Ashley Alder
Chairman
The Financial Conduct Authority
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OPEN LETTER TO FCA CHAIR ASHLEY ALDER REGARDING FCA HYPOCRISY

Monday, 4th December 2023, by Email only.

Dear Mr. Alder,

I write to you on behalf of members of the Transparency Task Force, in my capacity as its Founder; and also on behalf of members of the Woodford Campaign Group, in my capacity as one of its Co-Founders.

And I write to you on the day that voting in relation to the Scheme of Arrangement for the Woodford Scandal has come to a close; a vote whose outcome if 'in favour' of the Scheme may need to be deemed null and void, for the reasons I shall go on to explain.

OUR UNDERSTANDING OF YOUR ROLE

According to the FCA statements about your role, your job includes responsibility for:

- Providing a source of challenge to the Chief Executive on how the FCA is run
- Leading the communication of FCA policies with a wide range of consumers and other stakeholders, alongside the Chief Executive
- Evaluating the performance of the Board and individual directors
- Acting as a focus for the accountability of the FCA
- Fostering an open, inclusive discussion within the FCA that challenges executives, where appropriate

As such, it is clear that what we are writing to you about today is a matter you have senior responsibility for.

I therefore request a swift, considered and honest reply to the matters we are raising - they collectively represent a major public interest issue impacting hundreds of thousands of Woodford investors directly, plus all those that have an interest in the reputational integrity of the regulatory framework that is meant to be governing the financial services sector.

INTRODUCTION

I am writing to you about the FCA's unacceptable hypocrisy around its new Consumer Duty, particularly the FCA's unacceptable hypocrisy around the communications aspects of the Duty.

Hypocrisy that not only undermines the intentions behind the Duty but have also skewed the voting around the Scheme of Arrangement, thereby removing any legitimacy it may have had, making any 'in favour' outcome that may arise null and void.

The FCA states that the firms it regulates must:

- Be open, honest and avoid causing foreseeable harm
- Provide timely, clear and understandable information that supports good decision-making; where important information isn't buried in lengthy terms and conditions

Yet the way the FCA is handling the Woodford scandal shows it to be in direct breach of all these requirements, and more.

How can the FCA set standards for others that it is either unwilling or unable to live up to itself?

GENERAL CRITICISMS OF THE FCA IN RELATION TO THE WOODFORD SCANDAL

Before explaining in very precise terms the basis of our claim that the FCA's communication with regard to Woodford is misleading and thereby hypocritical in the context of the Consumer Duty, we shall first describe why there has been widespread criticism of the FCA's handling of the Woodford scandal, in general:

- **The FCA has failed to act assertively**. Its reluctance to act assertively in respect of WEIF may be a consequence of it being conflicted by its own historical actions and inactions in relation to the entities involved. To give just three examples, it may be difficult for the FCA to enforce against:

- LFSL, given the regulator's decision to allow the firm to continue trading under the existing leadership team, its permissions intact, after it played a central role in the causation of hundreds of millions of Pounds of consumer losses in the Arch Cru and Connaught scandals, especially since it is hard to believe that Link Group would have proceeded with the acquisition of the firm (for £888m) without receiving specific assurances from the FCA about any future enforcement actions in respect of any misconduct that began under Capita's ownership - and the FCA desperately needed that deal to complete, so Capita could afford to pay partial redress to Connaught investors;
- WIM, given the regulator's role in persuading then compelling it to use CFM (now LFSL) as its ACD, given that firm's previous misconduct in relation to Arch Cru and Connaught;
- Any firm that does not have sufficient means to meet the cost of any resulting restitution order, civil litigation or FOS claims, given that any shortfall would pass to the FSCS. The FSCS is funded by a mandatory industry levy, and is widely described by market participants as a 'regulatory failure tax', in that it is a mechanism by which well-run firms are forced to contribute toward the cost of remedying consumer detriment caused by firms that engage in misconduct and then become insolvent. Good actors argue, not unreasonably, that it is the job of the FCA to ensure that firms have sufficient resources to meet liabilities that arise as a result of their activities - the capital adequacy tests referred to earlier - and to prevent (so far as is possible) and thereafter promptly to curtail any misconduct. When claims pass to the FSCS, it is a reasonable supposition that the regulator has failed. And, for the reasons set out in this letter, it is especially clear that this has happened multiple times in respect of the WEIF. Given the criticism of the FCA in three recent external reviews - Connaught, London Capital & Finance plc, Interest Rate Hedging Products - and by the National Audit Office in respect of the British Steel Compensation Scheme, there are suspicions that the FCA is keen to avoid the political consequences of any regulatory action that would result in a large increase in the FSCS levy

