Factsheet No.015

For investment advisers

Traded Life Policy Investments (TLPIs)

It explains what Traded Life Policy Investments are and the marketing restriction rules applying to their distribution to retail investors in the UK. Firms should not promote TLPIs to ordinary retail clients (i.e. clients who are neither sophisticated nor high net worth).

What are TLPIs?

Traded Life Policy Investments (TLPIs) – also known as Traded Life Settlements or Senior Life settlements – are complex products with a number of inherent risks. They are pooled investments into US life assurance policies. TLPIs are complex, high-risk products that are not suitable for the vast majority of retail clients.

Our rules limit the ability of firms to promote these products in the retail market. Generally speaking, TLPIs cannot be promoted (whether with or without advice) to retail investors other than those who have been certified as sophisticated or of high net worth. (See Policy Statement 13/3). These rules are in COBS 4.12. Firms operating in this market should take care to ensure their marketing activities comply with the restrictions imposed by our rules.

Key risks associated with TLPIs

These are the risks firms should look at when considering TLPIs:

- Longevity risk – an accurate estimation of life expectancy is the most important factor in assessing the price of each underlying life insurance policy in a TLPI. The primary risk is that the underlying policyholders live longer than expected (e.g. because of medical advances and life assurance actuarial models not working as the basis for investment purposes), so the TLPI needs to continue to fund premiums on the policies for longer than expected. This could negatively affect the return on investment and liquidity on an ongoing basis.

Evidence shows significant problems with the way TLPIs are designed, marketed and sold to UK retail investors. Find out how what restrictions apply to the way firms distribute them.

- Liquidity risk – the underlying investments are illiquid due to their specialised nature; there is only a limited secondary market for them. This may mean they are sold at a significantly reduced value if the TLPI needs to raise funds, which will affect the value of the TLPI's portfolio. So investors may suffer financial loss at the point of redemption.
- TLPI models/structure – in some models, yields are promised to previous investors which can only be sustained by using new investors' money, so the model in effect 'borrows' from itself.
- The underlying assets are based offshore – there is an exchange rate risk, both in terms of the costs of meeting ongoing premiums and the final payout for the underlying insurance contracts. TLPI providers may use currency hedging instruments, but these may pose additional risks and involve extra costs.
- Many TLPIs sold in the UK are located offshore – this means investors may have limited or no recourse to the Financial Services Compensation Scheme if things go wrong and the product fails. Investors would only be able to complain to the Financial Ombudsman Service if, for example, the advice they have received from UK distributors was unsuitable or if a promotion from a UK provider or distributor was unfair, unclear or misleading.
- Parties involved in the TLPI may become insolvent – TLPIs often involve a chain of firms in their operation, any of which could fail and cause problems for investors in recovering their money. Additionally, the insurance companies behind the US policies may become insolvent and unable to meet claims when the original policyholders die.
- Awareness of authorisation/compensation arrangements – many funds for TLPIs are based outside our jurisdiction. We have evidence that providers and advisers have not fully understood or conveyed to investors the risks involved in how (or whether) the client's product will be authorised and what compensation arrangements apply.

Action taken

Our predecessor, the Financial Services Authority (FSA), fined Rockingham Independent Limited £35,000, and imposed partial prohibitions on two of their directors and one adviser for recommending clients invest in a TLPI product. The firm recommended the product to customers who did not want to expose their capital to higher levels of risk, and did not consider or impose limits on the maximum proportion of a customer's capital that should be invested in TLPIs. As a result, large proportions of some customers' investments were placed in the TLPI, magnifying the already significant risks associated with investment in a TLPI.

Our rules came into effect in January 2014 and limit the ability of firms to promote TLPIs to retail clients. Firms should not promote TLPIs to ordinary retail clients (i.e. clients who are neither sophisticated nor high net worth).

Further information

Our consumer alert on TLPIs explains our concerns to investors and the actions they should take if they are concerned about their investments in TLPIs. Our Policy Statement introduced new rules to ban the promotion of Unregulated Collective Investment Schemes (UCIS) and certain close substitutes, including TLPIs, together to be known as Non-Mainstream Pooled Investments (NMPIs), to the vast majority of retail investors in the UK.

For more information and the latest news, see the firms section of our website: www.fca.org.uk/firms