Before the Arbiter for Financial Services

Case No. 094/2018

OK

('the Complainant' or 'the Member')

vs

Momentum Pensions Malta Limited

(C52627) ('MPM' or 'the Service Provider' or 'the Retirement Scheme Administrator')

Sitting of the 28 July 2020

The Arbiter,

PRELIMINARY

Having seen the **Complaint** made against Momentum Pensions Malta Limited ('MPM' or 'the Service Provider') relating to the Momentum Malta Retirement Trust ('the Retirement Scheme' or 'Scheme'), this being a personal retirement scheme licensed by the Malta Financial Services Authority ('MFSA'). The Retirement Scheme is established in the form of a trust and administered by MPM as its Trustee and Retirement Scheme Administrator.

Having considered the particular circumstances of this case, the Arbiter decided to deal with this case separately from those cases made against the Service Provider in relation to the Scheme that were treated together in terms of Article 30 of Chapter 555 of the Laws of Malta. This decision was taken given a particularity of the case in question where the Complainant had an existing insurance policy and underlying investment portfolio held on trust with another trustee and which policy and investment portfolio were then transferred and assigned to MPM as trustee of the Retirement Scheme following the Complainant's membership with the Retirement Scheme.

The Case in question

The Complainant submitted that the negligence of the Service Provider has contributed significantly to the financial losses he incurred in relation to the Scheme.[1] The Complainant submitted that MPM has failed in its duty of care towards him and failed to act in his best interests.[2]

The Complainant explained that his QROPS commenced on 7 February 2012 with an investment of GBP143,000 where his risk profile required his funds to be invested at low to medium risk. The Complainant further explained that MPM became trustees for his funds on 22 July 2014. It was noted that the first annual statement provided by MPM for the year ending 31 December 2015, which showed his attitude to risk as being Medium, indicated that the value of his fund had fallen to GBP80,149.67 by 31 December 2014 and to GBP50,255.98 by 31 December 2015. The Complainant submitted that his 'professional adviser' had assured him that the values given reflected the secondary market and not the maturity value of his assets. It was noted that the annual statement provided by MPM contained a similar statement.

The Complainant highlighted that at the time of closure of business of his professional adviser, his fund value after encashment and charges of GBP20,585, had fallen to GBP65,187.59. The Complainant noted that the losses amount to a minimum of GBP57,227.41 based solely on his original investment. The Complainant further noted that, including earnings, the potential loss is between GBP91,027.41 and GBP118,827.41. [3]

The Complainant submitted that:[4]

a) MPM failed to take note of his attitude to risk, which from his original fact find was Low to Medium, and instead classified him as 'Medium' without consulting him;

[1] *A fol.* 4
[2] *Ibid.*
[3] *Ibid.*
[4] *Ibid.*

b) MPM failed to exercise 'Due Diligence'. The Complainant claimed that the actions of the professional/financial advisers were not monitored or called into question concerning the original investment at the time that MPM took over as Trustee/Policyholder and neither at any time until the financial advisers were forced to close their business. The Complainant also claimed that, as such, MPM failed to comply with their own published conditions/regulations for the protection of their clients;

c) The decline in value of his scheme was enhanced by the failure of MPM to note, react to, or prevent the reinvestment of the earnings into high risk structured notes such as Leonteq and EFG Participation Notes;

d) At no time since becoming Trustee, MPM has notified him of the high-risk investments or of the catastrophic losses. The Complainant submitted that the lack of communication throughout has been a feature of their *modus operandi*.

The Complainant further explained that rather than the caring attitude one might expect from a 'trustee', MPM tried to pass the blame for the losses entirely to the previous trustee. The Complainant submitted that MPM has not recognised its failure concerning the reinvestment of the earnings.[5]

The Complainant noted that despite having done nothing as 'trustees', MPM were content to take their charges and further diminish his pension pot.

The Complainant submitted that the funds initially invested in 2012 represented his cumulative pension investments over a period of nearly 40 years in order to provide his family with a reasonable standard of living during his old age.

The Complainant stated that he faces deprivation and probably poverty in his later life unless the losses are recovered and returned to his fund.[6]

The Complainant submitted that the disastrous situation has caused great distress and illness to himself and his disabled partner for which he believed should be compensated.[7]

[5] *Ibid.*
[6] *Ibid.*

The Complainant also submitted that responses to critical questions have been delayed or in some cases were non-existent. It was claimed that he believed MPM have delayed their final decision to his complaint in the hope that he will not have all of the information available for the Arbiter prior to 18 April. The Complainant claimed that MPM has also failed to provide all of the information and evidence that he required to finalise his complaint.[8]

The Complainant submitted that, most importantly, MPM failed to provide him with the dealing strips that were supposed to bear his signature to authorise transactions. The Complainant claimed that he had never been asked to sign one of these documents. The Complainant noted that he understood from some other complainants that they believed that their signatures had been forged or simply copied and pasted onto such documents. The Complainant submitted that he could not confirm nor deny this in his own case as MPM failed to provide such documents.[9]

It was also submitted that speculative currency transactions were also carried out using the funds from his account following the 22 July 2014.