- **Authorising Craig Newman** as Chief Executive Officer of Woodford Investment Management Limited ('WIM') despite him having been dismissed by Invesco Perpetual for allegedly having misappropriated client data;
- **Facilitating the accelerated authorisation of WIM**, potentially overlooking shortcomings in governance and compliance;
- **Failing to check that individuals authorised as non-executive directors of WIM actually registered with Companies House** as directors of that company;

- **Failing to remove permissions of Capita Financial Managers Limited** ('CFM'), the largest independent Authorised Corporate Director ('ACD') in the market, despite its failings in relation to two previous failed collective investment schemes, Arch Cru and Connaught, then putting WIM under pressure to use CFM as its ACD;
- **Failing to challenge the longstanding practice of Hargreaves Lansdown plc** ('HL') issuing 'best buy' lists to clients which were motivated by commercial concerns rather than being based purely on empirical research;
- **Implementing with insufficient rigour the capital adequacy checks** that form part of its threshold conditions tests in respect of WIM, CFM and perhaps HL;
- **Taking no, or inadequate steps, to challenge WIM and CFM** in relation to misallocation of client monies entrusted to the WEIF;
- **Failing to announce any meaningful enforcement action** almost four and a half years after the fund being suspended;
- **Failing to secure full redress for FSCS-eligible consumers**; it has had ample opportunity to do so by now;
- **Materially understating the true extent of the sums lost** by investors;
- **'Cheerleading' for the Scheme of Arrangement**; the FCA has publicly endorsed the Scheme, which we consider inappropriate given the shortcomings of the offer and the better outcomes potentially available by alternative means (for example through a restitution order, litigation, the Financial Ombudsman Service awards and the Financial Services Compensation Scheme).

COMMUNICATIONS-RELATED CRITICISMS OF THE FCA IN RELATION TO WOODFORD

We will now turn attention to matters relating to the FCA's communication failings i.e. its inability and or unwillingness to communicate in a straightforward and non-misleading way:

1) **The claims made by Joint Executive Director for Enforcement and Market Oversight**, Therese Chambers:
    - ***'But I also know you'll want to understand what went wrong and how we can improve outcomes in the future.'*** WEIF investors are being asked to vote for the Scheme *without* having sight of the outcomes of the FCA's investigation into LFSL. If they were able to see that information, they would be better placed to decide whether to back the Scheme or hold out for more via the three aforementioned alternatives, because they would have a better understanding of the strength of the case against LFSL. The FCA allowed LFSL to sell its contracts to Waystone Group ('WG'), and as a condition of that sale, key executives transferred from LFSL to WG. It is unlikely that LFSL will be sanctioned by the FCA, because Link

Group has indicated that it will be liquidated, and it is clear that neither WG nor the transferring executives will be sanctioned. So, as with CFM's failings in respect of Arch Cru and Connaught, the FCA is proposing to trade partial redress for regulatory inaction, a course of action that is unlikely to 'improve outcomes for the future';

- ***'Link Group, the ultimate parent of LFS, has agreed to voluntarily contribute up to £60 million of the £230 million to bolster the redress. This money would not be available to investors through either separate legal action or any other action we, or anyone else, could take.'*** It is possible that it may technically be true that it would not make the contribution *it has agreed to as part of the Scheme*, but that it might actually be bound to make a different contribution, one that might actually be larger. We understand it is often the case that the FCA, when considering whether a firm meets its threshold conditions, accepts parental or intra-group guarantees in partial lieu of assets on the firm's own balance sheet, or professional indemnity insurance. In other words, a firm may pass the threshold tests on financial strength because it can draw on its parent or other group companies if a liability emerges that its own balance sheet plus any insurance policies cannot meet;
- ***'This is despite unrealistic promises that there could be more money recovered through private litigation.'*** We believe it is inappropriate for anyone in the FCA to pass comment on the prospects of success of commercial litigation that is afoot, especially when doing so might be taken as advice by consumers and could be detrimental to their interests;
- ***'This redress scheme, together with sales from the suspended fund, means investors will potentially receive back up to 77p in the pound for their losses.'*** Here, the denominator is 'their losses', which is misleading; it should be the narrowly defined type of losses that enabled the FCA to get to a calculation of £298m. Losses are being narrowly measured by the FCA against the suspended balance of £3,613bn, when in fact they need to be seen against the losses investors have incurred since failures came to a head in late 2017/early 2018, if not before. The total mismanagement of the WEIF fund by Woodford and by LFSL were around much earlier than the suspension date and affected far more investor assets than the amounts gated at that time. The losses to investors are hard to determine, but we know that capital losses in the WEIF are substantial, due to a raft of issues. Primary to this, is the quantum bought and the valuations of these unquoted investments applied by LFSL and Northern Trust, who were responsible for ensuring this was properly carried out. Clearly, it has not been done by these parties, these investments were also inappropriate for an equity

