relevant Period, as described in paragraphs 4.104 to 4.105 below;

“SYSC” means the part of the Handbook entitled Senior Management Arrangements, Systems and Controls;

“TISE” means the International Stock Exchange, a stock exchange headquartered in Guernsey;

“the TISE companies” mean Benevolent, Industrial Heat, Ombu and Sabina;

"the TISE securities" mean securities in the TISE companies;

"the Tribunal" means the Upper Tribunal (Tax and Chancery Chamber);

"UCITS" means an undertaking for collective investment in transferable securities, as defined in section 236A of the Act;

"Unquoted Securities" means transferrable securities which are not listed and traded on an eligible market;

"the WEIF" means the LF Woodford Equity Income Fund (called the CF Woodford Equity Income Fund between 2014 and 2017 and, since 2018, the LF Equity Income Fund) (FRN 635902); and

"WIM" means Woodford Investment Management Limited (FRN 745433).

4. FACTS AND MATTERS

SECTION A: BACKGROUND

4.1. Link has been authorised by the Authority since 2001, with permission to manage funds, including UCITS. The WEIF is a sub-fund of the LF Woodford Investment Fund, an open-ended UCITS scheme, authorised by the Authority and opened in May 2014.

4.2. Link was the ACD of the WEIF from the fund's inception. The ACD's role was to manage and administer the WEIF in accordance with the functions set out in COLL 6.6.3. Broadly, an ACD maintains regulatory documentation (including the Prospectus and the Key Investor Information Document ("KIID")), maintains operational relationships with key stakeholders (including shareholders and the Authority), values and ensures accurate pricing of the fund's assets, and monitors relevant activities of the investment manager (WIM). As the WEIF's ACD, Link had regulatory responsibilities for the management of the fund. Link monitored and oversaw the WEIF and was required to ensure that it acted in the interests of all investors.

4.3. The ability of fund investors to redeem the value of their investments at short notice can be of particular importance to them. The WEIF's terms and conditions provided that investors were able to redeem their investments and be repaid within 4 days. However, as outlined in more detail below, many of the assets held by the WEIF could not be liquidated in such a short timeframe or could only be liquidated at significantly reduced prices. This gives rise to liquidity risk – the risk that, while a fund may hold assets of sufficient value to cover its liabilities (including redemption requests), it is unable to access liquid funds to meet these liabilities in the required timeframes.

4.4. It is the responsibility of the ACD to manage this liquidity risk. Liquidity risk will tend to be greater if a fund holds significant proportions of less liquid assets – that is those assets which take longer to liquidate – and may increase in the event of higher than expected net redemption requests. Meeting redemption requests by liquidating more liquid assets will generally lead to a deterioration in the liquidity profile of a fund (since this results in it holding a higher proportion of less liquid assets). This approach may lead to a position where the fund cannot meet redemption requests or can only do so by liquidating assets at significantly reduced values. This risks significant prejudice to those investors continuing to hold investments in the fund since they may be unable to access their funds and/or the value of their investments may reduce significantly.

4.5. Managing liquidity risk is therefore a key function of an ACD. Although there are a range of ways in which liquidity can be monitored and managed, the practices adopted must, at all times, be appropriate to the fund. In managing liquidity risk, the ACD is obliged to ensure that the fund complies with the Authority's rules, including specific threshold rules, for example that no more than 10% of the property of a UCITS scheme may be invested in Unquoted Securities, but also qualitative rules such as that the UCITS scheme aims to provide a prudent spread of risk (which includes liquidity risk) and that the liquidity profile is appropriate to the fund's redemption policy. While an ACD may delegate the investment management of a fund to an investment manager, the ACD remains responsible for ensuring that liquidity risk is managed appropriately.

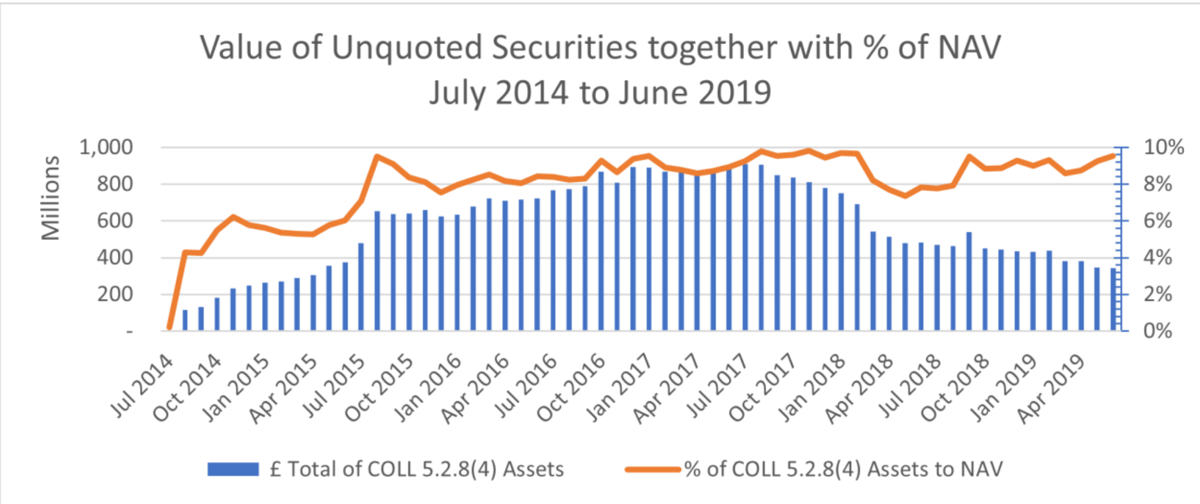
4.6. WIM had two roles: it was the Sponsor of the WEIF and the WEIF's Investment Manager. As Sponsor, WIM defined the principal features of the WEIF and engaged Link as ACD. WIM provided Link with all necessary documentation to establish the fund, and maintained those documents throughout the life of the fund. Link delegated the role of Investment Manager to WIM. As Investment Manager, WIM retained responsibility for discretionary investment management and advisory services, with a view to achieving the WEIF's investment objectives as permitted by regulations and the Prospectus. Link did not involve itself in deciding which particular investments were bought, held or sold, including which assets of the WEIF would be sold in order to meet redemptions. It did not require the WEIF to vertically slice the sale of investments across the liquidity profile, which is a recognised way of ensuring consistent liquidity is achieved.

4.7. The principal document that set out the investment objective and remit was the prospectus, accompanied by the KIID. Both the Prospectus and the KIID stated that the WEIF may invest in unlisted companies and overseas entities.

4.8. The WEIF made its first investment in Unquoted Securities in June 2014 (the month after the WEIF was launched). The WEIF made 68 investments in a number of Unquoted Securities during the lifetime of the fund. The value of Unquoted Securities that is permitted in a fund is 10% of its NAV, as set out in COLL.

4.9. The chart below illustrates the proportion of the WEIF's NAV which comprised Unquoted Securities over its lifetime.

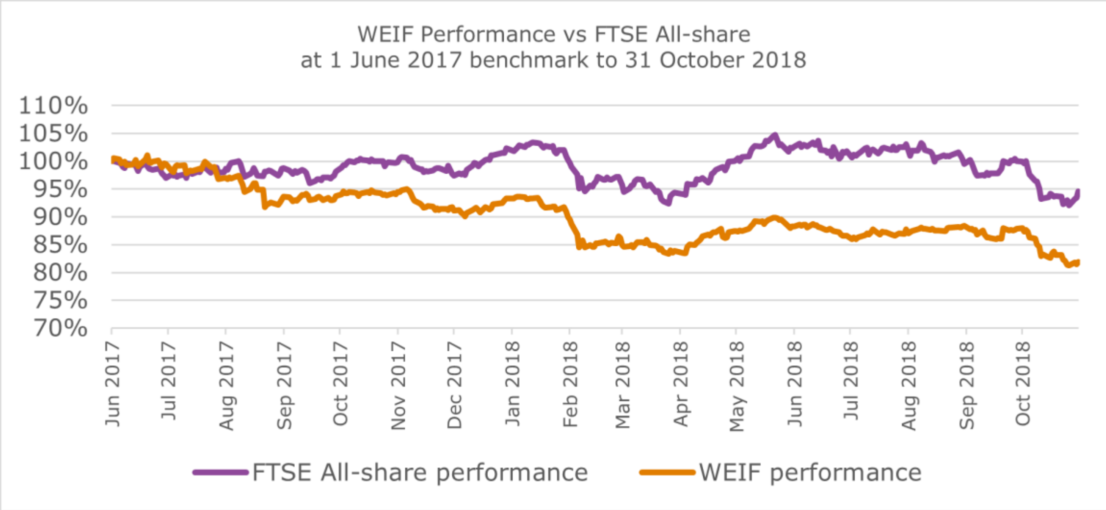
Chart 1



4.10. By the end of June 2014, the total NAV of the WEIF reached nearly £1.7 billion. From June 2014 to May 2017, the WEIF continued to attract investors and the fund grew to a peak of almost £10.2 billion by May 2017. Between 2 June 2014 and 31 May 2017, the WEIF generally outperformed the FTSE All-Share Index.

4.11. In April 2017, WIM began to implement a refocus of the WEIF's investments from global companies to UK focused companies, which were frequently smaller, less well capitalised companies. From June 2017 onwards, the WEIF generally underperformed against the market benchmark.

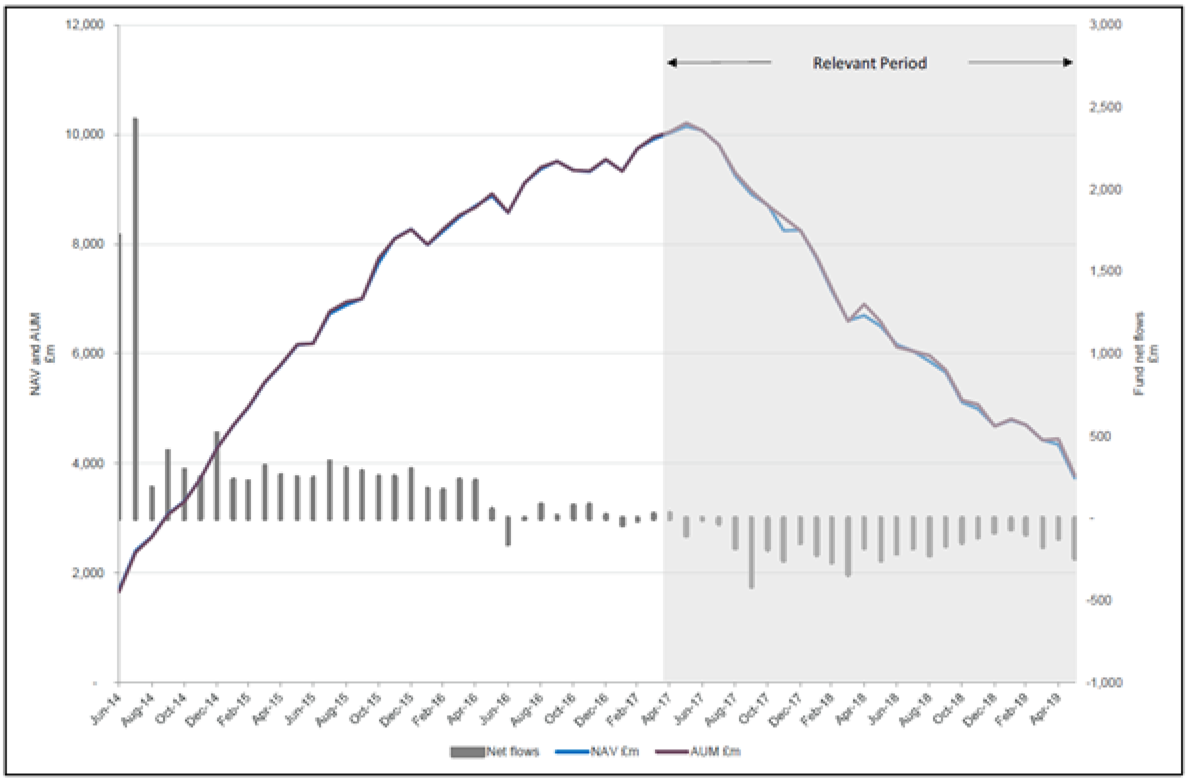
<u>Chart 2</u>



4.12. Owing to poor investment performance and persistent investor withdrawals, the WEIF's NAV dropped from £10.08 billion at the end of June 2017 to just over £3.5 billion by the end of May 2019.

<u>Chart 3</u>

The AUM, NAV and fund in/outflows of the WEIF from launch until its suspension



4.13. There was a wide range of types of investors in the WEIF, including significant levels of retail investors, investing directly or more generally via platforms or being invested indirectly via pension funds. Whilst there were other investors with significant holdings in the WEIF, Kent County Council ("KCC") was one of the largest single investors in the WEIF throughout the Relevant Period. Its holding was valued at between £325 million (3.2% of NAV) in June 2017 and £237 million (6.5% of NAV) at end of May 2019.

4.14. On 31 May 2019, KCC informed WIM that it would be redeeming its entire position in the WEIF. Following the instruction to sell being relayed to Link on the morning of 3 June 2019, Link made the decision to suspend the WEIF from 3 June 2019, meaning that all remaining investors were unable to redeem their units.

4.15. On 15 October 2019, Link wrote to investors in the WEIF that having considered the future of the fund, it had decided not to re-open the fund and to wind it up as soon as practicable.

SECTION B: THE LIQUIDITY FRAMEWORK USED FOR THE WEIF

4.16. The liquidity position of the WEIF was assessed and monitored by Link using several different metrics. In particular:

(a) Liquidity Buckets;

(b) T+ Metrics; and

(c) Redemption Metrics.

4.17. The core features of each of these types of metrics, and how they were altered by Link over time, are addressed immediately below.

<u>The Liquidity Bucket methodologies</u>

Overview of the model

4.18. One of the primary methods by which Link assessed the liquidity of the WEIF was by "liquidity bucketing". Liquidity buckets grouped the fund's assets by reference to the amount of time it would take to sell the asset. These buckets ranged from highly liquid (where the security could be sold relatively easily and quickly) to illiquid, frequently unlisted securities (where it would take a relatively long time to sell the security).

4.19. The time taken to liquidate a security was typically termed "T+" the relevant time period. For example, an asset that Link expected to be able to sell within one day without having a significant impact on its price would be categorised as "T+1". The bucket in which a security was categorised was determined by how quickly the shares held in that security could be liquidated. This was calculated as a product of:

(a) the Average Daily Traded Volume ("ADTV") of the security, which was the average number of shares traded per day on an exchange over a certain period of time; and

(b) the Participation Rate of the security, which reflected an estimate of the number of shares of that security that the WEIF could liquidate in one day, without having a significant impact on the price of that security.

4.20. During the time that the WEIF was operational, the following three versions of liquidity bucketing were used to assess the fund's liquidity, all of which are summarised below:

(a) the Five Category Model (used by Link for the WEIF from the inception of the fund until January 2018, this model was the standard model used by Link across all the other funds for which it was an ACD);

(b) the Initial Four Bucket Model (used by Link specifically for the WEIF from January 2018 until October 2018); and

(c) the Revised Four Bucket Model (used by Link specifically for the WEIF from October 2018 until the fund's suspension).

The Five Category Model

4.21. Between May 2017 and January 2018, Link assessed the WEIF's liquidity by allocating securities into five categories, based on their time to liquidate, as follows:

(a) T+1;

(b) T+5 (referred to by Link as "mini liquidity");

(c) T+2 >< T+7;

(d) Illiquid rump (>T+7); and

(e) Cash.