The Complainant stated that his original investment, which consisted of the RBC Diversified Blue Chip Income Notes, yielded GBP3,080 every 3 months. The Complainant noted that the duration was for 5 years and that the total yield from this product should have been GBP61,600 (5x4x3080).[10]

The Complainant claimed that the losses from this original investment amounted to GBP57,227.41 calculated as the Original Value of GBP143,000 less the Final Value of GBP65,187.59 and Encashments of GBP20,586.[11]

The Complainant submitted that the overall loss on his Scheme amounts to GBP118,827.41 (calculated as the sum of GBP61,600 and GBP57,227.41) and believed that this was the minimum sum that MPM should pay to his account. The Complainant submitted that he believed that, in addition to this, MPM should pay compensation for the extreme distress, anxiety and the resulting

[7] *Ibid.*
[8] *A fol.* 6
[9] *A fol.* 7
[10] *A fol. 4*
[11] *Ibid.*

illness. The Complainant noted that, so far, MPM have repaid their charges of GBP895 for last year to his account and have informed him that they will not make any charges for this year. The Complainant considered this to be an unsatisfactory response to the situation that it was claimed MPM has played a significant part in creating.[12]

In its reply, MPM essentially submitted the following: [13]

1. That Continental Wealth Management ('CWM') is a company registered in Spain. Before it ceased to trade, CWM acted as adviser and provided financial advice to investors. CWM was authorised to trade in Spain and in France by Trafalgar International GmbH ('Trafalgar'). Global Net Limited ('Global Net'), an unregulated company, is an associate company of Trafalgar and offers administrative services to entities outside the European Union.

2. That MPM is not linked or affiliated in any manner to CWM, Trafalgar or Global Net.

3. That MPM is not licensed to provide investment advice.

4. That, without prejudice to MPM's defence that it is not responsible for the Complainant's claims, more than two years have lapsed since the conduct complained of took place and, therefore, pursuant to Article 21(1)(c) of Chapter 555 of the Laws of Malta, the complaint cannot be entertained.

5. MPM stated, at the outset, that it was not the first Trustee and Retirement Scheme Administrator with respect to the investments of the Complainant. It was noted that an *in specie* transfer took place on 22 July 2014 following which MPM became the Trustee and the Retirement Scheme Administrator ('RSA').

   MPM submitted that the Complainant signed MPM's application form dated 19/06/2014. MPM noted that, in this application form, Dean Stogsdill from Continental Wealth Management ('CWM') is identified as

[12] *A fol.* 7
[13] *A fol.* 42-45

the Complainant's professional adviser. On the application form, Dean Stogsdill declares and confirms that the investment advice provided to the member is within the investment guidelines.

MPM stated that the policy was assigned to MPM from the previous Trustee following a notice of assignment dated 12 September 2014. MPM noted that a valuation was also provided by SEB Life International as at the date of the transfer – and that the policy value as at 30/09/14 was GBP94,589.80. MPM further noted that the Complainant made no comment about the losses suffered to his investment prior to the transfer to MPM.

MPM submitted that the fact find attached to the complaint was a document dated 30/11/11, before MPM became Trustee and RSA. It was also noted that such document was entered into between CWM and the Complainant and completed by them. MPM further noted that the information which was provided to MPM is that contained in the Application Form and not in the fact find completed by CWM. MPM pointed out that on the application form, the Complainant declared that the applicable risk profile to him is '*Medium*'.

MPM submitted that the member and the adviser appointed by the member, select the investments and that the adviser ensures that the investments comply with the member's risk profile. MPM noted that the RSA then reviews this in line with the risk profile on file, to ensure that it broadly reflects the risk profile and offers diversification.

6. It was noted that CWM has ceased trading and is no longer operating and that this was the only reason why the Complainant filed a claim against MPM and not against CWM. The Service Provider submitted that the proper respondent to this claim is CWM and/or Trafalgar. It was pointed out that MPM no longer accepted business from CWM as from September 2017 and that MPM is aware that CWM ceased trading on or around 29 September 2017.

MPM noted that it is not aware of any attempt by the Complainant to initiate proceedings against CWM or its officials and/or Trafalgar and/or

Global Net, which advised the Complainant to invest in products which have led to the Complainant's losses.

MPM submitted that any business introduced to it by CWM, fell within the MFSA's Pension Rules for Service Providers, as they relate to RSAs. MPM further replied that it does not work on a commission basis and that it neither receives commissions, nor pays commissions to any third parties.

7. MPM noted that the Complainant claims that the first annual statement provided to him is that attached to his complaint. MPM submitted that this was not the first annual statement provided by MPM and that the Complainant was provided with annual statements for the years 2014-2016 inclusive. MPM noted that the first annual statement was for the year ended 30 September 2014 were the valuation was GBP94,589.80. MPM also referred to a valuation provided by SEB Life International as at 20/03/2014 which predates MPM's role.

   MPM submitted that the annual member statements also noted '*Medium*' as the Complainant's attitude to risk. MPM noted that the Complainant did not raise any complaint with MPM at any time before February 2018.

8. MPM noted that the Complainant alleges that MPM has failed in its duty of care and has failed in exercising due diligence. It was also noted that the Complainant further alleges that MPM have failed to comply with their own published conditions/regulations. MPM replied that it has fulfilled all its obligations vis-à-vis the Complainant as will be shown throughout the course of the proceedings.

9. MPM noted that the Complainant alleges that his funds were invested into high risk structured notes. MPM replied that the investments made were in line with the Complainant's risk profile and in line with the guidelines applicable at the time of the Complainant's application with MPM, as will be shown throughout the course of the proceedings.

   MPM submitted that it had controls in place to ensure that the dealing instructions received by it bore the signature of the Complainant, ensuring the investment was directed by him and the Adviser appointed by the Complainant, in line with the attitude to risk and was then reviewed against the Scheme investment guidelines. MPM also noted that the dealing instructions were submitted by the appointed adviser, CWM, and met Momentum's Investment Guidelines.

MPM pointed out that it is aware that Old Mutual International Ireland Limited ('OMI'), the bond provider,[14] has initiated legal action against one of the structured note providers (Leonteq Securities AG) for losses incurred by the ultimate holders of the bonds, such as the Complainant. It was noted that it is OMI, and not MPM, who was pursuing litigation against Leonteq.