income scheme as well. Net capital losses from 2018 up to 30 June 2019 as reported by LFSL were £1.768bn and post suspension, there are further net capital losses of £940m reported to 31 March 2023 by LFSL. This needs to be considered carefully in this case, alongside all the other significant failures of Woodford, LFSL and other parties, not least, what appears to be a total lack of adequate capital arrangements to protect the £82.2bn of assets under management by LFSL. The FCA's lack of effective oversight is troubling. Overall, we estimate the losses to investors range from 40% to 45% on their investment cost, so using 77p/£ return is a totally inappropriate way to describe the situation;

- ***'Regulation cannot compensate for an investment strategy turning sour – and in this case the strategy was transparent and well disclosed.'*** The investment strategy did not 'turn sour'; it was recklessly departed from. The FCA has admitted that this happened from July 2018 (many investors say it began much earlier), yet considered the issue of redress only from November of that year. The *claimed* investment strategy was transparent and well disclosed; the problem is that it was not observed. The meaning of an equity income fund, and the constituents of the index within which the WEIF was included and against which it was compared in promotional materials were well understood; they did not include the early-stage, non dividend-paying, illiquid businesses that came to dominate the WEIF;
- ***'This is the quickest and best way to return as much money to investors as possible compared to other means.'*** For this to be true, the FOS would have to continue to pause its determinations of WEIF-related complaints (something the FCA can direct it to change), and LFSL would have to contest a restitution order and the three litigations. Given that LFSL is no longer trading, having sold its remaining contracts to WG on 9 October 2023, and that in any realistic scenario it is terminally insolvent, these scenarios are exceedingly unlikely. Realistically, we believe the Scheme, which will take until mid-2024 to distribute the last of the hoped-for payments, might actually be the slowest route to redress, as well as the least attractive financially.

2) **The FCA's approach to information disclosure** - the Scheme of Arrangement documentation is required to be impartial and informative, and in particular the Explanatory Statement must set out accurately the alternatives to the Scheme being adopted. We are concerned that the FCA, in its anxiety to get the Scheme approved, has failed to intercede to persuade LFSL - an authorised firm - to avoid causing consumer detriment by painting what we consider to be an unnecessarily negative picture of the

prospects of success of the alternatives to the Scheme (restitution order, FOS claims, litigation) and of failing to provide clear guidance that the FSCS will stand behind such awards. Much of the documentation needed to correct this is either within the FCA's gift or can be secured by it from entities that it either controls (FOS, FSCS) or regulates (LFSL). Investors have asked it to provide this information, but it has declined to do so.

3) **The FCA's wrongful willingness to tolerate misleading claims** - the Scheme documentation holds out that certain parties (for instance, the Investor Committee Chair, Investor Advocate and Scheme Supervisors) are independent. In fact they all know each other, the FCA and LFSL's Counsel, as they all worked together on a previous FCA-sanctioned Scheme of Arrangement, for Amigo Loans. The Woodford Campaign Group asked the FCA to bring pressure to bear on LFSL to correct these claims; it declined to do so.

It is self-evident that Scheme Creditors ought to have been put in a position to make a well-informed decision and thereby be capable of providing their informed consent. For this to be possible they needed to have the full facts before casting their vote.

But the information supplied by the FCA has been misleading; for it is not fully and fairly explaining the Scheme and its consequences.

WHY THE FCA'S STATEMENT OF 27TH NOVEMBER MUST NOT BE ALLOWED TO STAND

It is especially concerning to us that the statement issued by the FCA on Monday 27th November gives a wholly inaccurate account of claimants' potential recourse for legal action against third parties, if the Scheme of Arrangement comes into force.

This is an especially important issue because if investors believe the FCA's misinformation in the 27th November statement, they may vote in favour of the Scheme, with the expectation that they can then also seek redress from other parties. That would be an entirely logical view for an investor to form, because that is what the FCA's statement says.