4.22. This model was Link's standard liquidity monitoring model used to monitor the liquidity of all funds that it managed on a daily basis. It was described by Link to the Authority as "*conservative*" due to the way securities were allocated to the relevant buckets. In particular, the Five Category Model allocated securities to appropriate liquidity categories assuming a 100% market Participation Rate (except for the "mini liquidity" category, which assumed a 20% Participation Rate) and based on when the entire holding could be sold (the "Full Allocation Approach"). According to Link, the conservative nature of the requirement for a full position to be sold was offset by the 100% Participation Rate which assumed that the fund would be able to utilise the entire daily trading volume of the security.

4.23. The issue of the 100% participation rate formed subject of a comment in a report issued to Link by a skilled person on 19 October 2018 in relation to various issues regarding the activities of Link. The skilled person observed in the report about the 100% market participation rate being an optimistic assumption in the context of a sell off. It also noted that the participation rate was outside normal market practice, where a 20-30% participation is typically assumed. The skilled person recommended in the report that Link revisit the market participation rate of 100%. The skilled person referenced that they had observed that the typical assumption is 10% in a stressed scenario and 20-30% in good market conditions. Despite this recommendation, no changes were made to the rate used.

4.24. The Five Category Model used the lower of the previous 5 or 20-day ADTV for the relevant security on a rolling basis, using data from the Primary Exchange on which the security was listed.

4.25. Stress testing of the WEIF was considered as part of Link's liquidity monitoring in Autumn 2016. These initial stress tests were conducted in November and December 2016. Link described the stress tests as being based on trading volumes, and then on the cost to investors if large redemptions were made from the fund. Subsequently, stress testing for the Five Category Model (in the pre-September 2018 period) featured Link reducing the ADTV for Large Cap stocks by 20% and Small Cap stocks by 40%. This daily stress test was an approach Link used across all funds which it managed.

4.26. Link's Risk Policies Document set out Link's liquidity risk criteria for funds with liquidity concerns. The criteria was based on the percentage of a fund's NAV which could be liquidated within 5 days (T+5). It was set at different levels for 'Normal Conditions' and for 'Shock periods and Stress testing'. In particular, for Large Cap funds, if T+5 was less than 60% of the fund's NAV in Normal Conditions or less than 40% in Shock periods and Stress testing, the fund was deemed to have liquidity concerns. During the Relevant Period the WEIF did not hold the requisite percentage of T+5 assets to meet the 60% threshold, and as a consequence was subject to enhanced daily monitoring by Link.

The Initial Four Bucket Model

4.27. In January 2018, Link amended the Five Category Model that was used for the liquidity monitoring of the WEIF, and changed it to an Initial Four Bucket Liquidity Model as set out below:

(a) Bucket 1: T+1 - T+7 (i.e. positions that could be liquidated in 7 days or less).

(b) Bucket 2: T+8 - T+30.

(c) Bucket 3: T+31 - T+180.

(d) Bucket 4: T+181 - T+365+.

4.28. The Initial Four Bucket Model continued to assume a 100% Participation Rate and only considered ADTV data from the primary exchange on which the security was traded. However, instead of the lower of the previous 5 and 20 day average trading volumes (as used in the Five Category Model), Link used the lower of the 5 day and 20 day average trading volume as at March 2017.

4.29. Link explained to the Authority that the move to the March 2017 trading volumes from the rolling basis as a standard reference point across the funds for which it was ACD was aimed at minimising the market fluctuations by removing an element of seasonality in market volumes. There were also two sets of data analyses produced under this model: "True Data Analysis" and "Adjusted Data Analysis", with the former using the ADTV as used in the Five Category Model and the latter based on trading volumes as at March 2017. The effect of changing the reference point for trading volumes was that fluctuations in the WEIF's liquidity appeared to have been smoothed.

4.30. Although the Five Category Model was the standard liquidity measure that Link used for all other UCITS funds for which it was the ACD, the Initial Four Bucket Model was a "*bespoke control mechanism*" developed by Link for use in relation to the WEIF only.

4.31. In May 2018 Link introduced the following limits under the Initial Four Bucket Model: a limit of 35% of NAV in Bucket 4; and a limit of 70% of NAV in Buckets 3 and 4 combined.

4.32. Link continued daily stress testing in accordance with the testing for the Five Bucket model as described above.

The Revised Four Bucket Model

4.33. In October 2018, the Revised Four Bucket Model was subsequently adopted as Link's primary method of monitoring the WEIF's liquidity. The change occurred after discussions between WIM and Link, in which WIM raised concerns with Link in September 2018 on the suitability of the Initial Four Bucket methodology (in particular about the use of seasonally adjusted volumes fixed as at March 2017 for calculating bucket positions).

4.34. The bucket composition and allocation remained the same as the Initial Four Bucket Model with two new adjustments. The first was that the ADTV period changed from the lower of 5 and 20-day ADTV at March 2017 to a 12-month rolling average. The former methodology had been viewed by Link as "*potentially unreliable*" due to its reliance on average trading volumes over a short period, at a fixed point of time. The adjustment was, by Link's explanation, aimed at giving a fairer reflection of the volumes traded over a longer time horizon. Link also stated that the changes made the Four Bucket Model "*more responsive to changes in portfolio composition as well as secular changes in the market with the result that the liquidity monitoring became more precise*".

4.35. The second adjustment was that under the revised methodology, ADTV was intended to capture trades from all exchanges where a security was traded, as opposed to the Initial Four Bucket Model which only captured trades from primary exchange and therefore did not consider all potential pools of liquidity.

4.36. The Revised Four Bucket Model implemented further triggers and limits on the percentage of the WEIF's holdings in each bucket. In particular:

(a) The triggers required the launch of an investigation into the cause of the trigger being crossed, and an update to the contingency plan, if

Bucket 4 increased above 30%, Buckets 3 and 4 combined increased above 65%, or Bucket 1 decreased below 8% of NAV.

(b) The limits required the implementation of the contingency plan if Bucket 4 increased above 35%, Bucket 3 and 4 combined increased above 70% (with these two limits having already been introduced under the Initial Four Bucket Model, as noted above), or if Bucket 1 decreased below 5% of NAV.

4.37. For stress testing, Link tested the impact of sudden 10%, 15% and 20% redemptions of the portfolio, which Link described as presupposing an extreme approach, meeting redemptions by selling only the most liquid assets until these were exhausted, before moving on to the next level of liquidity.

4.38. The assumptions underpinning each of the three bucketing models described above can therefore be summarised as follows.

Figure 1- Summary of the assumptions underpinning the Five Category Model, the Initial Four Bucket Model and the Revised Four Bucket Model

Key inputs	**Five Category Model**	**Initial Four Bucket Model**	**Revised Four Bucket Model**
	Pre-September 2018	**January 2018 to September 2018**	**Post-September 2018**
ADTV exchange data	Primary exchange	Primary exchange	All exchanges
ADTV period	The lower of the previous 5 and 20 day average daily trading volumes	Presented on two bases: (i) unspecified, described as "*the average daily market volume, as obtained from Bloomberg*" (referred to in the Link Liquidity Reports as the "*True data*")[95]; and (ii) the lower of the 5 day and 20 day average volume as at March 2017 (referred to in the Link Liquidity Reports as the "*Adjusted Data*")	12 month rolling average
Participation Rate	i) 100% for all categories other than the "*mini-liq*" category ii) 20% for the "*mini-liq*" category	100%	100%
Allocation method	Full Allocation Approach	Full Allocation Approach	Full Allocation Approach

T+ Metrics

4.39. In addition to the liquidity bucketing model, Link analysed WEIF's liquidity by reference to the T+ Metrics which measured the proportion of the fund that was liquidable within a certain number of days, expressed as a percentage of the NAV of the fund. Similar to the bucket models, the T+ Metrics are expressed as "T+" and a number of days, with T+5, for example, reflecting the proportion of the WEIF's NAV which could be liquidated within five days.

4.40. In the pre-September 2018 period Link used a T+5 metric which formed part of the Five Category Model. It used data from the primary exchange, with ADTV calculated as the lower of the previous 5 or 20 day trading volume, a 100%

Participation Rate, and the Full Allocation Approach. It was also stress tested and monitored in accordance with the Five Category Model described above.

4.41. In the post-September 2018 period, following the adoption of the Revised Four Bucket Model, Link used the T+1, T+5 and T+20 Metrics which were introduced as a "*control mechanism*" to supplement the existing redemption monitoring procedures. These T+ Metrics used data from all exchanges, ADTV calculated as a 12-month rolling average, a 25% Participation Rate and a Linear Allocation Approach, which assigned a security to a T+ time period based on the amount that could be sold during that time period. This meant that the same security may appear in different T+ portions of the portfolio. The Redemption Coverage Ratios (see below) were produced using these outputs, and had specific triggers and limits associated with them. These metrics looked at liquidity which was immediately available in the WEIF.

<u>The Redemption Metrics</u>

4.42. Link also monitored the WEIF's liquidity through the use of the Redemption Metrics which measured the ability of the fund's assets to meet its potential liabilities, in circumstances such as a redemption shock.

Amivest Metric

4.43. In the pre-September 2018 period, in particular from November 2017, Link used the Amivest Metric which is an estimate of the cost of selling a portion of a fund in a single day of trading, based on trading volumes and prices. This measure shows the potential impact of disposing of a portion of a holding in a particular security on the price of that holding. Link assessed the price impact of liquidating 5% of the portfolio, using this measure. This impact, the Amivest Score, was expressed in basis points ("bps") which Link tracked against certain thresholds. The threshold before February 2018 was 50bp and assumed that 100% of each security would be sold (going from the most liquid down until 5% of the portfolio NAV is liquidated). After February 2018 the threshold was moved to 30bp under the assumption that only 5% of each security would be sold. The Link Liquidity Reports did not detail any contingency plans in the event the Amivest Metrics were to be breached.

Redemption Coverage Ratio (RCR)

4.44. In October 2018, after adopting the Revised Four Bucket Model, Link monitored the RCR, which was based on Link's T+1, T+5 and T+20 Metrics and measured the ability of the WEIF to meet redemption requests.

4.45. The RCR considered the proportion of the WEIF that could be liquidated in 1, 5 and 20 days (as explained in the paragraphs 4.39 – 4.41 above) and divided that by the average daily redemptions based on the previous 10-day rolling average. For example, if £18 million could be liquidated in 1 day and the average daily redemptions over the previous 10 days were £2 million then the 1 Day RCR would be 9. As with the T+ Metrics, RCR assumed a 25% Participation Rate, an ADTV of 12 months and captured trades from all exchanges.

4.46. Link set several additional triggers and limits based on the RCR. If a trigger was reached, an 'event' was to be launched to investigate the cause and update contingency plans. If a limit was reached, the liquidity contingency plan was to be executed. The RCRs had the following limits and triggers:

(a) 1 Day RCR had a trigger of 8 and a limit of 5;

(b) 5 Day RCR had a trigger of 30 and a limit of 25; and

(c) 20 Day RCR had a trigger of 150 and a limit of 120.

4.47. The RCR was stress tested in the same way as the T+ Metrics, by assessing the percentage of the portfolio realisable in 1 day, 5 days and 20 days after modelling redemptions of 10%, 15% and 20%. Link explained to the Authority that it also modelled "*… scenarios based on redemptions by the largest discretionary investors in the fund…"* and that "*the analysis presupposes an extreme approach, meeting redemptions by selling only the most liquid assets until these are exhausted, before moving on to the next level of liquidity."*

Unquoted Securities Limits

4.48. Link also monitored the level of Unquoted Securities in the WEIF. There were two limits associated with this monitoring. The first limit was at 8.5%. Once this level was reached, no further investments in new Unquoted Securities were permitted.

The second limit was at 9.5%. At this level, no further investments in Unquoted Securities were permitted.

<u>WIM's Initial T+20 Metric</u>

4.49. Until September 2018 (subsequent to which it adopted the Revised Four Bucket Model), WIM used the Initial T+20 Metric as its principal liquidity metric for assessing the WEIF. During the Relevant Period, Link was aware of WIM's Initial T+20 Metric and the underlying input parameters it used.

4.50. The Initial T+20 metric measured the percentage of the WEIF's portfolio realisable in 20 days expressed as a percentage of NAV. It was calculated on a daily basis, assumed a 20% Participation Rate and used a Linear Allocation Approach. Originally the primary exchange data for ADTV was used, however prior to September 2018 WIM extended this to include other trading venues. The ADTV was calculated using the preceding six months trading data.

4.51. WIM set an internal trigger on the Initial T+20 Metric if the amount that could be liquidated in the 20 day period fell below 25% and a limit if the amount that could be liquidated fell below 20%.

SECTION C: LINK'S RESPONSE TO THE WEIF'S DETERIORATING LIQUIDITY

4.52. Link was aware that the WEIF's liquidity was deteriorating throughout the Relevant Period, but did not effectively communicate these problems to WIM; and, insofar as Link did communicate them, it did not ensure that they were acted upon. Link also presided over changes to the liquidity monitoring framework which were adopted without proper justification.

4.53. Further, as set out in Section D below, Link was aware that the WEIF held a high percentage of Unquoted Securities Link failed to give sufficient consideration to the potential implications for the WEIF's general liquidity, but did not ensure that WIM acted upon this concern. However, Link failed to give sufficient consideration to the potential implication of the WEIF holding what it knew would be illiquid assets, in addition to those within the 10% limit. Link failed to sufficiently recognise the risks of increased levels of illiquid assets being held and the increased risk of liquidity issues arising. Link should have been fully aware of the risks and acted to prevent the repeated use of this process which enabled a higher level of illiquid funds to be held.

Link’s Early Awareness of and Response to Liquidity Problems (May 2017 - May 2018)

4.54. The WEIF was subject to sustained net asset outflow from May 2017 onwards. From November 2017 onwards, there were discussions within Link expressing concerns about the liquidity of the WEIF, as highlighted below:

(a) On **20 November 2017**, it was noted internally within Link that *“we need to now acknowledge that Woodford* [i.e. WIM] *is in need of better management of its liquidity”*.

(b) On **21 November 2017**, Link produced a liquidity analysis which showed that the WEIF’s liquidity was deteriorating, the fund had reached a “tipping point” and that there was a risk of the WEIF becoming “*unbalanced*”.

4.55. On **23 November 2017**, WIM wrote to Link about the proposed Sabina listing (dealt with in more detail in Section D below), which would result in certain securities moving from the Unquoted Securities category, and thus no longer counting towards the limit that Unquoted Securities must form no more than 10% of NAV. It was noted internally at Link that the proposal *“would indicate Woodford* [i.e. WIM] *have no idea of the real problem and that this is at best a sideshow and does nothing to improve liquidity. Do they realise that if this goes ahead they cannot buy anymore”*.

4.56. On **27 November 2017**, after completion of a liquidity review the previous day that considered the Initial Four Bucket Model, messages of concern about the WEIF’s liquidity profile were circulated internally at Link, with one senior individual noting that *“[t]he overall liquidity of the portfolio continues to decline and we need a firm plan on how to address”*.

4.57. On **30 November 2017**, a discussion was held between Link and WIM, for which Link had produced a paper (sent to WIM on 28 November 2017) which set out actions required of WIM *“now”* to explain: (i) how WIM would meet a redemption of 5% or more in one day without *“further compromising the liquidity profile of the fund*”; and (ii) the time it would take to bring the overall liquidity profile of the

WEIF into a more balanced position, such that the allocation to Liquidity Bucket 4 was reduced and the allocation to Liquidity Bucket 1 restored.

4.58. On **4 December 2017**, WIM wrote to Link raising a number of matters in respect of the recently issued IOSCO liquidity recommendations paper. WIM raised a number of questions with Link concerning how Link, as the *"responsible entity",* was dealing with issues raised in the IOSCO guidance.