The Service Provider further noted that it charges a fixed fee for the services that it provides and that this fee does not change regardless of the underlying investment which the Complainant was advised to invest into by CWM. It was claimed that MPM did not accordingly stand to make any gain or benefit from any particular underlying investment.

10. MPM noted that the Complainant further alleges that there was a lack of communication by MPM. The Service Provider submitted that this was false. MPM noted that the Complainant was kept updated through the annual statements sent to him. MPM noted that furthermore, with respect to the Complainant's allegation that MPM has purposely delayed its response to him, MPM replied that it required more time than anticipated in order to reply to the Complainant's letter. MPM noted that it informed the Complainant of the delay and provided its reasons therefor. MPM rejected the allegation that it was allegedly purposely delaying a response so that the Complainant would not have all information available – MPM noted that the Complainant was at liberty to file his Complaint if a reasonable time would have been allowed for MPM's response, as he did.

[14] The investments within the Retirement Scheme were undertaken via a life assurance bond provided by an insurance company – *A fol.* 120

MPM noted that it provided its reply to the Complainant on the 11 May 2018 and that all documents requested by the Complainant were sent to him, including the dealing instructions.

11. MPM submitted that, as already stated in its reply, it is not licensed to and does not provide investment advice and that it did not provide investment advice to the Complainant. MPM further submitted that the Complainant declared on the application forms that he acknowledged that the services provided by MPM did not extend to financial, legal, tax or investment advice as per declaration 8 on page 14 of the said form.

    To further reinforce the point that MPM does not provide investment advice, it was submitted that an entire section of the terms and conditions of business as attached to the application form, is dedicated solely to this point, as per page 10 of the application form.

12. MPM submitted that it is not responsible for payment of any of the amounts claimed by the Complainant. MPM further replied that the refund of the fees referred to in the complaint was a gesture of goodwill on its part and in no way constituted an admission of liability.

13. MPM further submitted that it has not committed any fraud, nor has it acted negligently. MPM stated that it has not breached any of its obligations in any way and submitted that the losses sustained by the Complainant are attributable to the adviser appointed by the Complainant.

    MPM pointed out that the Complainant must show that it was MPM's actions or omissions which caused the loss being alleged. MPM replied that in the absence of the Complainant proving this causal link, MPM cannot be found responsible for the Complainant's claims.

Having heard the parties and seen all the documents and submissions made including the affidavits, the notes of submissions, the additional submissions made and respective attachments,

Further Considers:

Preliminary Plea regarding the Competence of the Arbiter

The Service Provider raised the plea that the Arbiter does not have the competence to consider this case because it is time-barred under Article 21(1)(c) of Chapter 555, Article 21(1)(c) stipulates:

'An Arbiter shall also have the competence to hear complaints in terms of his functions under article 19(1) in relation to the conduct of a financial service provider occurring after the coming into force of this Act, if a complaint is registered in writing with the financial services provider not later than two years from the day on which the complainant first had knowledge of the matters complained of.'

The Act came into force on 18 April 2016. As to the '*conduct of a financial service provider*' the law does not refer to the date when a transaction takes place but refers to the date when the alleged misconduct took place.

In the case of a financial investment, the conduct of the service provider cannot be determined from the date when the transaction took place and, it is for this reason that the legislator departed from that date and laid the emphasis on the date when the conduct took place.

In this case, the conduct complained of involves the conduct of the Service Provider as trustee and retirement scheme administrator of the Scheme, which role MPM occupied since 22 July 2014, upon the member's acceptance into the Scheme, and continued to occupy after the coming into force of the Act. It is noted that the complaint in question also involves the conduct of the Service Provider during the period in which CWM was permitted by MPM to act as the adviser of the complainant.

In terms of Article 21(1)(c), the complainant had two years to complain to the Service Provider '*from the day on which the complainant first had knowledge of the matters complained of*'.

The fact that the Complainant was sent an Annual Member Statement, as stated by the Service Provider in its notes of submissions, could not be considered as enabling the Complainant to have knowledge about the matters complained of. This taking into consideration a number of factors including that the said Annual Member Statement was a highly generic report which only listed the underlying life assurance policy. The Annual Member Statement issued to the Complainant by MPM included no details of the specific underlying investments held within the policy, which investments contributed to the losses and are being disputed by the Complainant. Hence, the Complainant was not in a position to know from the Annual Member Statement he received what investment transactions were actually being carried out within his portfolio of investments.

It is also noted that the Annual Member Statement sent to the Complainant by the Service Provider had even a disclaimer highlighting that certain underlying investments may show a value reflecting an early encashment value or potentially a zero value prior to maturity and that such value did not reflect the true performance of the underlying assets.

The disclaimer read as follows:

'*Investment values are provided to Momentum Pensions Malta Limited by Investment Platforms who are responsible for the accuracy of this information. Every effort has been made to ensure that this statement is correct but please accept this statement on this understanding.*

Certain underlying assets with the Investment may show a value that reflects an early encashment value or potentially a zero value prior to maturity date. This will not reflect the true current performance of such underlying assets.'

Such a disclaimer did not reveal much to the Complainant about the actual state of the investment and the whole scenario could not have reasonably enabled the Complainant to have knowledge about the matters being complained of.

Moreover, the Arbiter, makes reference to Case Number 137/2018, whereby it results that the Service Provider itself declared in July 2015, in reply to a member's concern regarding losses, that:

'…. *whilst we, as Trustees, will review and assess any losses,* ***these can only be on the maturity of the note,***[15] *as any valuations can and will be distorted ahead of the expiry'.*[16]

The Service Provider did not prove the date of maturity of the structured notes comprising the portfolio of the Complainant. According to a statement presented by the Complainant, certain structured notes were still within his portfolio after the coming into force of the Act with certain notes also sold in May 2017.[17]

The Arbiter has also discovered from Case Number 127/2018 that the Service Provider sent communication to all members of the Scheme with respect to the position with CWM.[18] In this regard, in September 2017, members were notified by MPM about the suspension of the terms of business that MPM had with CWM. Later, in October 2017, MPM also notified the members of the Scheme about the full withdrawal of such terms of business with CWM.