But the FCA's statement is wholly misleading; perhaps intentionally so.

That FCA statement is reproduced below in full:

This scheme represents the best way for most people to get money back. Any other routes are highly uncertain, would take much longer and be unlikely to deliver anywhere near the levels of redress being suggested elsewhere.

The scheme does not prevent people making claims against third parties in relation to the failure of the fund and is one member, one vote so institutional investors have the same voice as individuals' ones.

The sentence '***This scheme represents the best way for most people to get money back'*** is, at best, opinion presented as fact. It is wholly misleading and wholly inappropriate because it is not possible for the FCA (or anybody) to predict the outcome of any possible counterfactuals such as a restitution order or a claim on the Financial Services Compensation Scheme. The FCA should not therefore be making any such statement; it is irresponsible, given the FCA's status and its own potential conflicts of interest with regard to Woodford.

With regard to the sentence ***'the scheme does not prevent people making claims against third parties in relation to the failure of the fund'*** - this is most likely untrue; there is legal opinion indicating that the waiver of all claims against Link Fund Solutions contained within the Scheme wording, and the risk of adverse costs if such claims nevertheless proceed, will kill all realistic claims against third parties.

If the FCA were to want to convey an accurate, real-world assessment of the situation, that sentence should be along the lines of

'the scheme, in effect, prevents people making claims against third parties in relation to the failure of the fund'

That's because whilst investors could theoretically file claims against third parties involved in the collapse of the former WEIF, it will not be possible to do so in practice, due to the contribution liability in the Scheme which has the effect of indemnifying Link Fund Solutions from any claims that arise from proceedings against third parties.

And of course the FCA must know this as it has been working in cahoots with Link to design and promote the Scheme.

The relevant clause reads:

"LFSL shall not be responsible for any cost, expense, loss or liability (including, without limitation, any liability for adverse costs) incurred by a scheme creditor or any of its representatives in connection with any third party proceedings.

"All costs associated with commencement or continuation of proceedings in respect of the third party proceedings shall be for the account of the scheme creditor only (including, for the avoidance of doubt, in respect of any amount paid to LFSL in accordance with Clause 7.5 below), and shall not be for the account of LFSL."

So if for example an investor sues Hargreaves Lansdown, and Hargreaves Lansdown claims (as it surely would) that Link is partly responsible for any losses it may be found to have caused, the investor will have to give back to Link/indemnify Link for anything that Link may be found to have to pay to Hargreaves Lansdown; and to make it even worse the investor will have to pay Link its costs of defending itself.

The Scheme therefore means that Hargreaves Lansdown, Northern Trust or any other third party can state they have a contribution claim against Link, in the full knowledge that the Scheme's terms empower them to effectively block any claim.

And the Scheme guidance supports that view:

Scheme Creditors' rights to receive proceeds from proceedings that they may take in respect of the WEIF against a Third Party will be reduced if LFSL would be liable to pay a Contribution Claim to that Third Party in respect of that claim.

52.Under the Scheme, each Scheme Creditor gives authority to LFSL to sign a document called the Third Party Litigation Deed on the Scheme Creditor's behalf on the Effective Time. A copy of the Third Party Litigation Deed is available at [https://lfwoodfordfundscheme.com/documents/.](https://lfwoodfordfundscheme.com/documents/)

53. It is important to understand that neither the Scheme nor the Third Party Litigation Deed stops Scheme Creditors from bringing a claim against those Third Parties. However, these documents limit the amount payable by the Third Party to the extent that those amounts are ultimately payable by LFSL.

54. The purpose of the Third Party Litigation Deed is to make sure that the releases given by Scheme Creditors in the Scheme are fully effective. This means that if:
(a) a Scheme Creditor brings a WEIF-related claim (a Third Party Proceeding) against a person (a Third Party); and

(b) the Third Party seeks to bring a claim against LFSL in respect of that Third Party Proceeding (the Contribution Claim), any monies that the third party is required to pay to the Scheme Creditor in respect of that Third Party Proceeding will not be paid to the Scheme Creditor but instead paid into a separate account (the Escrow Account) and otherwise held on trust until the validity and amount of the Contribution Claim has been determined. If a Contribution Claim is owed by LFSL to the third party (the Established Contribution Liability), the amount held in the Escrow Account will be paid in the following order:
(i) escrow costs;
(ii) amounts owing under any Pre-Existing Funding Arrangements;
(iii) amounts owing to LFSL up to the amount of the Established Contribution Liability; and
(iv) the balance to the Relevant Scheme Creditor.