4.59. On **5 December 2017**, Link circulated a paper, the context for which was described in the background section as follows: *"[i]n response to a number of concerns raised with* [WIM] *by* [Link] *in respect of the liquidity structure of* [the WEIF]*, WIM have raised a number of matters in respect of the IOSCO paper"*. The Link paper set out its response to the questions raised by WIM. It referenced the discussion on 30 November 2017 and paper described in paragraph 4.57 above. Appendix A to the paper noted that failure to ensure adequate liquidity within a fund at its extreme could lead to a suspension and investors being unable to redeem their holdings, which in periods of volatility could *"cause capital erosion"*. The next day, an individual at Link noted concern about *"the perilous state of the liquidity"* in the WEIF. The Authority has seen no evidence that the urgency of this concern was conveyed to WIM.

4.60. On **11 December 2017**, a series of internal Link emails recorded that (1) there was serious concern about the WEIF's liquidity, but (2) it was decided to wait for a paper from WIM before considering what action to take. WIM submitted that paper in early January 2018. However, the Authority has seen no evidence that Link took any particular formal action in response to the submission of the paper.

4.61. On **18 January 2018**, a Link liquidity analysis, presented at a committee meeting, concluded that the circumstances *"could suggest that the redemption flow has been met by selling the more liquid assets and thereby increasing exposure to assets which will be more difficult to sell in volume",* and noted that the position required action to be taken. Nonetheless, the Authority has seen no evidence that Link directed WIM to ensure that redemptions were met by selling assets from across the liquidity buckets, even though that would help to ensure that the WEIF's liquidity profile was maintained. This *"vertical-slicing"* (in other words, sourcing liquidity from across the portfolio, rather than solely from the more liquid buckets) is recognised within the Authority's guidance entitled "Liquidity Management for investment firms: good practice", published on 29 February 2016, as an example of good practice in liquidity management.

4.62. Also in **January 2018**, the Initial Four Bucket Model was introduced (see paragraphs 4.27 – 4.28 above), adopting a 100% Participation Rate and Full Allocation Approach. Had Link adopted a Participation Rate of 20% and a Linear Allocation Approach (which would have been reasonable and appropriate, as set out at paragraph 4.117 below– unlike the assumptions actually adopted), the Bucket 4 trigger that Link contemporaneously set would immediately have been crossed, and would have remained so continuously until the WEIF was ultimately suspended in June 2019.

4.63. On **1 February 2018**, Link sent an email to WIM, pointing out that the level of redemptions had risen recently and that a meeting would be helpful to discuss next steps.

4.64. On **8 February 2018**, a Link liquidity analysis reiterated the concern expressed at the Link committee meeting on 18 January 2018. It noted a deterioration in the overall liquidity profile of the WEIF over the period from January 2017 to January 2018. Reference was made to increased exposure to assets within Liquidity Buckets 3 and 4; a decrease in assets within Liquidity Buckets 1; and, *"more significantly",* a decrease in assets within Liquidity Bucket 2. It was noted that further discussion with WIM would be required. This was discussed at a meeting involving Link and WIM the next day, but the Authority has seen no record of any formal action plan having been agreed at that stage.

4.65. On **15 February 2018**, there was a meeting of a Link committee at which reference was made to *"the need to focus not only on the unquoted stock but also on the overall liquidity position"*. It was suggested that Link should fix an internal benchmark against which the volume of unquoted holdings could be monitored, but (save as set out below) the Authority has seen no evidence of this having been communicated to WIM. It was recognised that realising assets to meet redemptions would affect the shape of the WEIF for remaining investors; and that while the majority of the assets within the WEIF could be sold quickly, there would be assets that would take longer to sell. It was observed that the proportion of such assets that would take longer to sell would increase incrementally as the more liquid assets are sold.

4.66. In **early May 2018**, there were discussions between Link and WIM as to the position to be taken in regulatory correspondence with the Authority. At WIM's suggestion, Link changed an original draft slide in order to remove references to a limit of 35% on Buckets 3 and 4 which Link had proposed be implemented. Link has stated that the reason for the change to the document was that, although Link would monitor that limit internally, it had not imposed a specific limit on the WEIF's portfolio, nor had this been agreed with WIM. The subsequent references relayed to the Authority were that these figures were *"guidelines"*.

<u>The Monitoring Changes of May 2018</u>

4.67. In response to contemporaneous questions from the Authority's Supervisors, Link stated that at or around the time of a Link committee meeting on **17 May 2018,** Link started to give serious internal consideration to whether it was necessary to impose specific limits on WEIF's liquidity profile.

4.68. On **30 May 2018**, Link held a meeting to discuss the WEIF's liquidity profile and responses to be made to questions from the Authority. Link's view of the meeting was that it had been agreed that a limit of 35% of NAV on Bucket 4 and a limit of 70% on Buckets 3 and 4 combined would be imposed. However, Link and WIM appear to have had different understandings of what had been agreed. In particular, WIM believed that it had not agreed to hard limits, and that any breaches would just lead to a discussion. In contrast, an individual within Link stated to the Authority that even if the WEIF stayed within these limits, that did not mean that its liquidity profile was acceptable. They thought that these particular thresholds were set simply because they reflected the liquidity profile of the WEIF at the time, and that the intention was simply to prevent further deterioration.

4.69. By **July 2018**, the WEIF's liquidity had declined significantly. For example, from this point on, the time it would have taken the WEIF to liquidate 5%, 10% and 20% of its NAV significantly increased, and it consistently would have taken significantly longer to liquidate 5% and 10% of its NAV than the bottom ranked comparator fund. Furthermore:

(a) Had Link adopted reasonable and appropriate assumptions, in particular a Participation Rate of 25% and a Linear Allocation Approach, the Bucket 4 trigger would have been breached continuously from this point on.

(b) Had a 20% Participation Rate been adopted, the trigger in respect of Buckets 3 and 4, and the limit in respect of Bucket 4, would have been breached continuously from this point on.

(c) Whilst a range of Participation Rates might be used, and LFS has indicated 30% might reasonably be used, we note that LFS did not use that rate for any other metrics and variously used 20% and 25% participation rates in other areas of monitoring. In the circumstances, we consider that 25% was the appropriate and reasonable Participation Rate to use for the liquidity bucket monitoring during the period being considered.

4.70. On **16 July 2018**, the liquidity of the WEIF was raised at a meeting involving Link and WIM. WIM questioned Link about the rationale for the limits and sought clarity from it about wording as to when the limits applied and what was required if the WEIF approached these limits.

<u>The Monitoring Changes of September 2018</u>

4.71. In **September 2018**, WIM pressed for changes to be made to the liquidity framework, having previously questioned the trading venues used for volume data. Following discussions, Link accepted that such changes should be made.

4.72. WIM maintained throughout September 2018 that – contrary to Link's view – it (WIM) did not need to improve the liquidity in the WEIF. In particular:

(a) On **11 September 2018**, WIM approached Link with a proposal to adjust the liquidity management framework.

(b) On **20 September 2018**, Link held a call with WIM. There was an immediate dispute between Link and WIM as to whether it was agreed on this call that the WEIF's liquidity needed improving. Link's position, as set out in an email to WIM, was that there was a *"need to improve the overall liquidity profile of the fund"* and for the *"fund to be rebalanced to a considerably more liquid profile"*.

(c) On **24 September 2018**, Link accepted that it might be *"useful"* to *"consider"* alternative calculations, but that the current monitoring framework should remain in place for now, and that Link *"continue[d] to press the need for a long term rebalancing of the portfolio to a more liquid overall profile as well as a reassessment and reformulation of an effective liquidity monitoring framework"*.

(d) On **25 September 2018** (at the latest), Link changed position and agreed to change the monitoring framework to the Revised Four Buckets Model, as set out at paragraphs 4.33 – 4.38 above.

(e) On **26 September 2018**, Link recorded the change in an email and stated that WIM and Link needed to *"work together to formulate a proposal for a more refined liquidity management framework"* and *"acknowledge the need to rebalance the portfolio in the longer term (6m +) to a more balanced liquidity profile appropriate for a daily dealing UCITS fund".*

(f) On **27 September 2018**, WIM acknowledged the change in framework and accepted that there were limits that could not be crossed. However, WIM also stated that it did not *"believe there is a need to rebalance the [WEIF's] profile to a more liquid one over the longer term"*.

4.73. In reality, the liquidity of the WEIF had undergone a serious deterioration. For example, applying Link's own calculations under the Five Category Model, in February 2018, 58% of the NAV was only liquidable in 8 or more days. This category of securities was referred to by Link in its Five Category Model as the *"illiquid rump";*. However, by September 2018, this figure had increased to 100% of the WEIF's NAV (i.e. the entire fund classified as an "illiquid rump" under this model).

4.74. On **30 September 2018**, Link produced a liquidity analysis of the WEIF. It pointed out that *"…bucket 4 was above the 35% threshold as at the end of September"*. The impact of the introduction of the Revised Four Bucket Model at this time meant that the proportion of assets falling into Bucket 4 level went from a breach position of 37.41% of NAV to 24.6%, thus enabling compliance with the limit.

Link’s Later Awareness of and Response to Liquidity Problems (October 2018 – June 2019)

4.75. Over the period from **October 2018 to April 2019**, the WEIF’s liquidity continued to deteriorate. Applying Link’s own calculations under the Revised Four Bucket Model:

(a) Bucket 1 assets decreased from 14% to 8% of the NAV between September 2018 and April 2019;

(b) Bucket 2 assets increased from 26% of the NAV in September 2018 to 29% of the NAV in April 2019;

(c) Bucket 3 assets decreased from 36% of the NAV in September 2018 to 32% in April 2019; and

(d) Bucket 4 assets increased from 25% of the NAV in September 2018 to 33% in April 2019. As noted above, the starting position of 25% was actually a revised lower level due to the new methodology being introduced.

4.76. From **October 2018**:

(a) Had a 25% Participation Rate been used (even with a Linear Allocation Approach), the Buckets 3 and 4 trigger would have been continuously crossed (and limits would have been breached in November and-December 2018 and between April and-May 2019); while the Bucket 4 limit would have been continuously breached.

(b) Had a 20% Participation Rate been adopted, the Buckets 3 and 4 limits would have been continuously breached.

4.77. On **1 October 2018**, it was reported at a Link committee that a new contingency plan had been received on 28 September 2018 from WIM regarding the WEIF’s *“35% liquidity limit”* and that *“Woodford* [i.e. WIM] *had now acknowledged that they had a liquidity issue with the Fund”.* It was noted that a meeting had been arranged for 2 October 2018 with WIM to discuss the matter in more detail. At that meeting Link *“confirmed that* [Link] *do not foresee any liquidity issues on the* *current redemption numbers and will look to meet* [the Authority] *with WIM once the metrics are concluded"*.

4.78. On **18 October 2018**, it was reported to a Link committee that *"the new methodology [i.e. the Revised Four Bucket Model] suggested that the fund has more liquidity than previous analysis had shown… previously figures were too conservative"*. This assertion (that previous analyses of liquidity were too conservative) was incorrect, as Link would have realised had it adopted appropriate assumptions as set out at paragraph 4.116 when applying the Revised Four Bucket Model.

4.79. On **30 November 2018**, Link conducted its monthly liquidity analysis, finding that the WEIF's liquidity had continued to deteriorate.

4.80. On **10 December 2018**, a meeting was held between Link and WIM. Link produced a summary of that meeting for WIM on **12 December 2018**, including recording its expectation that WIM would *"be undertaking prompt action to address both the valuation and liquidity concerns with the ultimate goal of bringing the hard to value assets down from 19% to less than 10% and for the portfolio to return to a more balanced position between the four liquidity buckets"*. However, no deadlines were set for this to happen. WIM replied with a holding email, stating that it would *"respond more fully shortly"*. The Authority has seen no evidence that any immediate formal action was taken in response to this expectation.

4.81. On **17 December 2018**, it was noted internally at Link that WIM were *"still too relaxed about things…Short term actions are risible and longer term actions are still too leisurely"*. The Authority has seen no evidence of any action by Link arising from this concern.

4.82. The Link liquidity analysis of the WEIF dated **31 December 2018** noted that *"the overall trend of deteriorating liquidity has continued, with buckets 1-3 decreasing as a % of NAV while bucket 4 increased by 48bps".*

4.83. On **21 January 2019**, it was noted in response to a document that set out the contingency plans for dealing with the level of Unquoted Securities which had been sent by WIM to Link that *"parts of the document reflect an overly positive perspective…but that it [sic] not of any consequence at the moment"*.

4.84. Liquidity concerns continued to be expressed by Link, including at a Link committee meeting on **24 January 2019**; and at a meeting involving WIM on **25 February 2019**.

4.85. On **28 March 2019**, Link wrote to WIM, making it clear that, having read the latest liquidity contingency plan, it was not satisfied with WIM's proposed actions to improve the WEIF's liquidity. It required WIM to identify *"concrete actions that have been or will be taken to improve the combined buckets 3 and 4 metric, particularly if the 70% limit is breached",* and noted that Link *"continues strongly to urge WIM to bring the liquidity profile out of the trigger by month end"*. WIM responded the next day, resisting the need to restore the WEIF's position to below the amber trigger threshold, and arguing that the buckets did not reflect the WEIF's true liquidity. WIM also noted that such a request was not in accordance with the limit framework plan that Link had approved, namely that, when an amber threshold was crossed, WIM should prepare contingency plans which would then be enacted if the red threshold was crossed.

4.86. It was recognised internally within Link that WIM's response was not adequate to the scale of the problem, with views being raised within Link that action to take WIM out of the trigger needed to be taken by the end of the week. The Authority has seen no evidence that this urgency was passed on to WIM: instead, on **4 April 2019**, Link told WIM only that the WEIF should be brought out of the trigger *"as soon as practicable"*, and that the Buckets 3 and 4 metric was *"concerning"*.

4.87. On **26 April 2019**, Link identified a breach of the Buckets 3 and 4 limit, with Link measuring the metric as 70.01% of NAV, compared to the 70% limit. Link noted, in correspondence with WIM, that WIM had notified them of the upcoming expected breach of the limit and was already taking action to bring the metric back below the limit. Given the steps outlined by WIM, Link told WIM that they did not see a need for further action in relation to the breach.

4.88. On **22 May 2019**, Link told WIM on a call that they were very concerned about the level of fair value assets and the WEIF's liquidity profile. The next day, it was noted internally that *"reality is beginning to dawn on Woodford* [i.e. WIM] *and they are at last looking to sell less liquid stocks"*.

4.89. However, by this point, as recalculated using the reasonable and appropriate parameters of a 25% Participation Rate and the Linear Allocation Approach:

(a) the proportion of the WEIF's holdings that were classified as Bucket 1 decreased from a high point of 27% in September 2017 to a low point of 8% in May 2019;

(b) the proportion of the WEIF's holdings that were classified as Buckets 3 and 4 increased from a low point of 50% in May 2017 to a high point of 74% in May 2019; and

(c) the proportion of the WEIF's holdings that were classified as Bucket 4 increased from a low point of 23% in May 2017 to a high point of 41% in May 2019.

4.90. If a Participation Rate of 20% is adopted, the position was as follows:

(a) the proportion of the WEIF's holdings that were classified as Bucket 1 decreased from a high point of 23% in September 2017 to a low point of 7% in May 2019; and

(b) the proportion of the WEIF's holdings that were classified as Buckets 3 and 4 increased from a low point of 53% in September 2017 to a high point of 77% in May 2019.

(c) the proportion of the WEIF's holdings that were classified as Bucket 4 increased from a low point of 25% in May 2017 to a high point of 45% in December 2018.