The Complainant made a formal complaint with the Service Provider on the 12 February 2018[19] and, therefore, within the two-year period established by Art. 21(1)(c) of Chapter 555.

Therefore, the Service Provider did not prove that the Complainant raised the complaint '*later than two years from the day on which the complainant first had knowledge of the matters complained of*'.

It is also noted that not even two years had passed from the coming into force of Chapter 555 of the Laws of Malta and the date when the formal complaint was made by the Complainant with the Service Provider.

For the above-stated reasons, this plea is being rejected and the Arbiter declares that he has the competence to deal with this complaint.

The Merits of the Case

[15] Emphasis of the Arbiter
[16] Case Number 137/2018 (*a fol.* 7 of the file) decided today
[17] *A fol.* 18
[18] Case Number 127/2018 (*a fol.* 53 of the file) decided today
[19] *A fol.* 29/30

The Arbiter will decide the complaint by reference to what, in his opinion, is fair, equitable and reasonable in the particular circumstances and substantive merits of the case.[20]

The Arbiter is considering all pleas raised by the Service Provider relating to the merits of the case together to avoid repetition and to expedite the decision as he is obliged to do in terms of Chapter 555[21] which stipulates that he should deal with the complaint in 'an economical and expeditious manner'.

The Complainant

The Complainant is of British nationality and resided in Spain at the time of application as per the details contained in the *Application for Membership of the Momentum Malta Retirement Trust* ('the Application Form for Membership').

It was not proven during the case that the Complainant was a professional investor. Accordingly, the Complainant can be treated as a retail client.

The Complainant was accepted by MPM as member of the Retirement Scheme in the year 2014.

The Service Provider

The Retirement Scheme was established by Momentum Pensions Malta Limited ('MPM'). MPM is licensed by the MFSA as a Retirement Scheme Administrator[22] and acts as the Retirement Scheme Administrator and Trustee of the Scheme.[23]

The Legal Framework

The Retirement Scheme and MPM are subject to specific financial services legislation and regulations issued in Malta, including conditions or pension rules issued by the MFSA in terms of the regulatory framework applicable for personal retirement schemes.

[20] Cap. 555, Art. 19(3)(b)
[21] Art. 19(3)(d)
[22] *https://www.mfsa.mt/financial-services-register/result/?id=3453*
[23] Role of the Trustee, pg. 4 of MPM's Scheme Particulars (attached to Stewart Davies's affidavit).

The Special Funds (Regulation) Act, 2002 ('SFA') was the first legislative framework which applied to the Scheme and the Service Provider. The SFA was repealed and replaced by the Retirement Pensions Act (Chapter 514 of the Laws of Malta) ('RPA'). The RPA was published in August 2011 and came into force on the 1 January 2015.[24]

There were transitional provisions in respect of those persons who, upon the coming into force of the RPA, were registered under the SFA. The Retirement Pensions (Transitional Provisions) Regulations, 2015 provided that retirement schemes or any person registered under the SFA had one year from the coming into force of the RPA to apply for authorisation under the RPA.

In terms of Regulation 3 of the said Transitional Provisions Regulations, such schemes or persons continued to be governed by the provisions of the SFA until such time that these were granted authorisation by MFSA under the RPA.

As confirmed by the Service Provider, registration under the RPA was granted to the Retirement Scheme and the Service Provider on 1 January 2016 and hence the framework under the RPA became applicable as from such date.[25]

Despite not being much mentioned by MPM in its submissions, the Trusts and Trustees Act (Chapter 331 of the Laws of Malta), ('TTA') is also much relevant and applicable to the Service Provider, as per Article 1(2) and Article 43(6)(c) of the TTA, in light of MPM's role as the Retirement Scheme Administrator and Trustee of the Retirement Scheme.

Indeed, Article 1(2) of the TTA provides that:

'*The provisions of this Act, except as otherwise provided in this Act, shall apply to all trustees, whether such trustees are authorised, or are not required to obtain authorisation in terms of article 43 and article 43A*', with Article 43(6)(c) in turn providing that '*A person licensed in terms of the Retirement Pensions Act to act as a Retirement Scheme Administrator acting as a trustee*

[24] *Retirement Pensions Act, Cap. 514/Circular letter issued by the MFSA https://www.mfsa.com.mt/firms/regulation/pensions/pension-rules-applicable-as-from-1-january-2015/*

[25] As per pg. 1 of the affidavit of Stewart Davies and the Cover Page of MPM's Registration Certificate issued by MFSA dated 1 January 2016 attached to his affidavit.

to retirement schemes shall not require further authorisation in terms of this Act provided that such trustee services are limited to retirement schemes …'.

Particularities of the Case

The Retirement Scheme in respect of which the Complaint is being made

The Momentum Malta Retirement Trust ('the Retirement Scheme' or 'the Scheme') is a trust domiciled in Malta. It was granted a registration by the MFSA[26] as a Retirement Scheme under the Special Funds (Regulation) Act in April 2011[27] and under the Retirement Pensions Act in January 2016.[28]

As detailed in the Scheme Particulars dated May 2018 presented by MPM during the proceedings of this case, the Scheme '*was established as a perpetual trust by trust deed under the terms of the Trusts and Trustees Act (Cap. 331) on the 23 March 2011*'[29] and is '*an approved Personal Retirement Scheme under the Retirement Pensions Act 2011*'.[30]

The Scheme Particulars specify that:

'*The purpose of the Scheme is to provide retirement benefits in the form of a pension income or other benefits that are payable to persons who are resident both within and outside Malta. These benefits are payable after or upon retirement, permanent invalidity or death*'.[31]

The case in question involves a member-directed personal retirement scheme where the Member was allowed to appoint an investment adviser to advise him on the choice of investments.