And the final part of the November 27th statement, i.e. '***and is one member, one vote so institutional investors have the same voice as individuals' ones'*** is partially untrue and certainly misleading. In a Scheme of Arrangement process, there are two votes: in one, a simple majority of the voting parties is required; and in the other, a 75 percent supermajority by value of the claims voting is required. The first is indeed a 'one member, one vote' process, in which it is true to say that a private investor's vote has the same weight as an institution's. But this is not the case with the second: here, it is the *value* of the holding that determines the weight of the vote, so (for example) a single entity, Hargreaves Lansdown Fund Management, holds 14.36 percent of the votes. Indeed, it is possible that the HLFM's block vote will determine the outcome. This is obviously a matter for concern, given that the Scheme's potential to deter claims against third parties, Hargreaves Lansdown included, provides it with a compelling incentive to vote in the Scheme's favour - an obvious conflict of interest.

So there you have it.

In summary the FCA has knowingly and wilfully misled, in an attempt to ensure the vote goes the way the FCA desperately needs it to, to avoid a substantial claim on the Financial Services Compensation Scheme.

For all these reasons we feel duty bound to challenge the FCA in relation to its problematic and persistent pattern of misleading communications connected to the Woodford scandal.

Whether the FCA's misleading communications are *deliberately* deceptive or not is a matter of opinion; but it's a matter of fact that if the regulator that you have significant responsibilities for carries on behaving like this, more and more people are going to question the FCA's integrity – I

for one already do; and that belief is born of my understanding about how corrosively conflicted the FCA is on Woodford.

In short, and as I have touched on already, the FCA's troubling behaviour on Woodford can all be explained by its desperation to side-step a massive claim on the Financial Services Compensation Scheme, for if that were to happen the FCA would find its very existence being questioned, again; not just by investors who suffer because of one catastrophic regulatory failure or another – think LC&F, Connaught, Collateral, Blackmore Bond, High Street Group, et al – but also by the very sector they regulate who are increasingly fed up with the 'regulatory failure tax' they keep having to pay through the Financial Services Compensation Scheme.

There's no doubt in my mind that if the FCA is committed to communicating only credibly, it will withdraw the statement it issued on 27th November; or at the very least it will issue a correction with an accompanying apology - for whether deliberately or not, the 27th November statement is dangerously deceptive.

And that just isn't good enough for a regulator that has conduct responsibility for the sector that generates roughly 8% of UK GDP - we all have a right to expect more and better from a public body that is subject to the Seven Principles of Public Life.

CIRCLING BACK TO THE FCA'S HYPOCRISY

There is no doubt that the FCA would certainly be in breach of its own Consumer Duty standards in relation to being open, honest and avoiding causing foreseeable harm; and providing timely, clear and understandable information that supports good decision-making; where important information isn't buried in lengthy terms and conditions.

Quite how the damage done to the decision-making that the FCA's misinformation will have caused can be undone, we do not know; for once people have been misled, it's not clear to us whether there could ever be an untainted vote on the subject. So perhaps as indicated earlier, it may have to be that any 'in favour' outcome of the vote will have to be deemed illegitimate and, therefore, null and void.

Whilst the FCA is entitled to have the view that 'a bird in the hand is worth two in the bush,' we believe its proper role should be to ensure that investors are provided with the best possible information in order that they can make up their own minds. For this to happen it should not be endorsing Link's proposal, and should certainly not be wading into the debate with endorsements based on claims that are at best contested and at worst untrue and misleading.

Therefore, as requested, please provide a swift, considered and honest reply to all the matters raised; they are very serious and leave us wondering whether the FCA may have crossed the line from regulatory failure in respect of Woodford into outright misconduct. It's as if there has been a collusive process in which Link Fund Solutions and the FCA have worked together to mislead creditors and deprive them of valuable information.

The approach taken is wrong and must surely be placing a 'blot' on the Scheme.

And please arrange for the 27th November FCA statement to be withdrawn or unambiguously corrected; and a suitable apology to all voting investors to be given unreservedly.

Naturally, we reserve the right to escalate this matter as a complaint to the Financial Regulators Complaints Commissioner and to raise it as one of several major public interest issues at the Sanction Hearing on 18th January.

We look forward to hearing from you.

Yours sincerely,

A.P. Agathangelou

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