4.91. Further, each of the T+ Metrics had followed a clearly declining trend from January 2018 (at the latest) to the end of the Relevant Period, with the proportion of the WEIF's securities that were liquidable, based on assessments conducted, within:

(a) 1 day decreasing from 5% in May 2017, to 2% in September 2018 to 1% in May 2019;

(b) 5 days decreasing from 20% in September 2017, to 11% in September 2018 to 6% in May 2019; and

(c) 20 days decreasing from 45% in September 2017, to 31% in September 2018 to 23% in May 2019.

4.92. Yet further, by May 2019, based on assessments conducted, WEIF would have taken:

(a) 5 days to liquidate 5% of its NAV (compared with 2 days in May 2017);

(b) 9 days to liquidate 10% of its NAV (compared with 3 days in May 2017); and

(c) 17 days to liquidate 20% of its NAV (compared with 6 days in May 2017).

4.93. On **31 May 2019**, KCC informed WIM it would be redeeming in full its holding in the WEIF. In the days following this request, Link liaised with WIM concerning options to meet the redemption which was valued at £237 million (6.5% of NAV) at that time. After considering a number of options, on **3 June 2019**, Link concluded that immediate suspension was the appropriate response in order to protect the interests of investors in the WEIF.

SECTION D: UNQUOTED SECURITIES AND LISITNGS ON THE INTERNATIONAL STOCK EXCHANGE

<u>WEIF's investments in Unquoted Securities</u>

4.94. The WEIF invested in a number of Unquoted Securities whose shares were not listed and traded on an exchange.

4.95. Between October 2014 and October 2015, WEIF invested in Benevolent, Industrial Heat, Ombu and Sabina ("the TISE companies" or "the TISE securities"), which were all, when the investments were first made, Unquoted Securities:

	Initial investment Date
Benevolent	17 October 2014
Industrial Heat	13 May 2015
Ombu	28 October 2015
Sabina	17 December 2015

4.96. As a part of WIM's investment into the TISE companies, WIM made commitments to provide further funding to the TISE companies via future share subscriptions.

4.97. In August 2017, WIM entered a moratorium on any further investments in Unquoted Securities, as the WEIF was approaching the 10% limit. By the end of November 2017, the percentage of Unquoted Securities held by WEIF stood at 9.82%.

4.98. Unknown to Link, WIM notified each of the TISE companies in the first instance about the issues arising from the funding moratorium as well as the WEIF nearing the 10% limit. WIM was unable to provide further funding to the TISE companies unless the securities held by the WEIF became listed, meaning that they would no longer be covered by the 10% limit. Subsequently, each of these 4 companies listed shares in their companies on TISE, the listings occurring as set out below:

Company	**Date of listing**	**Stock exchange**
Sabina	28 December 2017	TISE
Ombu	15 June 2018	TISE
Industrial Heat	5 October 2018	TISE
Benevolent	21 March 2019	TISE

4.99. Notwithstanding their listing, prior to the suspension of the WEIF on 3 June 2019, there were no arm's length market dealings in any of the TISE securities, and only one trade recorded for any of the TISE securities, that being a trade involving Sabina shares with the WEIF acquiring shares from the Woodford Patient Capital Trust (another fund managed by WIM).

4.100. Link was of the view that the TISE listings had no effect on the WEIF's overall liquidity profile, as they would remain categorised as Bucket 4 securities even after listing. Link was also aware, prior to the relevant listings, that the TISE securities were likely to be, at most, thinly traded, if traded at all. Other than Ombu, the only shares listed were those held by the WEIF. In these circumstances, the listing of these securities did nothing to improve the liquidity profile of the WEIF. This was recognised by Link. It was also recognised by Link that whilst, in the short term, the TISE listings had no effect on the liquidity profile of the WEIF, on a longer-term basis the TISE listings enabled WIM to: (a) reduce pressure on the 10% Unquoted

Securities limit; (b) increase the size of the securities which were either unquoted or otherwise subject to FVP; and (c) hold further securities which, in terms of liquidity, had the same characteristics as the Unquoted Securities.

4.101. Although ACDs are not usually expected to be involved in an underlying asset's corporate actions, including listing on exchange, Link failed to give consideration to the potential implications for the WEIF's liquidity profile, as outlined above, where businesses which the WEIF had holdings in announced an intention to convert from unlisted status to becoming listed on an exchange.

4.102. The WEIF also held shares in a further Unquoted Security, Proton Partners (that subsequently became Rutherford Health), initially purchased in January 2015. Subsequent to this, Proton Partners issued shares to the WEIF which were listed on the NEX exchange in February 2019. The issue of shares, and the subsequent listing, meant that the shares were removed from WEIF's Unquoted Securities total. Although listed, there was no market for pricing purposes, and only one trade was ever made. Proton Partners continued to be valued by Link using FVP after it was listed on NEX.

4.103. As well as enabling the WEIF to continue to hold the Unquoted Securities noted above, the listings also enabled the further investment of the WEIF's funds into them. The proportion of the WEIF's portfolio that comprised securities that were valued using FVP (including all but 2 of the Unquoted Securities) increased significantly from 8.8% in May 2017 to 21.5% in May 2019. This added to the deterioration to WEIF's overall liquidity.

SECTION E: THE AUTHORITY'S ANALYSIS OF THE WEIF'S LIQUIDITY DURING THE RELEVANT PERIOD

<u>Overview</u>

4.104. The Authority has assessed the WEIF's liquidity over the Relevant Period by reference to a statistical model based on the historical trading data for the securities in which the WEIF and peer funds invested (the "Statistical Model"). The Statistical Model uses data relating to the monthly composition of the funds, as well as data on the investments each fund held (the number of shares, their value, and their average daily trading volume), in order to ascertain:

(a) relevant liquidity metrics for the WEIF and the comparator funds;

(b) the effect of stressed scenarios on the WEIF; and,

(c) the time it would take to liquidate various percentages of the portfolios held by the WEIF and comparator funds.

4.105. In summary, the Statistical Model shows:

(a) Link's contemporary liquidity calculations were flawed. In particular, they inappropriately assumed a Participation Rate of 100%.

(b) Liquidity in the WEIF was deteriorating by reference to the contemporary metrics of which Link was aware:

a. Even on the results of Link's contemporary calculations, it was clear that liquidity in the WEIF was deteriorating.

b. Had Link adopted appropriate assumptions in calculating those liquidity metrics, it would have identified that the liquidity profile of the WEIF deteriorated significantly during the Relevant Period.

c. This deterioration in liquidity came about because redemptions tended to be met by liquidating the more liquid assets first (rather than because of a disproportionate increase in the value of the more illiquid securities).

4.106. There were further indicators which Link did not contemporaneously monitor (in particular: the time it would have taken to liquidate certain proportions of the NAV; the Amivest metric after September 2018; and WIM's calculation of the Initial T+20 Metric after September 2018), which establish that the liquidity of the WEIF was deteriorating. Had Link been in any doubt as to the deteriorating liquidity position (which it should not have been), these indicators would have confirmed the position beyond doubt.

4.107. The proportion of the WEIF invested in Unquoted Securities was generally within the 9.5% limit set by Link. While the proportion of the WEIF's portfolio that comprised Unquoted Securities remained broadly stable during the Relevant Period, that calculation excluded securities which were quoted but which were subject to FVP, and so did not capture the true amount of the WEIF assets which were not readily tradeable. The WEIF's securities which were subject to FVP were a driving factor in the deterioration of the WEIF's liquidity, and the proportion of the WEIF's portfolio that comprised such securities increased during the Relevant Period.

4.108. The stress-testing conducted by Link was inadequate. Had adequate stress-testing been conducted, it would have become apparent that the WEIF was not able to withstand certain stressed but plausible scenarios. In particular, Link's stress testing failed to test for the possibility of KCC redeeming *alongside* other redemptions at the largest retail redemption rate over the preceding 5-day period. Had that stress-testing (or stress-testing using similar appropriate parameters) been conducted, it would have shown that, from 1 September 2018, the WEIF would have been unable to meet its required redemptions in such plausible circumstances.

4.109. The WEIF was an outlier in terms of its liquidity, and among the least liquid of comparable funds, and on a number of metrics, the least liquid.

4.110. Each of these six findings is addressed in more detail immediately below.

<u>Inappropriate Assumptions and data issues</u>

4.111. The metrics used to measure the liquidity of the WEIF during the Relevant Period were not reasonable and relied upon inappropriate assumptions:

(a) First, as to the assumption of a 100% Participation Rate:

a. That assumption was not realistic, because it assumed that a single entity could access the entire liquidity in respect of a particular security without significantly impacting the price of that security.

b. Link suggested that the use of the unrealistic 100% Participation Rate was offset by the use of another unrealistic (but supposedly overly-prudent) measure – a Full Allocation Approach. The Statistical Model shows that these two partly offsetting assumptions resulted in a model that failed to reflect the liquidity of the underlying assets; and in the liquidity profile of the WEIF generally appeared better than it would have done without employing those assumptions.

(b) Secondly, as to the ADTV for the Four Bucket Model:

a. It was not appropriate to fix the ADTV at the traded volume in March 2017 (in respect of the Pre-September 2018 Period). This would have provided an increasingly outdated view on liquidity.

(c) Thirdly, Link used an incorrect data source for its liquidity calculations. The data relied on was based on the *"ALL_BROKERS_ADV_TOT_AGGR _VOL"* Bloomberg field, which reflects the total volume of shares advertised by all brokers for one specific exchange, and not the total volume of shares traded across all exchanges a security is quoted on, which is one of the assumptions underpinning metrics used to monitor liquidity i.e. that the ADTV was sourced from all exchanges.

(d) Fourthly, in relation to the Amivest Score, Link did not limit the assumptions to the amount of a security that could be sold.

<u>Deterioration of the WEIF's Liquidity during the Relevant Period</u>

4.112. This section sets out the WEIF's liquidity position as assessed both contemporaneously, and by reference to the Statistical Model. In respect of each metric, either (1) the contemporaneous calculation showed liquidity to be deteriorating, and once the inappropriate assumptions are corrected, that deterioration is shown to have been even worse; or (2) the contemporaneous calculation did not show liquidity to be deteriorating, but once the inappropriate assumptions are corrected, that is shown to have been false.

<u>The Liquidity Buckets</u>

As Calculated by Link

4.113. Based on the metrics set out in the Link liquidity reports, Link's own calculations demonstrated that the liquidity of the WEIF deteriorated significantly:

(a) Applying the *Five Category Model:*

a. In February 2018, the assets liquidable in: (i) one day represented 2% of the WEIF's NAV; (ii) between two and seven days represented 38% of the WEIF's NAV; and (iii) eight days or more(referred to by Link as the *"illiquid rump"*) represented 58% of the WEIF's NAV.

b. In September 2018, 100% of the WEIF's NAV would take eight days or more to liquidate (i.e. under this model the entire fund classified as an *"illiquid rump"*).

(b) *Applying the Revised Four Bucket Model:*

a. Bucket 1 assets decreased from 14% to 8% of the WEIF's NAV between September 2018 and April 2019;

b. Bucket 2 assets remained broadly consistent throughout the period, ranging from 24% to 29% of the WEIF's NAV;

c. Bucket 3 assets decreased from 36% of the WEIF's NAV in September 2018 to 32% in April 2019; and

d. Bucket 4 assets increased from 25% of the WEIF's NAV in September 2018 to 33% in April 2019.

4.114. This led to breaches of applicable triggers and limits (as contemporaneously calculated by Link), as follows:

(a) In September 2018, the WEIF breached the 35% limit for Bucket 4;

(b) In December 2018, the WEIF breached the 65% trigger for Buckets 3 and 4 combined;

(c) In March 2019, the WEIF breached the 65% trigger for Buckets 3 and 4 combined; and

(d) In April 2019, the WEIF breached the 70% limit for Buckets 3 and 4 combined.

The Four Bucket Model as re-calculated using the Statistical Model

4.115. If the Four Bucket Model is applied using appropriate assumptions, the WEIF's liquidity deterioration is even more acute.

4.116. First, using a 25% Participation Rate and the Linear Allocation Approach:

a) During the Relevant Period:

a. the proportion of the WEIF's holdings that were classified as Bucket 1 decreased from a high point of 27% in September 2017 to a low point of 8% in May 2019;

b. the proportion of the WEIF's holdings that were classified as Buckets 3 and 4 increased from a low point of 50% in May 2017 to a high point of 74% in May 2019; and

c. the proportion of the WEIF's holdings that were classified as Bucket 4 increased from a low point of 23% in May 2017 to a high point of 41% in May 2019.

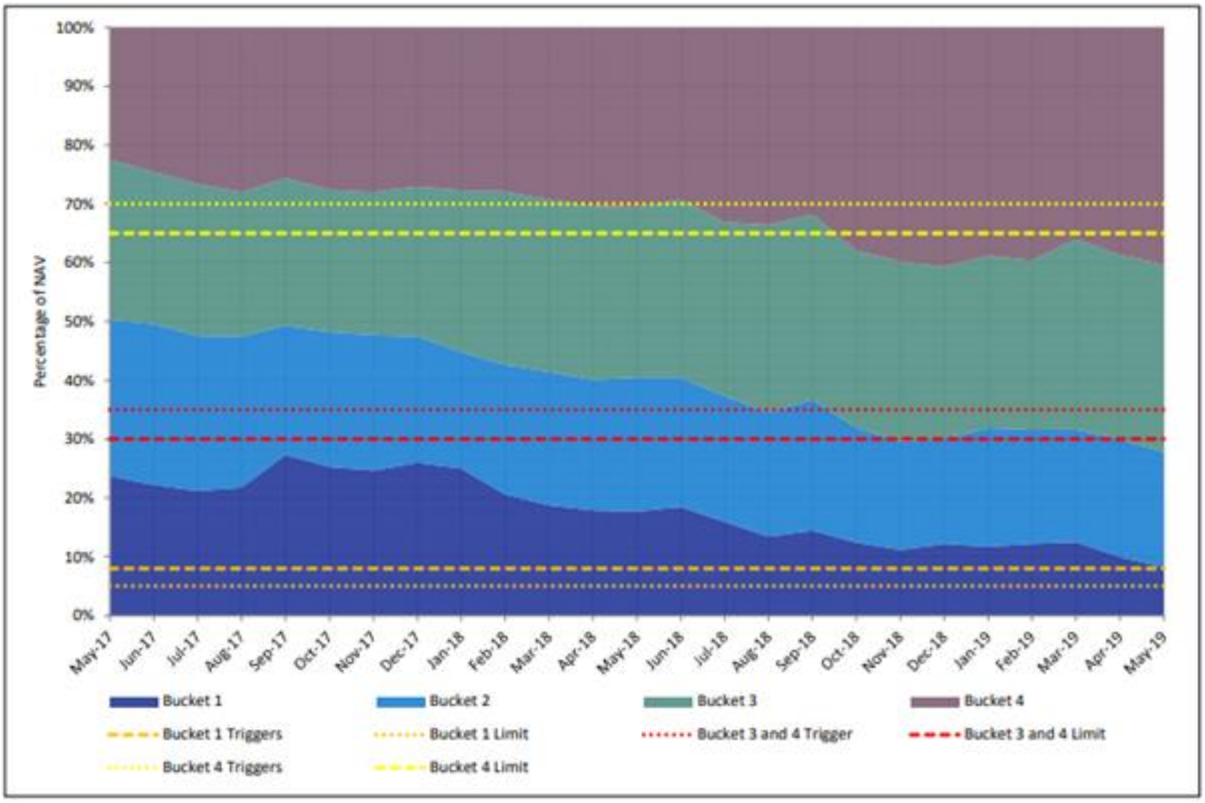
(b) Further, the thresholds set by Link in respect of the Liquidity Buckets were breached:

a. In respect of Buckets 3 and 4, the trigger was continuously breached from October 2018; and the limit in November and December 2018, and April and May 2019.

b. In respect of Bucket 4, the trigger was continuously breached from July 2018, and the limit from October 2018.