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[26] https://www.mfsa.com.mt/financial-services-register/result/?id=3454

[27] Registration Certificate dated 28 April 2011 issued by MFSA to the Scheme (attached to Stewart Davies's Affidavit).

[28] Registration Certificate dated 1 Jan 2016 issued by MFSA to the Scheme (attached to Stewart Davies's Affidavit).

[29] Important Information section, Pg. 2 of MPM's Scheme Particulars (attached to Stewart Davies's Affidavit).

[30] Regulatory Status, Pg. 4 of MPM's Scheme Particulars (attached to Stewart Davies's Affidavit).

[31] *Ibid.*

Prior to joining the Scheme, the Complainant was already invested into the '*Spanish Portfolio Bond*', this being a policy issued by SEB Life International which policy commenced on the 7 February 2012 ('the SEB Policy').[32]

The said policy issued by SEB International was assigned to MPM as Trustee of the Retirement Scheme following the Complainant's membership of the Retirement Scheme on the 12 September 2014.[33] At the time of assignment of the policy to MPM, there were already certain investments underlying the policy which were made prior to membership and which MPM accepted to retain within the Scheme following the assignment of the policy to MPM. The SEB Policy and the underlying assets within the SEB Policy, became assets of the Scheme since 12 September 2014.

The valuation for the SEB Policy as at 30 September 2014, indicated the policy to comprise one investment, the RBC Diversified Blue Chip Income Notes Series 1 ('RBC Investment'), valued at GBP70,391.38 which comprised 74.42% of the policy value at the time.[34] The said valuation also indicated cash holdings of GBP24,198.42 with such cash holdings comprising 25.58% of the indicated policy at the time. Pending transactions into two Leonteq structured notes were also indicated in the valuation marked 30 September 2014.[35]

After the transfer of the policy to MPM as trustees of the Retirement Scheme on 12 September 2014, additional investments to the RBC Investment were made within the SEB Policy as summarised in the table of investments provided by the Service Provider.[36]

The Service Provider indicated the valuation of the Retirement Scheme amounting to GBP58,643 as at 27 April 2018 with a loss (which excluded fees) of GBP8,836 as at that date.[37] The loss experienced by the Complainant is thus higher when taking into account the fees incurred and paid within the Scheme's structure.

[32] *A fol.* 61-62
[33] *A fol.* 62
[34] *A fol.* 63
[35] *A fol.* 63/64
[36] *A fol.* 196
[37] *Ibid.*

The Service Provider does not explain whether the loss (excluding fees) it indicated in the '*current valuation*' for the Complainant relates to realised or paper losses or both.

Investment Adviser

Continental Wealth Management ('CWM') was the investment adviser appointed by the Complainant.[38] The role of CWM was to advise the Complainant regarding the assets held within the Retirement Scheme.

It is noted that in the notices issued to members of the Scheme in September and October 2017, MPM described CWM as '*an authorised representative/agent of Trafalgar International GmbH'*, where CWM's was Trafalgar's '*authorised representative in Spain and France'*.

In its reply, MPM explained *inter alia* that CWM '*is a company registered in Spain. Before it ceased to trade, CWM acted as adviser and provided financial advice to investors. CWM was authorised to trade in Spain and in France by Trafalgar International GmbH*'.[39]

In its submissions, it was further explained by MPM that '*CWM was appointed agent of Trafalgar International GmbH ('Trafalgar') and was operating under Trafalgar International GmbH licenses*'[40] and that Trafalgar '*is authorised and regulated in Germany by the Deutsche Industrie Handelskammer (IHK) Insurance Mediation licence 34D Broker licence number: D-FE9C-BELBQ-24 and Financial Asset Mediator licence 34F: D-F-125-KXGB-53'*.[41]

Underlying Investments

The investments undertaken within the life assurance policy of the Complainant were summarised in the table of investment transactions

[38] As per pg. 1/2 of MPM's reply to the OAFS.
[39] Pg. 1 of MPM's reply to the OAFS.
[40] Para. 39, Section E, titled *'CWM and Trafalgar International GmbH'* of the affidavit of Stewart Davies.
[41] *Ibid.*

included as part of the '*Investor Profile*' information sheet provided by the Service Provider in respect of the Complainant.[42]

The extent of investments in structured notes, indicated as '*SN*' in the column titled '*Asset Type*' in the said table of investment transactions, was substantial as can be seen in the said table.

The said table indicates that the portfolio of investments for the Complainant involved substantial investments in structured notes with the portfolio comprising at times solely, or predominantly, of structured notes during the tenure of CWM as investment adviser.

The underlying policy, the Spanish Portfolio Bond issued by SEB Life International ('the SEB Policy') commenced on 7 February 2012 but was assigned to MPM as Trustee of the Retirement Scheme on 12 September 2014.[43] As confirmed by both the Complainant and the Service Provider, upon the assignment of the said policy to MPM, the policy included an investment into the RBC Diversified Blue Chip Income Notes Series 1 GBP (XS0741467756), ('the RBC Investment).[44] The Service Provider indicated that the RBC Investment was originally purchased for the amount of GBP140,000 on 24 February 2012 and that this investment matured for the amount of GBP55,989 in 2017.[45]

The investments that were undertaken within the SEB Policy after this was assigned to MPM as trustee of the Scheme were also summarised in the table of investment transactions provided by the Service Provider.[46] The said table indicates that from September 2014 till 10 December 2015 a purchase of 6 structured notes and 1 fund were made as per the column titled '*Asset Type*' indicated in the table.[47]

The table indicates that apart from the original investment into the RBC Diversified Blue Chip Income Notes, which was a structured note itself as

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[42] Attachment to the '*Additional submissions*' made by MPM in respect of the Complainant.
[43] *A fol.* 62
[44] *A fol.* 15, 33 & 63
[45] *A fol.* 196
[46] *Ibid.*
[47] *Ibid.*

indicated in the same table, the bulk of the investments were done into Leonteq/EFG structured notes. The investments into structured notes undertaken following the assignment of the SEB Policy to MPM as trustee of the Scheme comprised 3 investments into structured notes undertaken in 2014 for a total of GBP26,153,[48] two investments in structured notes for a total of EUR17,000 undertaken in 2015,[49] and an investment of GBP3,000 into another structured note undertaken in 2015.[50] An investment of GBP5,000 was also undertaken into a fund in December 2015.

Further Considerations

Responsibilities of the Service Provider

MPM is subject to the duties, functions and responsibilities applicable as a Retirement Scheme Administrator and Trustee of the Scheme.

Obligations under the SFA, RPA and directives/rules issued thereunder

As indicated in the MFSA's Registration Certificate dated 28 April 2011 issued to MPM under the SFA, MPM was required, in the capacity of Retirement Scheme Administrator, '*to perform all duties as stipulated by articles 17 and 19 of the Special Funds (Regulation) Act, 2002 … in connection with the ordinary or day-to-day operations of a Retirement Scheme registered under the [SFA]*'.

The obligations of MPM as a Retirement Scheme Administrator under the SFA are outlined in the Act itself and the various conditions stipulated in the original Registration Certificate which *inter alia* also referred to various Standard Operational Conditions (such as those set out in Sections B.2, B.5, B.7 of Part B and Part C) of the '*Directives for Occupational Retirement Schemes, Retirement Funds and Related Parties under the Special Funds (Regulation) Act, 2002'* ('the Directives').

In terms of the said Registration Certificate issued under the SFA, MPM was also required to assume and carry out, on behalf of the Scheme, any functions

[48] GBP10,725 + GBP10,428 + GBP5,000 (*A fol.* 196)
[49] Eur9,000 + Eur8,000 (*A fol.* 27)
[50] *A fol.* 196

and obligations applicable to the Scheme under the SFA, the regulations and the Directives issued thereunder.

Following the repeal of the SFA and issue of the Registration Certificate dated 1 January 2016 under the RPA, MPM was subject to the provisions relating to the services of a retirement scheme administrator in connection with the ordinary or day-to-day operations of a Retirement Scheme registered under the RPA. As a Retirement Scheme Administrator, MPM was subject to the conditions outlined in the '*Pension Rules for Service Providers issued under the Retirement Pensions Act*' ('the Pension Rules for Service Providers') and the '*Pension Rules for Personal Retirement Schemes issued under the Retirement Pensions Act*' ('the Pension Rules for Personal Retirement Schemes').

In terms of the said Registration Certificate issued under the RPA, MPM was also required to assume and carry out on behalf of the Scheme any functions and obligations applicable to the Scheme under the RPA, the regulations and the Pension Rules issued thereunder.

One key duty of the Retirement Scheme Administrator emerging from the primary legislation itself is the duty to *'act in the best interests of the scheme'* as outlined in Article 19(2) of the SFA and Article 13(1) of the RPA.

From the various general conduct of business rules/standard licence conditions applicable to MPM in its role as Retirement Scheme Administrator under the SFA/RPA regime respectively, it is pertinent to note the following general principles:[51]

a) Rule 2.6.2 of Part B.2.6 titled '*General Conduct of Business Rules applicable to the Scheme Administrator*' of the Directives issued under the SFA, which applied to MPM as a Scheme Administrator under the SFA, provided that:

   '*The Scheme Administrator* ***shall act with due skill, care and diligence – in the best interests of the Beneficiaries*** …'.

   The same principle continued to apply under the rules issued under the RPA. Rule 4.1.4, Part B.4.1 titled '*Conduct of Business Rules*' of the Pension Rules for Service Providers dated 1 January 2015 issued in terms of the

[51] Emphasis added by the Arbiter.

RPA, and which applied to MPM as a Scheme Administrator under the RPA, provided that:

'*The Service Provider* ***shall act with due skill, care and diligence*** *…*'.

b) Rule 2.7.1 of Part B.2.7 titled '*Conduct of Business Rules related to the Scheme's Assets*', of the Directives issued under the SFA, which applied to MPM as a Scheme Administrator under the SFA, provided that:

'***The Scheme Administrator shall arrange for the Scheme assets to be invested in a prudent manner and in the best interest of Beneficiaries*** *…*'.

The same principle continued to apply under the rules issued under the RPA. Standard Condition 3.1.2, of Part B.3 titled '*Conditions relating to the investments of the Scheme*' of the Pension Rules for Personal Retirement Schemes dated 1 January 2015 issued in terms of the RPA, provided that:

'***The Scheme's assets shall be invested in a prudent manner and in the best interest of Members and Beneficiaries*** *and also in accordance with the investment rules laid out in its Scheme Particulars and otherwise in the Constitutional Document and Scheme Document.*'

c) Rule 2.6.4 of Part B.2.6 titled '*General Conduct of Business Rules applicable to the Scheme Administrator*' of the Directives issued under the SFA, which applied to MPM as a Scheme Administrator under the SFA provided that:

'*The Scheme Administrator shall organise and control its affairs in a responsible manner and* ***shall have adequate operational, administrative*** *and financial procedures* ***and controls in respect of its own business and the Scheme*** *to ensure compliance with regulatory conditions and to enable it to be effectively prepared to manage, reduce and mitigate the risks to which it is exposed …'.*

The same principle continued to apply under the rules issued under the RPA. Standard Condition 4.1.7, Part B.4.1 titled '*Conduct of Business Rules*' of the Pension Rules for Service Providers dated 1 January 2015 issued in terms of the RPA, provided that:

'*The Service Provider shall organise and control its affairs in a responsible manner and* ***shall have adequate operational, administrative*** *and financial* *procedures* ***and controls in respect of its own business and the Scheme*** *or Retirement Fund, as applicable, to ensure compliance with regulatory conditions and to enable it to be effectively prepared to manage, reduce and mitigate the risks to which it is exposed*.'