(c) These points are illustrated in the diagram set out below:

<u>Chart 4</u>



4.117. Second, using a 20% Participation Rate and the Linear Allocation Approach:

(a) During the Relevant Period:

a. the proportion of the WEIF's holdings that were classified as Bucket 1 decreased from a high point of 23% in September 2017 to a low point of 7% in May 2019;

b. the proportion of the WEIF's holdings that were classified as Buckets 3 and 4 increased from a low point of 53% in September 2017 to a high point of 77% in May 2019; and

c. the proportion of the WEIF's holdings that were classified as Bucket 4 increased from a low point of 25% in May 2017 to a high point of 45% in December 2018.

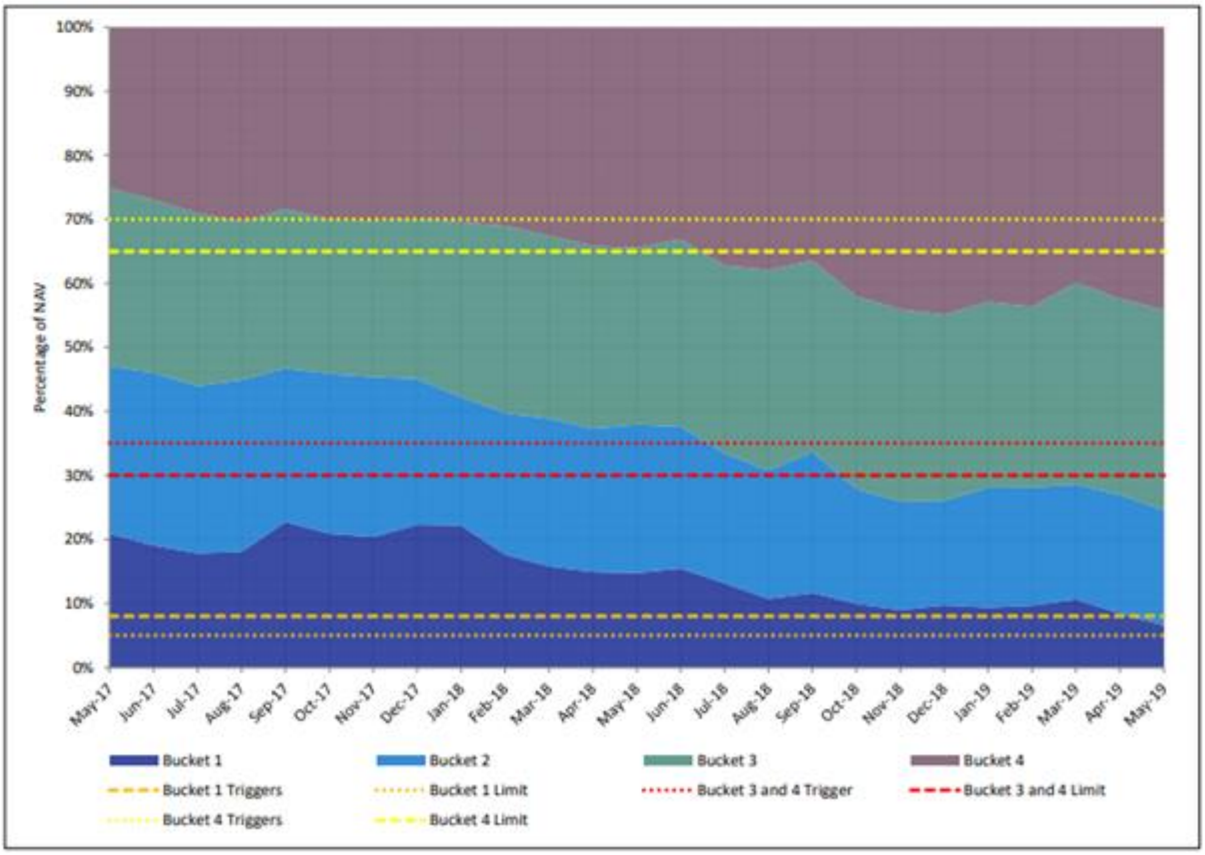
(b) Further, the thresholds set by Link in respect of the Liquidity Buckets were breached:

a. In respect of Buckets 3 and 4, the trigger was continuously breached from July 2018, and the limit was breached in August 2018 and then continuously from October 2018; and

b. In respect of Bucket 4, the trigger was breached in August, September and October 2017, and then continuously from January 2018; while the limit was breached in April 2018 and then continuously from July 2018.

(c) These points are illustrated in the diagram set out below:

<u>Chart 5</u>



4.118. The deterioration of the liquidity of the WEIF was primarily due to the lack of "vertical slicing" over time; however, instead the WEIF disproportionately liquidated the most liquid assets first (from Buckets 1 and 2) while retaining more illiquid assets (from Buckets 3 and 4).

The T+ Metrics

4.119. The T+1, T+5 and T+20 Metrics as analysed by Link remained broadly consistent throughout the Relevant Period.

4.120. Analysed through the Statistical Model, the true position was that each of the T+ Metrics assessed by Link clearly followed a declining trend from January 2018 (at the latest) to the end of the Relevant Period, with the proportion of the WEIF's securities that were liquidable, under the model used, within:

(a) 1 day decreasing from 5% in May 2017, to 2% in September 2018, to 1% in May 2019;

(b) 5 days decreasing from 20% in September 2017, to 11% in September 2018, to 6% in May 2019; and

(c) 20 days decreasing from 45% in September 2017, to 31% in September 2018, to 23% in May 2019.

4.121. Moreover, WIM's calculation of the Initial T+20 metric (which used a 20% Participation Rate) showed a deterioration from around September 2017, and would have shown a continuous breach of the trigger and persistent breaches of the limit applicable prior to September 2018 from August 2018 and September 2018 respectively, had those thresholds been maintained.

The Redemption Metrics

Amivest

4.122. As calculated by Link up until August 2018, the Amivest Score did not breach the then-applicable limit of 30bps. After August 2018, Link did not calculate the Amivest Score.

4.123. However, the Amivest Score as calculated by Link did not adequately reflect changes in the liquidity profile of the WEIF. In particular, this was because Link did not limit their assumptions to the amount of a security which could be sold. Recalculated to correct for that inappropriate assumption, the limit of 30bps would have been breached in 13 months across the whole of the Relevant Period.

The RCR

4.124. The RCR of the WEIF broadly declined over the Relevant Period and first breached:

(a) the limit (and accordingly the trigger) in May 2019 for the 1-day and 5-day RCR; and

(b) the limit (and accordingly the trigger) in March 2019 for the 20-day RCR.

<u>Conclusion</u>

4.125. Accordingly, each of the metrics monitored by Link contemporaneously either showed a deterioration in liquidity, or would have done so (or would have done so more accurately), had it been calculated appropriately.

4.126. In particular, if Link had used a Participation Rate of 25% and Linear Allocation, the WEIF would have breached thresholds in respect of the Liquidity Buckets in April and May 2018, and continuously from July 2018.

<u>Other Indications of Deteriorating Liquidity</u>

Time to Liquidate

4.127. Had Link considered the time which it would have taken to liquidate various portions of the WEIF (which would have been appropriate, given the level of redemption), it would have identified that, during the Relevant Period, the time it would have taken to liquidate portions of the portfolio (either 5%, 10% or 20%) increased significantly from August 2018. In particular, the WEIF would have taken:

(a) 2 days to liquidate 5% of its NAV between May 2017 and July 2018. This increased to 5 days by May 2019.

(b) 3 days to liquidate 10% of its NAV in May 2017. This increased to 9 days by May 2019.

(c) 6 days to liquidate 20% of its NAV in May 2017. This increased to 18 days by May 2019.

The Amivest Redemption Metric

4.128. Had the Amivest metric continued to apply post-September 2018, the threshold of 30bps would have been breached in 13 months of the Relevant Period (as set out at paragraph 4.123 above).

WIM's Calculation of the T+20 Metric

4.129. Had the thresholds applicable to WIM's calculation of the Initial T+20 Metric been maintained throughout the Relevant Period, there would have been a continuous breach of the trigger and persistent breaches of the limit from August 2018 and September 2018 respectively on WIM's own contemporaneous calculations (as set out at paragraph 4.121 above).

<u>Unquoted Securities</u>

4.130. The portfolio data for the WEIF provided by Link shows the proportion of the NAV that was invested in Unquoted Securities decreased between September 2017 and February 2019. However:

(a) The percentage of Unquoted Securities in the WEIF was more than 8.5% of the NAV (the initial Link limit) for almost the entirety of the Relevant Period, except for March to August 2018.

(b) The percentage of Unquoted Securities in the WEIF also breached Link's second internal limit (of 9.5%) in August to November 2017, January to February 2018, September 2018 and June 2019.

4.131. The proportion of the WEIF's portfolio that comprised Unquoted Securities did in fact remain broadly stable during the Relevant Period, with the WEIF breaching the initial Link limit of 8.5% at month-end in 20 of 26 months during the Relevant Period, and breaching the second limit of 9.5% at month-end in 8 of 26 months.

4.132. In addition to the breaches of Link's internal limits for Unquoted Securities, the WEIF also breached the regulatory limit of 10% on three occasions during the

Relevant Period. The three occasions were 21 November 2017, 2 February 2018 and 6 March 2018.

4.133. However, securities which were quoted but which were subject to FVP were excluded from the calculation of Unquoted Securities, and so the calculation did not capture the true amount of the WEIF's assets which were not readily tradeable. In this respect:

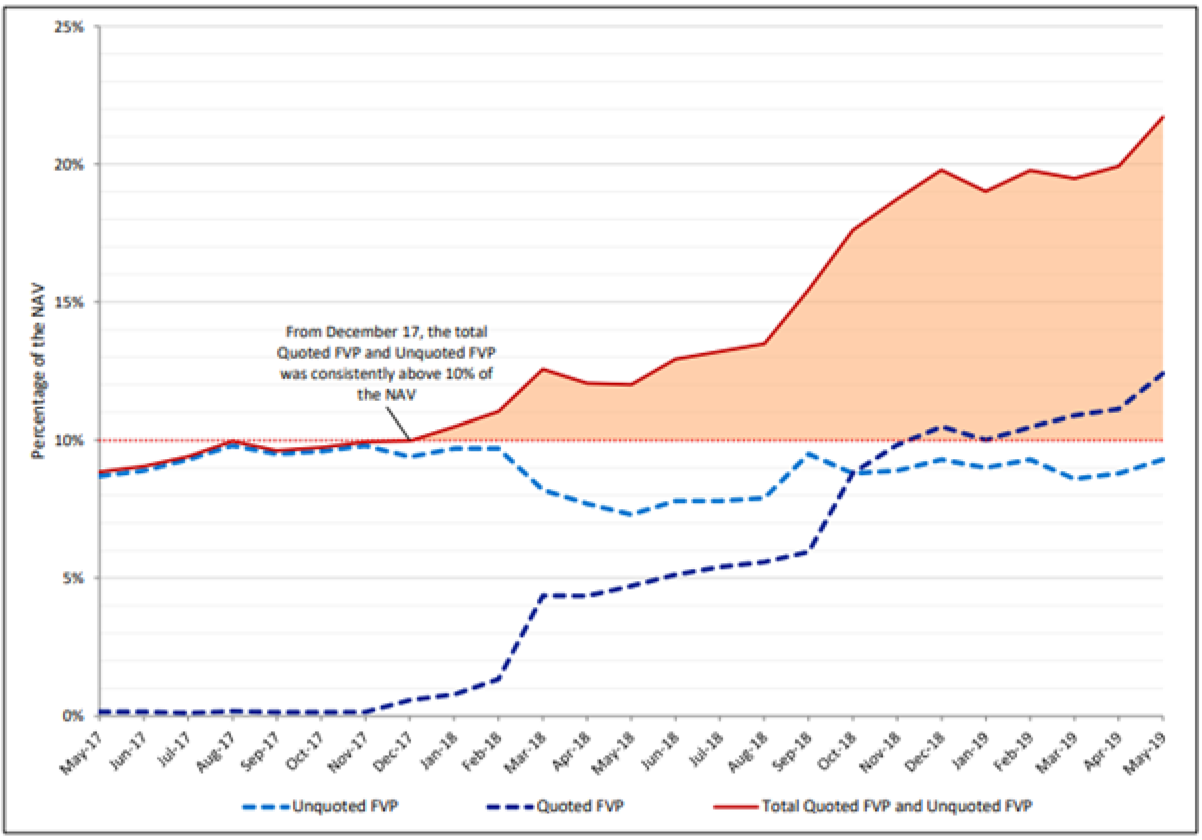
(a) The percentage of securities that were quoted but were subject to FVP increased significantly between May 2017 (when they represented 0.2% of the NAV) and May 2019 (when they represented 12.4% of the NAV).

(b) When the quoted securities and Unquoted Securities that were subject to FVP are combined, they increased significantly in the Relevant Period from 8.8% in May 2017 to 21.5% in May 2019. This appears to have been a driving factor in the deterioration of the WEIF's liquidity.

(c) From December 2017, the quantity of securities classified both as unquoted, and quoted but subject to FVP, continuously exceeded 10% of the NAV.

4.134. The impact of the significant increase in securities subject to FVP is illustrated in the chart below (the 10% breaches noted in paragraph 4.132 above are intra month so do not appear on the chart):

Chart 6



Inadequate Stress Testing

4.135. The stress-testing conducted by Link was inadequate. Had adequate stress-testing been conducted, it would have become apparent that the WEIF was not able to withstand certain stressed but plausible scenarios.

ADTV Stresses

4.136. The stressed scenarios used by Link for stress-testing were not statistically representative of stressed but plausible scenarios for the ADTV of the securities in which the WEIF had invested.

4.137. Link performed stress testing by stressing the ADTV of securities held by the WEIF by 20% for Large Cap securities and 40% for Mid Cap and Small Cap securities. However, this approach did not encompass the stresses to which the WEIF might plausibly have been exposed. In fact, on proper analysis:

(a) For the Large Cap securities, the chance of a 20% decrease in the ADTV was between one in seven and one in five.

(b) For the Mid Cap securities, the chance of a 40% decrease in the ADTV was between one in 20 and one in 10.

(c) For the Small Cap securities, the chance of a 40% decrease in the ADTV was between one in five and one in four.

4.138. None of these represent sufficiently unlikely scenarios to provide an appropriate proxy of *"stressed but plausible"* scenarios for the ADTV of the securities held by the WEIF.

Redemption Stress Rates

4.139. After September 2018, Link performed stress testing on the RCR by modelling the impact of redemptions of 10%, 15% and 20% of the portfolio. However, this stress testing failed to test for the possibility of KCC redeeming *alongside* other redemptions at the largest retail redemption rate over the preceding 5-day period. Had such a stress-test (or stress-testing using similar appropriate parameters) been performed, based on assessments conducted, it would have shown that, from September 2018, the WEIF would have been unable to meet redemptions in these circumstances.

Combined Stresses on ADTV and Redemption Rate

4.140. Had the stress-testing been conducted for the plausible eventuality of combined stress on ADTV and the largest retail redemption rate over the preceding 5-day period, it would have revealed that the trigger set by Link in respect of the 5-day RCR was breached throughout the Relevant Period under *all* of the scenarios analysed.