Standard Condition 1.2.2, Part B.1.2 titled '*Operation of the Scheme*, of the Pension Rules for Personal Retirement Schemes dated 1 January 2015 issued in terms of the RPA, also required that:

'***The Scheme shall organise and control its affairs in a responsible manner and shall have adequate operational, administrative*** *and financial procedures* ***and controls to ensure compliance with all regulatory requirements***'.

Trustee and Fiduciary obligations

As highlighted in the section titled '*The Legal Framework*' above, the Trusts and Trustees Act ('TTA'), Chapter 331 of the Laws of Malta is also relevant for MPM considering its capacity as Trustee of the Scheme. This is an important aspect on which not much emphasis has been made by the Service Provider in its submissions.

Article 21(1) of the TTA which deals with the '*Duties of trustees*', stipulates a crucial aspect, that of the ***bonus paterfamilias***, which applies to MPM.

The said article provides that:

'(1) ***Trustees shall in the execution of their duties and the exercise of their powers and discretions act <u>with the prudence, diligence and attention of a bonus paterfamilias</u>,*** *act in utmost good faith and avoid any conflict of interest'.*

It is also to be noted that Article 21(2)(a) of the TTA, further specifies that:

'Subject to the provisions of this Act, trustees shall carry out and administer the trust according to its terms; and, subject as aforesaid, the trustees shall ensure that the trust property is vested in them or is under their control and shall, so far as reasonable and subject to the terms of the trust, safeguard the trust property from loss or damage *…'.*

In its role as Trustee, MPM was accordingly duty bound to administer the Scheme and its assets to high standards of diligence and accountability.

The trustee, having acquired the property of the Scheme in ownership under trust, had to deal with such property '*as a fiduciary acting exclusively in the interest of the beneficiaries, with honesty, diligence and impartiality*'.[52]

As has been authoritatively stated:

'*Trustees have many duties relating to the property vested in them. These can be summarized as follows:* ***to act diligently, to act honestly and in good faith and with impartiality towards beneficiaries, to account to the beneficiaries and to provide them with information, to safeguard and keep control of the trust property and to apply the trust property in accordance with the terms of the trust'***.[53]

The fiduciary and trustee obligations were also highlighted by MFSA in a recent publication where it was stated that:

'In carrying out his functions, a RSA [retirement scheme administrator] of a Personal Retirement Scheme has a fiduciary duty to protect the interests of members and beneficiaries*. It is to be noted that by virtue of Article 1124A of the Civil Code (Chapter 16 of the Laws of Malta), the RSA has certain fiduciary obligations to members or beneficiaries, which arise in virtue of law, contract, quasi-contract or trusts. In particular,* ***the RSA shall act honestly, carry out his obligations with utmost good faith, as well as exercise the diligence of a bonus paterfamilias in the performance of his obligations****'.*[54]

Although this Consultation Document was published in 2017, MFSA was basically outlining principles established both in the TTA and the Civil Code which had already been in force prior to 2017.

The above are considered to be crucial aspects which should have guided MPM in its actions and which shall accordingly be considered in this decision.

[52] Pg. 174, '*An Introduction to Maltese Financial Services Law*', Editor Dr Max Ganado, Allied Publications 2009.
[53] Pg. 178, '*An Introduction to Maltese Financial Services Law*', Editor Dr Max Ganado, Allied Publications 2009.
[54] Page 9 – Consultation Document on Amendments to the Pension Rules issued under the Retirement Pensions Act [MFSA Ref: 09-2017], dated 6th December 2017.

Other relevant Aspects

One other important duty relevant to the case in question relates to **the oversight and monitoring function of the Service Provider in respect of the Scheme including with respect to investments**. As acknowledged by the Service Provider whilst MPM's duties did not involve the provision of investment advice, however, MPM did '*… **retain the power to ultimately decide whether to proceed with an investment or otherwise***'.[55]

Once an investment decision is taken by the member and his investment adviser and such decision is communicated to the retirement scheme administrator, MPM explained that as part of its duties:

***'The RSA will then ensure that the proposed trade on the dealing instruction, when considered in the context of the entire portfolio, ensures a suitable level of diversification, is in line with the member's attitude to risk and in line with the investment guidelines (applicable at the time the trade is placed)** …'.*[56]

MPM had accordingly the final say prior to the placement of a dealing instruction, in that, if MPM was satisfied that the level of diversification is suitable and in order, and the member's portfolio as a whole is in line with his attitude to risk and investment guidelines '*the dealing instruction will be placed with the insurance company and the trade will be executed. **If the RSA is not so satisfied, then the trade will not be proceeded with***'.[57]

This, in essence, reflected the rationale behind the statement reading:

'*I accept that I or my designated professional adviser may suggest investment preferences to be considered, however, **the Retirement Scheme administrator will retain full power and discretion for all decisions relating to the purchase, retention and sale of the investments** within my Momentum Pensions Retirement Fund*' which featured in the '*Declarations*' section of the Application Form for Membership signed by the Complainant.