Comparison with Other Funds

4.141. The WEIF was significantly less liquid than comparator funds. As set out below, on a number of metrics, it was the least liquid fund when compared against 225 comparable funds.

4.142. First, applying the Four Bucket Model using the Statistical Model to the comparator funds:

(a) Bucket 1**:** From July 2018 to the end of the Relevant Period, the proportion of the WEIF's securities that were allocated to Bucket 1 (and therefore liquidable within 7 days) deteriorated from 18% to 8%, which was significantly lower than the bottom ranked fund.

(b) Buckets 1 and 2: From October 2017 onwards, the proportion of the WEIF's securities that were allocated to Buckets 1 and 2 (and therefore liquidable within 30 days) were amongst the least liquid 5% of the comparable funds.

(c) Buckets 1, 2 and 3: From January 2018 onwards, the proportion of the WEIF's securities that were allocated to Buckets 1, 2 and 3 (and therefore liquidable within 180 days) were amongst the least liquid 5% of the comparable funds.

4.143. Second, applying the T+ Metrics to comparator funds:

(a) T+5 Metric: From July 2018 for the remainder of the Relevant Period, the proportion of the WEIF's securities that were liquidable in 5 days deteriorated from 12% to 6%, which was significantly lower than the bottom ranked comparable fund.

(b) T+10 Metric: From July 2018 for the remainder of the Relevant Period, the proportion of the WEIF's securities that were liquidable in 10 days deteriorated from 22% to 12%, which was significantly lower than the bottom ranked comparable fund.

(c) T+20 Metric: From October 2018 for the remainder of the Relevant Period, the proportion of the WEIF's securities that were liquidable in 20 days deteriorated from 25% to 22%, which meant that the WEIF was amongst the least liquid 5% of the comparable funds.

4.144. Third, the WEIF was also significantly less liquid than most comparator funds when assessed by reference to how long it would take to liquidate various percentages of the NAV of the WEIF:

(a) The WEIF would have taken significantly longer to liquidate 5% of its NAV than comparable funds, with the position worsening from August 2018. For example, 95% of the comparable funds could liquidate 5% of their NAV within 1 day, whereas the WEIF took between 2 and 5 days to liquidate 5% of its NAV.

(b) The WEIF would have taken longer to liquidate 10% of its NAV than comparable funds, with the position worsening significantly from July 2018. For example, 95% of the comparable funds could liquidate at least 10% of their NAV within between 1 and 2 days, whereas the WEIF took between 3 and 9 days to liquidate 10% of its NAV.

(c) The WEIF would have taken longer to liquidate 20% of its NAV than comparable funds (being in the bottom 1% of such funds), with the position worsening significantly from July 2018.

(d) Accordingly:

a. The time it would have taken to liquidate the WEIF's NAV was significantly longer than would have been the case for the comparable funds. At least 50% of those funds could liquidate up to 20% of their NAVs within 1 day, compared with between 5 and 18 days for the WEIF; and

b. From July 2018, the time it would have taken the WEIF to liquidate 5%, 10% and 20% of its NAV significantly increased and it consistently would have taken the WEIF significantly longer to liquidate 5% and 10% of its NAV than the bottom ranked comparator fund.

4.145. Fourth, during the Relevant Period, the WEIF experienced the worst performance of the least liquid comparator funds until September 2018, when its performance was in line with just one other fund. For that reason, compared to its peers, the WEIF had a heightened liquidity risk throughout the Relevant Period.

Impact on ability of investors to redeem

4.146. In the circumstances, the Authority considers that the WEIF's liquidity profile deteriorated significantly during the Relevant Period and that Link's failings (as particularised in the Failings section immediately below): (a) materially contributed to the risk that suspension would be required; and (b) placed those investors who did not redeem prior to the point of suspension at a disadvantage.

4.147. The 'first mover advantage' for those redeeming earlier was exacerbated by the failure of Link to adequately monitor how redemptions were being met by WIM and to help prevent further deterioration of liquidity. More liquid assets were sold to meet redemptions exacerbating the decline in liquidity. Link could have done this in a number of ways including requiring assets to be sold down equally across the liquidity profile, referred to as vertical slicing. This would have prevented a disproportionate sale of the most liquid assets. Had vertical slicing been required by Link, the WEIF's liquidity would not have deteriorated in the manner in which it did.

4.148. Suspension was not something Link had adequately considered. This resulted in urgent consideration being given to options following the KCC redemption. Had suspension occurred earlier, it would have been likely to provide better outcomes for investors than the outcomes resulting from the suspension which occurred. Link's failure to proactively consider and plan for the possibility of suspension was a significant failing on its part.

4.149. In a similar way to failure to consider suspension, the failure by Link to understand the significance of the liquidity problems meant that it also failed to proactively and appropriately manage what information should be provided to unitholders and putative investors about the increased risks caused by holding large levels of illiquid assets. Whilst Link should have been running the fund in a way which avoided the risks which arose, the fact that it failed to appreciate the scale of risk meant that it missed opportunities to appropriately update investors and the Authority's supervisors in any informed way about the increased risks.

5. FAILINGS

5.1. The statutory and regulatory provisions relevant to this Notice are referred to in Annex A.

5.2. By reason of the facts and matters set out above, during the period from 31 July 2018 to 3 June 2019, Link breached:

(a) Principle 2 (skill, care and diligence);

(b) Principle 6 (fair treatment of customers);

<u>Failings in respect of the WEIF's liquidity profile</u>

5.3. By 31 July 2018, the WEIF's liquidity profile was unreasonable and inappropriate in light of the redemption policy in the fund prospectus. In particular, as set out in section E above:

(a) Had Link adopted, as it should have done, an appropriate Participation Rate (even assuming it also altered the allocation method) for its Liquidity Bucket Metric, the thresholds which it had set for that metric would have been breached from July 2018 (if Link had used the 25% Participation Rate and linear allocation method it used for the T+ and Redemption Metrics) and from January 2018 (if Link had used the 20% Participation Rate and linear allocation method).

(b) There were other indications which Link contemporaneously monitored and of which Link was aware throughout the Relevant Period which clearly indicated that the liquidity of the WEIF was deteriorating and imprudent.

(c) There were further indications which Link did not contemporaneously monitor that establish that the liquidity of the WEIF was deteriorating and imprudent. Had Link been in any doubt as to the deteriorating and inappropriate liquidity position (which it should not have been), it should have conducted further investigations which would have identified these indications and confirmed the position beyond doubt. This deterioration in liquidity (and the consequent breaches) came about in part because redemptions tended to be met by liquidating the more liquid assets first (rather than because of a disproportionate increase in the value of the more illiquid securities).

(d) The stress-testing conducted by Link was inadequate. Had adequate stress-testing been conducted, it would have become apparent that the WEIF was not able to withstand stressed but plausible scenarios. In particular, Link's stress testing failed to test for the possibility of KCC redeeming *alongside* other redemptions at the largest retail redemption rate over the preceding 5-day period. Had that stress-testing (or stress-testing using similar appropriate parameters) been conducted, it would have shown that from 1 September 2018, the WEIF would have been unable to meet its required redemptions in such plausible circumstances.

(e) The WEIF was an outlier and among the least liquid of comparable funds:

a. the proportion of the WEIF's securities that were easily liquidable (i.e. within 7 days) was significantly lower than that of comparable funds throughout the Relevant Period; and

b. from August 2018, and for the remainder of the Relevant Period, the WEIF's liquidity was lower than the bottom ranked comparable fund in a number of respects.

(f) In all the circumstances, based on the indications that Link contemporaneously monitored and the stress testing that it in fact carried out, together with the implications of sustained and significant diminution of NAV over an extended period of time, Link should have appreciated that there were compelling signs that liquidity was a significant issue in the context of the WEIF's redemption requirements and that urgent and significant action should have been taken to reduce risks to remaining unitholders.

5.4. In these circumstances, those investors who redeemed between November 2018 and 3 June 2019 were treated more favourably than the remaining investors. Given the continued trend of redemptions (outflows) exceeding subscriptions (inflows) and no obvious reason for this to change, it was apparent that redemptions would continue to be met by the sale of the more liquid assets, which had been the pattern over the previous 18 months. Urgent steps to rebalance the portfolio should have been taken to ensure fairness to all investors, not just those seeking to redeem.

5.5. LFS failed to appreciate the urgency of the situation or to consider the possibility of suspension, with the KCC redemption request appearing to be the first and only point at which it had become aware that suspension might be needed. This was despite the fact that once the WEIF's liquidity profile had deteriorated to an unreasonable extent Link should have been considering the full range of options to protect investors.

5.6. The prospectus for the WEIF included various provisions which could be used to manage liquidity, including use of notice periods and suspension. Whilst suspension because of poor liquidity management should never normally need to occur, at no stage prior to the KCC redemption did Link sufficiently consider taking this step to protect the remaining unitholders. This exposed remaining unitholders to detriment caused by first mover advantage when others redeemed their holdings. The fact that the need to suspend was not sufficiently considered by Link before the KCC redemption increased the harm to remaining investors. Given the precarious state of the WEIF's liquidity over an extended period of time, Link should have at least considered whether suspension was required at an earlier date in order to protect unitholders from harm. Link's failure to proactively consider and plan for the possibility of suspension was a significant failing on its part.

5.7. Similarly to the failure to consider suspension, the failure by Link to understand the significance of the liquidity problems meant that it also failed to proactively manage what information should be provided to unitholders and putative investors about the increased risks caused by holding large levels of illiquid assets. Whilst Link should have been running the WEIF in a way that avoided the risks which arose, the fact that it failed to appreciate the scale of risk meant that it was unable to appropriately update investors and supervisors of the Authority in any informed way about the increased risks. Had Link recognised the problems earlier, it could have taken appropriate action, including how to keep investors appropriately informed about the emerging issues. The fact that suspension was a surprise to investors, as well as to others, increased the impact to unitholders most of whom were retail investors unable to access their money, when many would have been reliant upon the money held within the WEIF.

5.8. Link was reliant upon WIM to update it on individual investors and their intentions. This included KCC. Had Link been more proactive in understanding the likelihood of redemptions, it would have been able to manage this redemption and others better. It was also naïve of Link to rely upon a view that, if KCC redeemed, it would do so in tranches rather than in full.

5.9. The first mover advantage created by the poor liquidity was exacerbated by the failure of Link to adequately monitor how redemptions were being met by WIM and to help prevent further deterioration of liquidity which they could have done by requiring assets to be sold down equally across the liquidity profile. Had vertical slicing been required by Link, the WEIF's liquidity would not have deteriorated in the manner in which it did.

5.10. The liquidity thresholds were inappropriate in light of the redemption policy and metrics adopted. They were set in such a way that action would only be required when it was already too late.

5.11. Link failed to consider suspension of the fund at an earlier stage to protect the remaining investors. Further, in October 2018, Link received an independent report which specifically highlighted a flaw with the WEIF's liquidity methodology. Again, Link failed to act. The consequence was that the WEIF's most liquid assets were realised to meet redemptions, unfairly leaving behind only the most illiquid assets for the remaining investors. This resulted in the further deterioration of the liquidity profile of the WEIF.

<u>Specific Failings in respect of Link's Analysis</u>

Inappropriate Participation Rates

5.12. Participation Rate: Link used a 100% Participation Rate for the WEIF in respect of its Liquidity Buckets Metric, however it adopted a Participation Rate of 25% in respect of its T+ and Redemption Metrics, and a 20% Participation Rate for the T+1 metric. No satisfactory explanation has been given for the use of the 100% Participation Rate. Insofar as Link has suggested that the use of this extreme and unrealistic metric was compensated for by its use of the supposedly balancing Full Allocation metric, this is incorrect as a matter of statistical analysis (and there is in any event no reason why the use of one unrealistic metric should be justified by the purportedly compensating use of another unrealistic metric). The Participation Rate assumption is a highly significant one:

(a) Had Link used a Participation Rate of 25% for the Liquidity Bucket Metrics (and assuming they had also altered the Full Allocation metric to a Linear Allocation metric), thereby mirroring its methodology for the T+ and Redemption Metrics, the thresholds that Link contemporaneously set against this metric would have been breached from July 2018.

(b) Had Link used a Participation Rate of 20% for the Liquidity Bucket Metrics (and assuming it had also altered the Full Allocation metric to a Linear Allocation metric), thereby mirroring its methodology for all other funds for which it acted as ACD at the time, the thresholds that Link contemporaneously set against this metric would have been breached from January 2018.

5.13. The use of inappropriate Participation Rates led to an unjustifiably positive assessment of the WEIF's liquidity.

5.14. The issue of the 100% participation rate formed subject of comment in a s166 report issued by a skilled person on 19 October 2018 in relation to various issues regarding the activities of Link. The skilled person observed in the report about the 100% market participation rate being an optimistic assumption in the context of a sell off. It also noted that the participation rate was outside the normal market practice, where 20-30% participation is typically assumed. Despite warnings contained in the skilled person's report of 19 October 2018 concerning the use of a 100% participation rate, and a recommendation that Link revisit this, no changes were made.

Inappropriate liquidity limits

5.15. As set out in paragraph 4.31 and 4.36 above, Link imposed the following liquidity limits on the WEIF's NAV during 2018:

(a) Bucket 1 (T+1 - T+7) – no lower than 5% ("amber" warning at 8%).

(b) Bucket 4 (T+181 - T+363+) – no higher than 35% ("amber" warning at 30%).

(c) Buckets 3 and 4 (T+31 – T+363+) – no higher than 70% ("amber" warning at 65%).

5.16. Link decided to suspend the fund in June 2019 and therefore had determined that the contingency plan was not the appropriate way to resolve the issues. Had the limits set been appropriate in practice, it should have been possible for Link to ensure that the contingency plans were workable and implemented before having to suspend. The fact that Link decided to suspend, rather than require initiation of the plans, demonstrates the inappropriateness of the red / amber limits being: (a) set at the level they were; and/or (b) calculated in the manner that they were, in particular by reference to the Participation Rates addressed in paragraphs 5.12 – 5.13 above.

Inappropriate Data Sources

5.17. Link used an incomplete data set for its liquidity calculations. The data relied on was based on the *"ALL_BROKERS_ADV_TOT_AGGR _VOL"* Bloomberg field, which reflects the total volume of shares advertised by all brokers for one specific exchange, and not the total volume of shares traded across all exchanges a security is quoted on.

Inappropriate ADTV Period

5.18. Link fixed the ADTV traded volume as at March 2017 for the Initial Four Bucket Model, which would have provided an increasingly outdated view on liquidity.

Inadequate stress testing

5.19. For the reasons set out in section E and paragraphs 4.135 – 4.140 and 5.3(d) above, the stress-testing conducted by Link was inadequate. In particular:

(a) more unlikely scenarios should have been used for the purposes of identifying stressed but plausible scenarios in respect of the ADTV of the securities held by the WEIF for the reasons set out at paragraphs 4.136 – 4.138 above; and

(b) the stress testing set out at paragraphs 4.139 – 4.140 above (or stress testing using similar appropriate parameters) should have been carried out. Had adequate stress-testing been conducted, it would have become apparent that the WEIF was not able to withstand stressed but plausible scenarios.

5.20. Without other market factors in play, the redemption of KCC, albeit a significant investor, should not have led to an "extreme" scenario if the WEIF had an appropriate liquidity profile. It should not have taken the actual redemption request by KCC for Link to recognise that the liquidity profile had become inappropriate. The potential need for a suspension if KCC redeemed its funds should, through adequate stress testing, have been appreciated well before the redemption occurred.

Specific Failings in Respect of Link's Supervision and Oversight of WIM

5.21. Link communicated to WIM as early as November 2017 that the WEIF's liquidity profile was becoming unbalanced with respect to Buckets 1 and 4 and that action needed to be taken such that the allocations to Bucket 4 could be reduced and Bucket 1 could be increased. However, the liquidity profile continued to deteriorate with there being a lack of "vertical slicing" of the portfolio as redemptions continued. The subsequent limits imposed by Link in May 2018 were meant to be a backstop position that prevented the liquidity of the WEIF from deteriorating any further, as liquidity had continued to deteriorate in early 2018, as more liquid securities were sold to meet redemptions of just over £1 billion in the first four months of the year. Instead, the limits became a framework (both at WIM and Link) within which the WEIF was run. They therefore became a key factor in preventing a fundamental rebalancing of the portfolio as WIM insisted on managing within the limits and Link failed properly to challenge WIM's approach and attitude. The inappropriate nature of the limits therefore failed to tackle the root cause of the issue, meaning that by June 2019 the WEIF held insufficient liquidity to be able to continue after KCC's redemption.

5.22. In particular, when Link approved the change in the Liquidity Bucket Metric in September 2018 from ADTV on the primary market in which a security was traded to the amended measure of the ADTV across all markets on which that security was traded, it should have recognised the fact that this required the relevant triggers and limits to be adjusted downwards to reflect the nature of the newly approved metric and ensured that this change was implemented.

5.23. Further, Link should have recognised that the new model involved ceasing to monitor or place reliance at all on the two metrics – Link's Amivest Metric and WIM's T+20 metric, which had hitherto been part of the monitoring programme and which were identifying, and were likely to continue (and did in fact continue) to identify breaches of what had been relevant triggers and limits.

5.24. Link should not have permitted the relevant Liquidity Metrics to be amended such that three relevant Metrics which had hitherto been part of the monitoring programme, and which were identifying, and were likely to continue to identify, breaches of what had been relevant triggers and limits, were altered or removed, with the result that the Liquidity Metrics purported to show that relevant triggers and limits were not, and were not likely to be, breached. This was particularly so in the light of the deteriorating performance and liquidity of the WEIF which clearly established that such a relaxation of prudency requirements was inappropriate.

5.25. In particular, Link should not have permitted what became the leading measure of liquidity (i.e. the 4-Bucket Liquidity Model) to be calculated by reference to unrealistic metrics (i.e. a 100% Participation Rate and a Full Allocation Method) which it did not apply to its other Contemporaneous Liquidity Metrics for the WEIF.

5.26. Further, having recognised and clearly communicated to WIM by its email of 20 September 2018 *"the need to improve the overall liquidity profile of the fund"* and for the *"fund to be rebalanced to a considerably more liquid profile",* Link failed to enforce and require the necessary actions to be taken to achieve this result, instead implicitly accepting and failing properly to challenge WIM's assertive communications that it did not agree with and had not agreed with this conclusion.

5.27. Despite asserting on 24 September 2018 that *"[Link] continue to press the need for a long term rebalancing of the portfolio to a more liquid overall profile as well as a reassessment and reformulation of an effective liquidity monitoring framework for [the WEIF]"* Link failed to ensure that appropriate steps were identified and actioned.

5.28. Having again informed WIM, on 26 September 2008, that WIM and Link needed to *"work together to formulate a proposal for a more refined liquidity management framework"* and *"acknowledge the need to rebalance the portfolio in the longer term (6m +) to a more balanced liquidity profile appropriate for a daily dealing UCITS fund",* and requiring WIM to *"advise [Link] of their plan to achieve this",* Link failed to enforce and require the necessary actions to be taken to achieve this result, instead implicitly accepting and failing properly to challenge WIM's assertive communications that it did not *"believe that there is a need to rebalance the portfolio to a more liquid one over the longer term".*

5.29. Further, having informed WIM on 10 December 2018 that *"[Link's] position is that we expect WIM to be undertaking prompt action to address … liquidity concerns with the ultimate goal of bringing the hard to value assets down from 19% to less than 10% and for the portfolio to return to a more balanced position between the four liquidity buckets",* Link failed to ensure that appropriate steps were identified and actioned (despite being aware that WIM had promised, but never provided, a detailed response to its email).

5.30. Further, on 28 and 29 March 2019 and 4 April 2019, having again required WIM to identify *"concrete actions that have been or will be taken to improve the combined buckets 3 and 4 metric, particularly if the 70% limit is breached",* Link implicitly accepted and failed properly to challenge WIM's assertive communications that it did not agree with and had not agreed with this conclusion (although Link did at least object to WIM's proposal that the relevant Liquidity Metrics should be yet further amended).

<u>Conclusion on liquidity</u>

5.31. By reason of the matters set out in paragraphs 5.3 – 5.30 above, during the period from 31 July 2018 to 3 June 2019:

(a) In breach of Principle 2, Link failed to exercise due care skill and diligence as ACD in its oversight of the liquidity profile of the WEIF;

(b) In breach of Principle 6, Link failed to pay due regard to the interests of its customers and treat them fairly. Link placed the interests of one group of unitholders (those who redeemed between 1 November 2018 and 3 June 2019) above the interests of another group of unitholders (those who remained) and failed to ensure that the unitholders of the scheme were treated fairly;

<u>The TISE securities</u>

5.32. The WEIF invested in the TISE securities including after they were listed as follows:

(a) Sabina listed on TISE on 28 December 2017;

(b) Ombu listed on TISE on 15 June 2018;

(c) Industrial Heat listed on TISE on 5 October 2018;

(d) Proton Partners listed on NEX on 29 February 2019; and

(e) Benevolent listed on TISE on 21 March 2019.

5.33. Although ACDs are not usually expected to be involved in an underlying asset's corporate actions, including listing on exchange, Link failed to give adequate consideration to the potential implications for the WEIF's liquidity profile where businesses which the WEIF had holdings in announced an intention to convert from unlisted status to becoming listed on an exchange. Link did not adequately consider, or act upon, the risks created if other companies were able to use the same process that Sabina had used to enable WIM to continue to invest. It was recognised within Link that there were risks created should this happen. Despite this clear and obvious risk, Link failed to engage appropriately with WIM to understand what future plans other investments within the WEIF portfolio might have had. WIM was able to use the process as it chose, without prior notification to Link or prior permission. It was entirely foreseeable by Link that the use of the 'intention to list' process increased liquidity risks. It created an ability to invest in more assets within the WEIF which were of the same characteristic in liquidity terms as unquoted assets. WIM capitalised on this opportunity not only to continue to hold the assets once they had been removed from the 10% unquoted restrictions but, significantly, in some cases to increase the holdings in the TISE assets above the amount originally held. By allowing this process to be used by WIM, without adequately considering the implications of doing so, Link allowed an increased level of fair value and illiquid assets to be held within the Fund. This increased the risks of liquidity issues arising. Link should have been fully aware of that and acted to prevent the repeated use of this process by WIM.

5.34. By enabling WIM to focus on bucket levels and maintenance of those levels, rather than requiring a rebalance of the buckets, Link missed the opportunity to prevent further investments in illiquid assets. Had Link required a focus on significant and urgent reductions in buckets 3 and 4 and rebalancing to bucket 1, including by ensuring that no new investments could be made, or additional funding provided within those buckets, the liquidity risks could have been reduced at a much earlier stage. An absolute moratorium on any further investments in fair value assets within the WEIF could have been required by Link. It failed to take that step and missed an opportunity to help prevent further deterioration in the WEIF's liquidity.

6. SANCTION

Financial penalty

6.1. The Authority's policy for imposing a financial penalty is set out in Chapter 6 of DEPP. In respect of conduct occurring on or after 6 March 2010, the Authority applies a five-step framework to determine the appropriate level of financial penalty. DEPP 6.5A sets out the details of the five-step framework that applies in respect of financial penalties imposed on firms.

6.2. The Authority has calculated the financial penalty which it considers would be appropriate in this case on this basis, as follows.

Step 1: Disgorgement

6.3. Pursuant to DEPP 6.5A.1G, at Step 1 the Authority seeks to deprive a firm of the financial benefit derived directly from the breaches where it is practicable to quantify this.

6.4. Where a firm agrees to carry out a redress programme to compensate those who have suffered loss as a result of the breach, or where the Authority decides to impose a redress programme, the Authority will take this into consideration. Link has agreed to implement a scheme of arrangement which is envisaged to involve the payment of restitution which, it is envisaged, will exceed any financial benefit derived by Link.

6.5. Step 1 is therefore £0.

Step 2: The seriousness of the breaches

6.6. Pursuant to DEPP 6.5A.2G, at Step 2 the Authority determines a figure that reflects the seriousness of the breaches. Where the amount of revenue generated by a firm from a particular product line or business area is indicative of the harm or potential harm that its breaches may cause, that figure will be based on a percentage of the firm's revenue from the relevant products or business area.

6.7. The Authority considers that the revenue generated by Link is an indicator of the harm or potential harm caused by its breaches. The Authority has therefore determined a figure based on a percentage of Link's relevant revenue. Link's relevant revenue is the revenue derived by LFS during the period of the breaches. The period of Link's breaches was from 31 July 2018 to 3 June 2019. Where a breach lasts less than 12 months, the relevant revenue will be that derived by the firm in the 12 months preceding the end of the breach (DEPP 6.5A.2G(2)). The Authority accordingly considers Link's relevant revenue to be £42,073,475.

6.8. In deciding on the percentage of the relevant revenue that forms the basis of the step 2 figure, the Authority considers the seriousness of the breach and chooses a percentage between 0% and 20%. This range is divided into five fixed levels which represent, on a sliding scale, the seriousness of the breach; the more serious the breach, the higher the level. For penalties imposed on firms there are the following five levels:

(a) Level 1 – 0%

(b) Level 2 – 5%

(c) Level 3 – 10%

(d) Level 4 – 15%

(e) Level 5 – 20%

6.9. In assessing the seriousness level, the Authority takes into account various factors which reflect the impact and nature of the breach, and whether it was committed deliberately or recklessly. DEPP 6.5A.2G(11) lists factors likely to be considered 'level 4 or 5 factors'. Of these, the Authority considers the following factors to be relevant:

(a) Link’s breaches caused a significant loss or risk of loss to a large number of individual consumers and investors, causing considerable inconvenience and distress to those invested in the WEIF at the time of the suspension. Many of the holders of the £3.5 billion NAV of the WEIF at that time were retail investors.

(b) Link’s breaches have had an adverse effect on confidence in financial services markets.

6.10. DEPP 6.5A.2G(12) lists factors likely to be considered ‘level 1, 2 or 3 factors’. Of these, the Authority considers the following factors to be relevant:

(a) Little, or no, profits were made or losses avoided as a result of the breaches.

(b) Link’s breaches were committed negligently or inadvertently.

6.11. The impact of Link’s breaches was extremely serious, in particular:

(a) As above, the breaches caused significant loss and risk of loss to investors;

(b) Link’s breaches resulted in considerable inconvenience and distress to underlying investors in the WEIF; and

(c) The failure of the WEIF has had an adverse effect on financial services markets, in particular by damaging consumer confidence in the fund management sector.

6.12. Taking all of these factors into account, the Authority considers the seriousness of Link’s breaches to be level 4 and so the Step 2 figure is 15% of £42,073,475.

6.13. Step 2 is therefore £6,311,021.

<u>Step 3: Mitigating and aggravating factors</u>

6.14. Pursuant to DEPP 6.5A.3G, at Step 3 the Authority may increase or decrease the amount of the financial penalty arrived at after Step 2, but not including any amount to be disgorged as set out in Step 1, to take into account factors which aggravate or mitigate the breaches.

6.15. The Authority considers that the following factors aggravate the breaches:

(a) The firm's previous disciplinary record and general compliance history, including:

a. On 13 November 2012, Link, under its former name of Capita Financial Managers Limited ("CFM"), was given a public censure for breaches of Principles 2 and 3 and various of the COLL rules between June 2006 and March 2009 in connection with failures in its oversight, as ACD, of the CF Arch cru Investment Funds and the CF Arch cru Diversified Funds ("the Arch cru Funds"). The Arch cru Funds were retail investment funds which invested in various cells of a Guernsey-incorporated company, listed on the Channel Islands Stock Exchange. Trading in the Arch cru Funds was suspended in March 2009 and the Arch cru funds were subsequently wound up. The FSA found that Link had, inter alia, failed adequately to monitor the liquidity of the Arch cru Funds. As part of the settlement reached with the FSA, Link agreed voluntarily to contribute £32 million towards a £54 million payment scheme. The Final Notice stated that "*The serious nature of the breaches identified in this Notice would ordinarily have led the FSA to impose a penalty of £4.025 million after the application of a 30% discount for early settlement. However, in light of the specific circumstances of this case…, the FSA has decided that it is not appropriate to impose a financial penalty on CFM*"; and

b. On 10 November 2017 Link again under its former name of CFM, was given a public censure for breaches of Principles 2 and 7 in relation to its failures in its oversight, as operator, of the Connaught Income Fund, Series 1 ("the Connaught Fund") between 7 April 2008 and 25 September 2009. The Connaught Fund was an unregulated collective investment scheme which invested in short-term property bridging loans. It was suspended in March 2012 and subsequently wound up. The Final Notice noted that there was agreement to pay up to £66m in redress and stated that "*The Authority has taken account of the fact that CFM itself would not have been able to make [that] payment …*

and that this will only be possible with the financial support given to CFM by its ultimate parent, Capita plc…. Had it not been for CFM's (with the assistance of its ultimate parent company, Capita plc) agreement to make the payment then the Authority would have imposed a financial penalty of £15 million. In that event CFM would have qualified for a 30% discount (stage 1) in accordance with the Authority's executive settlement procedure, which would have reduced the penalty to £10.5 million."

c. Link's failure to make changes to its participation rate after a s166 report was issued that recommended it do so during the Relevant Period. A s166 report issued on 19 October 2018, found that the firm used inappropriate participation rates for its liquidity monitoring (including of the WEIF). Despite the firm being informed of this, it took no action to remediate the position and then suspended the WEIF on 3 June 2019.

d. The Authority considers that Link's failings: (a) materially contributed to the risk that suspension would be required; and (b) placed those investors who did not redeem prior to the point of suspension at a disadvantage. The 'first mover advantage' for those redeeming earlier was exacerbated by the failure of Link to adequately monitor how redemptions were being met by WIM and to help prevent further deterioration of liquidity. More liquid assets were sold to meet redemptions exacerbating the decline in liquidity. Link could have managed the liquidity issues which arose in a number of ways, including requiring assets to be sold down equally across the liquidity profile, referred to as vertical slicing. This would have prevented a disproportionate sale of the most liquid assets. Had vertical slicing been required by Link, the WEIF's liquidity would not have deteriorated in the manner in which it did.

6.16. Having taken into account these aggravating factors, the Authority considers that the Step 2 figure should be increased by 55%.

6.17. Step 3 is therefore £9,782,083.

Step 4: Adjustment for deterrence

6.18. Pursuant to DEPP 6.5A.4G, if the Authority considers the figure arrived at after Step 3 is insufficient to deter the firm who committed the breach, or others, from committing further or similar breaches, then the Authority may increase the penalty.

6.19. The Authority does not consider that the Step 3 figure of £9,782,083 represents a sufficient deterrent in the circumstances of this case, either generally or to Link which acted as ACD to some 175 funds during the Relevant Period.

6.20. Link's serious failure to manage properly the liquidity of one of the funds it supervised as ACD following its previous serious failings (when known as CFM) in respect of the Arch Cru Funds and the Connaught Fund has further exposed many thousands of investors to the risk of, and actual, significant detriment. It has also undermined public confidence in the funds industry. At the time of its suspension on 3 June 2019, the WEIF was valued at just over £3.5 billion. Since then, the value of many of the WEIF's holdings have reduced significantly on realisation, meaning that investors (nearly three quarters of whom were retail investors) have received, or will receive, significantly less than the value of their investments at the point of suspension. These losses were unfairly and disproportionately borne by those investors who did not redeem early and were left with a fund with an illiquid rump of unquoted assets. The Authority regards these circumstances as a matter of significant importance when considering the need for credible deterrence.

6.21. One of the Authority's stated objectives when introducing the penalty policy on 6 March 2010 was to increase the level of penalties to ensure credible deterrence. The Authority considers that penalties imposed under this policy should be materially higher than penalties for similar breaches imposed pursuant to the policy applicable before that date, which were applicable when disciplinary action was taken against the firm in relation to its serious Arch cru and Connaught failings.

6.22. The Authority considers that for credible deterrence purposes the penalty imposed for the failings in this Notice should as a minimum significantly exceed the level of the penalty that would have been imposed on Link in 2012 and again in 2017 in respect of its failings in respect of the Arch cru Funds and the Connaught Fund respectively had it not been for the substantial payments by way of redress made on each of those occasions.

6.23. Accordingly, the Authority considers that in order to achieve its objective of credible deterrence, the Step 3 figure should be increased to £50,000,000.

6.24. Step 4 is therefore £50,000,000.

Step 5: Settlement discount

6.25. Pursuant to DEPP 6.5A.5G, if the Authority and the firm on whom a penalty is to be imposed agree the amount of the financial penalty and other terms, DEPP 6.7 provides that the amount of the financial penalty which might otherwise have been payable will be reduced to reflect the stage at which the Authority and the firm reached agreement. The settlement discount does not apply to the disgorgement of any benefit calculated at Step 1.

6.26. Had the Authority and Link reached agreement on the appropriate penalty at Stage 1 of the settlement process, a 30% discount would have been applied to the Step 4 figure.

6.27. Step 5 would in those circumstances have been £35,000,000.

Proposed sanction

6.28. In accordance with the above, were it not for the factors outlined below, the Authority would have proposed to impose a financial penalty of £50,000,000 (or £35,000,000 if settled) on Link for breaching Principle 2 and Principle 6.

6.29. However, Link has agreed to implement the Scheme, under which restitution will be payable. The Scheme will involve the disposal by Link of substantially all of its value and, because it includes an additional significant voluntary contribution from Link’s ultimate parent, LAHL, will result in the payment of restitution above what would otherwise be available to Link.

6.30. The Authority is satisfied that the additional imposition of a financial penalty would reduce the amount of restitution available to be paid by Link. As a result, instead of imposing a financial penalty, the Authority hereby publishes a statement of Link’s misconduct, pursuant to section 205 of the Act, in the form of this Final Notice. The Final Notice is published on the Authority’s website on 11 April 2024.

7. RESTITUTION

7.1. Under section 384 of the Act, the Authority has the power, if it is satisfied that a person has contravened a relevant requirement and that one or more persons have suffered loss or been otherwise adversely affected as a result of the contravention, to require the person concerned to pay to the appropriate person or distribute among the appropriate persons, such an amount as appears to the Authority to be just having regard to the extent of the loss or other adverse effect. The Authority has published guidance on the exercise of its power under section 384 of the Act in Chapter 11 of the Enforcement Guide.

7.2. For the reasons outlined above, the Authority considers that, during the relevant period, Link breached Principle 2 and Principle 6. As rules made under the Act, Principle 2 and Principle 6 are each relevant requirements for the purposes of section 384 of the Act.

7.3. As a result of Link's failure to ensure that redemptions from the WEIF were met by the liquidation of assets with liquidity profiles proportionate to the total assets held by the WEIF, the Authority considers that the assets held by the WEIF at the time of its suspension were disproportionately illiquid by comparison with the assets held at 1 November 2018.

7.4. This meant that those investors who continued to hold investments in the WEIF at the time of its suspension were disproportionately affected by the significant reduction in value of the assets remaining in the WEIF at the point of its suspension and subsequent liquidation.

7.5. Had Link suspended the WEIF earlier, when its deteriorating liquidity was apparent, rather than allowing early redeemers to take the benefits of the sale of the WEIF's liquid assets, and leaving those that remained with progressively more concentrated holdings of less liquid assets whose earlier recorded NAVs could not ultimately be realised upon sale, those investors who remained in the fund in June 2019 would have incurred significantly lower losses.

7.6. Given the above, the Authority considers that part of the losses incurred by investors who remained invested in the WEIF at the time of its suspension were suffered as a result of Link's contraventions of relevant requirements.

7.7. The Authority considers that an appropriate means to assess these losses is to compare the difference between the monies that the investors in the WEIF at the time of suspension have received or are estimated to receive on liquidation of the WEIF with what they would have received had the proceeds of the sale of assets realised between November 2018 and the suspension of the WEIF been shared equally between those who redeemed their investments during that period and those who remained invested in the WEIF at the time of suspension.

7.8. The Authority has calculated that, using this approach, those investors who remained invested in the WEIF at the time of its suspension would have received an additional £298,403,919 had all investors received a fair and proportionate share of the proceeds of the asset sales.

7.9. The Authority has assessed this sum by calculating the share in the proceeds of the WEIF's assets which were sold after November 2018 which would have been received by those investors who remained invested at the point of suspension had the proceeds of total asset sales been divided fairly among all investors.

7.10. In the circumstances, having regard to the extent of the losses, it appears to the Authority to be just to require Link to pay to those investors in the WEIF who lost money as a result of Link's failures.

7.11. The Authority therefore considers that Link should pay restitution to reflect the losses incurred as a result of its contraventions of relevant requirements.

7.12. Link has agreed to implement the Scheme, under which substantially all of its value will be used to contribute to a redress scheme. In addition, LAHL has agreed to make a significant voluntary contribution to the Scheme.

7.13. Accordingly, the Authority hereby requires Link to pay restitution of £298,403,919, or such lesser sum as is payable under the Scheme, to the WEIF for the benefit of Relevant Investors in accordance with arrangements specified in the Scheme.

8. PROCEDURAL MATTERS

8.1. This Notice is given to Link under, and in accordance with, section 390 of the Act.

Decision maker

8.2. The decision which gave rise to the obligation to give this Notice was made by the Settlement Decision Makers.

Manner and time for payment

8.3. Link must pay the restitution required by this Final Notice to the WEIF pursuant to the terms of, and within the period specified by, the rules of the Scheme.

Publicity

8.4. Sections 391(4), 391(6) and 391(7) of the Act apply to the publication of information about the matter to which this notice relates. Under those provisions, the Authority must publish such information about the matter to which this notice relates as the Authority considers appropriate. The information may be published in such manner as the Authority considers appropriate. However, the Authority may not publish information if such publication would, in the opinion of the Authority, be unfair to Link or prejudicial to the interests of consumers or detrimental to the stability of the UK financial system.

8.5. The Authority intends to publish such information about the matter to which this Final Notice relates as it considers appropriate.

Authority contacts

8.6. For more information concerning this matter generally, contact Ross Murdoch (direct line: 020 7066 3999/email: ross.murdoch@fca.org.uk) or Natalie Birtle (direct line: 020 7066 6856/email: natalie.birtle@fca.org.uk) at the Authority.

Ross Murdoch
Interim Head of Department
Financial Conduct Authority, Enforcement and Market Oversight Division

ANNEX A - RELEVANT STATUTORY AND REGULATORY PROVISIONS

FINANCIAL SERVICES AND MARKETS ACT 2000

s.1B- The FCA's general duties:

1. In discharging its general functions the FCA must, so far as is reasonably possible, act in a way which –

    (a) is compatible with its strategic objective, and

    (b) advances one or more of its operational objectives.

2. The FCA's strategic objective is: ensuring that the relevant markets (see section 1F) function well.

3. The FCA's operational objectives are –

    (a) […];

    (b) the integrity objective (see section 1D);

    (c) […]

s.1D- The integrity objective:

4. The integrity objective is: protecting and enhancing the integrity of the UK financial system.

5. The "integrity" of the UK financial system includes –

    (a) its soundness, stability and resilience,

    (b) its not being used for a purpose connected with financial crime,

(c) its not being affected by contraventions by persons of Article 14 (prohibition of insider dealing and of unlawful disclosure of inside information) or Article 15 (prohibition of market manipulation) of the market abuse regulation,

(d) the orderly operation of the financial markets, and

(e) the transparency of the price formation process in those markets.

s.206 – Financial penalties:

6. If the Authority considers that an authorised person has contravened a relevant requirement imposed on the person, it may impose on him a penalty, in respect of the contravention, of such amount as it considers appropriate.

PRINCIPLES FOR BUSINESSES

7. The Principles are a general statement of the fundamental obligations of firms under the regulatory system and are set out in the Authority's Handbook. They derive their authority from the Authority's rule-making powers set out in the Act. The relevant Principles are as follows:

Principle 2:

A firm must conduct its business with due skill, care and diligence.

Principle 6:

A firm must pay due regard to the interests of its customers and treat them fairly.

THE COLLECTIVE INVESTMENT SCHEMES SOURCEBOOK ("COLL")

8. Link was required to comply with relevant rules and have regard to guidance set out in COLL which included the following:

COLL 5.1.2G:

(1) *This chapter [Chapter 5] helps in achieving the statutory objective of protecting consumers by laying down minimum standards for the investments that may be held by an authorised fund. In particular:*

i. the proportion of transferable securities and derivatives that may be held by an authorised fund is restricted if those transferable securities and derivatives are not listed on an eligible market; the intention of this is to restrict investment in transferable securities or derivatives that cannot be accurately valued and readily disposed of; and

ii. authorised funds are required to comply with a number of investment rules that require the spreading of risk.

COLL 5.2.3R(1):

"An [AFM] must ensure that, taking account of the investment objectives and policy of the UCITS scheme as stated in the most recently published prospectus, the scheme property of the UCITS scheme aims to provide a prudent spread of risk."

COLL 5.2.7AR(1)(c):

"A UCITS scheme may invest in a transferable security only to the extent that… reliable valuation is available for it as follows:

i. in the case of a transferable security admitted to or dealt in on an eligible market, where there are accurate, reliable and regular prices which are either market prices or prices made available by valuation systems independent from issuers;

ii. in the case of a transferable security not admitted to or dealt in on an eligible market, where there is a valuation on a periodic basis which is derived from information from the issuer of the transferable security or from competent investment research;"

COLL 5.2.8R (3):

"Transferable securities and approved money-market instruments held within a UCITS scheme must be:

a) *admitted to or dealt in on an eligible market within COLL 5.2.10 R (1)(a) (Eligible markets: requirements); or*

b) *dealt in on an eligible market within COLL 5.2.10 R (1)(b); or*

c) *admitted to or dealt in on an eligible market within COLL 5.2.10 R (2); or*

d) *for an approved money-market instrument not admitted to or dealt in on an eligible market, within COLL 5.2.10AR (1); or*

e) *recently issued transferable securities, provided that:*

   i. *the terms of issue include an undertaking that application will be made to be admitted to an eligible market; and*

   ii. *such admission is secured within a year of issue.*

COLL 5.2.8R (4):

However, a UCITS scheme may invest no more than 10% of the scheme property in transferable securities and approved money-market instruments other than those referred to in (3).

COLL 6.1.2G

This chapter helps in achieving the statutory objective of protecting consumers. It provides the operating framework within which the authorised fund must be operated on a day-to-day basis to ensure that clients are treated fairly when they become, remain or as they cease to be unitholders.

COLL 6.2.2G:

(1) *"… the statutory objective of securing an appropriate degree of protection for consumers. In accordance with Principle 6, this section is also concerned with ensuring the authorised fund manager pays due regard to its clients' interests and treats them fairly.*

(2) *An authorised fund manager of an AUT, ACS or ICVC is responsible for arranging for the issue and the cancellation of units for the authorised fund. An authorised fund manager of an AUT, ICVC or co-ownership scheme is permitted to sell and redeem units for its own account. An authorised fund manager of a limited partnership scheme is only permitted to sell and redeem units as agent for the scheme. The rules in this section are intended to ensure that the authorised fund manager treats the authorised fund fairly when arranging for the issue or cancellation of units, and treats clients fairly when they purchase or sell units….*

COLL 6.6A.2(1)-(2):

"An [AFM] of a UCITS scheme must:

(1) *ensure that the unitholders of any such scheme it manages are treated fairly; and*

(2) *refrain from placing the interests of any group of unitholders above the interests of any other group of unitholders;"*

COLL 6.2.9R(1) and (2):

(1) *As the authorised fund manager normally controls the issue, cancellation, sale and redemption of an authorised fund's units, it occupies a position that could, without appropriate systems and controls, involve a conflict of interest between itself and its clients.*

(2) *SYSC 3.1.1 R (Systems and controls) requires that a firm take reasonable care to establish and maintain such systems and controls as are appropriate to its business and Principle 8 requires a firm to manage conflicts of interest between itself and a customer fairly.*

COLL 6.12.12R:

"an [AFM] … must ensure that, for each UCITS it manages, the liquidity profile of the investments of the scheme is appropriate to the redemption policy laid down in the instrument constituting the fund or the prospectus."

COLL 6.6.14 (1):

"The authorised fund manager must avoid the scheme property being used or invested contrary to COLL 5, or any provision in the instrument constituting the fund or the prospectus as referred to in COLL 5.2.4 R (Investment powers:general), and COLL 5.6.4 R (Investment powers: general), except to the extent permitted by (3)(b)."

COLL 6.6.14 (2):

"The authorised fund manager must, immediately upon becoming aware of any breach of a provision listed in (1), take action, at its own expense, to rectify that breach, unless the breach occurred as the result of any of the circumstances within (3)."

COLL 6.6.14 (3):

"The authorised fund manager must restore compliance with COLL 5 as soon as reasonably practicable having regard to the interests of the unitholders and, in any event, within the period specified in (5) or, when applicable, (6) where:

(a) *the scheme property is:*

- *i. used or invested contrary to COLL 5 (other than a provision excusing a failure to comply on a temporary basis); and*
- *ii. the contravention is beyond the control of both the authorised fund manager and the depositary; or*

(b) *there is a transaction ("subsequent transaction") deriving from a right (such as the right to convert stock or subscribe to a rights issue) attributable to an investment ('original investment') of the scheme if:*

- *i. the subsequent transaction, but for this rule would constitute a breach of COLL 5; and* *ii. at the time of the acquisition of the original investment, it was reasonable for the authorised fund manager, to expect that a breach would not be caused by the subsequent transaction; and*

iii. in this rule the reference to the exercise of a right includes the taking effect of a right without any action by or on behalf of the depositary or the authorised fund manager."

COLL 6.6.14 (5)(a):

"The maximum period for restoration of compliance under (3) starts at the date of discovery of the relevant circumstance and lasts, subject to any extension under (6), for six months".

COLL 6.12.11R:

(1) An authorised fund manager must employ an appropriate liquidity risk management process in order to ensure that each UCITS it manages is able to comply at any time with COLL 6.2.16 R (Sale and redemption).

(2) Where appropriate, the authorised fund manager must conduct stress tests to enable it to assess the liquidity risk of the UCITS under exceptional circumstances.

COLL 6.2.16R(3):

Subject to COLL 6.2.19 R (Limited redemption) and COLL 6.2.21 R (Deferred redemption), the authorised fund manager must, at all times during the dealing day, on request of any qualifying unitholder, effect the redemption of units in accordance with the conditions in the instrument constituting the fund and the prospectus unless it has reasonable grounds to refuse such redemption.