[55] Para. 17, page 5 of the affidavit of Stewart Davies
[56] Para. 31, Page 8 of the affidavit of Stewart Davies
[57] Para. 33, Page 9 of the affidavit of Stewart Davies. Para. 17 of Page 5 of the said affidavit also refers.

The MFSA regarded the oversight function of the Retirement Scheme Administrator as an important obligation where it emphasised, in recent years, the said role.

The MFSA explained that it:

'… is of the view that as specified in SLC 1.3.1 of Part B.1 (Pension Rules for Retirement Scheme Administrators) of the Pension Rules for Service Providers, the RSA, in carrying out his functions, shall act in the best interests of the Scheme members and beneficiaries. The MFSA expects the RSA to be diligent and to take into account his fiduciary role towards the members and beneficiaries, at all times, irrespective of the form in which the Scheme is established. The RSA is expected to approve transactions and to ensure that these are in line with the investment restrictions and the risk profile of the member in relation to his individual member account within the Scheme'.[58]

The MFSA has also highlighted the need for the retirement scheme administrator to query and probe the actions of a regulated investment adviser stating that *'the MFSA also remains of the view that the RSA is to be considered responsible to verify and monitor that investments in the individual member account are diversified, and the RSA is not to merely accept the proposed investments, but it should acquire information and assess such investments'.* [59]

Despite that the above quoted MFSA statements were made in 2018, an oversight function applied during the period relating to the case in question as explained earlier on.

As far back as 2013, MPM's Investment Guidelines indeed also provided that:

[58] Pg. 7 of the MFSA's Consultation Document dated 16 November 2018 titled '*Consultation on Amendments to the Pension Rules for Personal Retirement Schemes issued under the Retirement Pensions act*' (MFSA Ref. 15/2018) - https://www.mfsa.com.mt/publications/policy-and-guidelines/consultation-documents-archive/.

[59] Pg. 9 of MFSA's Consultation Document dated 16 November 2018 titled *'Consultation on Amendments to the Pension Rules for Personal Retirement Schemes issued under the Retirement Pensions Act' (MFSA Ref. 15/2018).*

'***The Trustee need to ensure that the member's funds are invested in a prudent manner and in the best interests of the beneficiaries. The key principle is to ensure that there is a suitable level of diversification** …'*,[60]

whilst para. 3.1 of the section titled 'Terms and Conditions' of the Application Form for Membership into the Scheme also provided *inter alia* that:

'… ***in its role as Retirement Scheme Administrator [MPM] will exercise judgement as to the merits or suitability of any transaction** …*'.

Other Observations and Conclusions

Reference to Old Mutual International

In its reply, MPM pointed out that '*Momentum is aware that Old Mutual International Ireland Limited ('OMI'), the bond provider, has initiated legal action against one of the structured note providers (Leonteq Securities AG ('Leonteq')) for losses incurred by the ultimate holders of the bonds, such as the Complainant'*.[61]

It is pertinent to note that Old Mutual International is however <u>not</u> the bond provider for the Complainant. In the Complainant's case, the underlying bond is actually the Spanish Portfolio Bond, which is issued by a different provider, this being SEB Life International.[62]

Key considerations relating to the principal alleged failures

The Arbiter will now consider the principal alleged failures. The principal alleged failures of the Service Provider that were made in this regard include that (i) MPM failed to exercise due diligence and monitor or question: the original investment at the time MPM took over as Trustee; as well as the actions of CWM with respect to the portfolio CWM created until it ceased business (ii) MPM failed to comply with its own published conditions/ regulations (iii) MPM allowed investments into high risk structured products

[60] Investment Guidelines titled January 2013, attached to the affidavit of Stewart Davies. The same statement is also included in page 9 of the Scheme Particulars of May 2018 (also attached to the same affidavit).
[61] *A fol.* 44
[62] *A fol.* 62 & 196

(iv) there was a lack of communication by MPM throughout including on the high risks, losses and dealing transactions.

General observations

On a general note, it is noted that MPM did not provide investment advice in relation to the underlying investments of the member-directed scheme. The role of the investment adviser was the duty of other parties, such as CWM. **This would reflect on the extent of responsibility that the financial adviser and the RSA and Trustee had in this case as will be later seen in this decision.**

However, despite that the Retirement Scheme Administrator was not the entity which provided the investment advice to invest in the contested financial instruments, **MPM had nevertheless certain obligations to undertake in its role of Trustee and Scheme Administrator. The obligations of the trustee and retirement scheme administrator in relation to a retirement plan are important ones and could have a substantial bearing on the operations and activities of the scheme and affect directly, or indirectly, its performance**.

Consideration thus needs to be made as to whether MPM failed in any relevant obligations and duties, and if so, to what extent any such failures are considered to have had a bearing or otherwise on the financial performance of the Scheme and the resulting losses for the Complainant.

A. <u>The appointment of the Investment Adviser</u>

It is noted that the Complainant chose the appointment of CWM to provide him with investment advice in relation to the selection of the underlying investments and composition of the portfolio within the member-directed Scheme. **However, from its part, MPM allowed and/or accepted CWM to provide investment advice to the Complainant within the Scheme's structure**. **MPM even had itself an introducer agreement with CWM**.

There are a number of aspects which give rise to concerns on the diligence exercised by MPM when it came to the acceptance of, and dealings with, the investment adviser as further detailed below.

Inappropriate and inadequate material issues involving the Investment Adviser

i. *Inaccurate, incorrect and unclear information relating to the adviser in MPM's Application Form for Membership*

It is considered that **MPM accepted and allowed inaccurate, incorrect and unclear information relating to the Adviser to prevail in its own Application Form for Membership**. MPM should have been in a position to identify, raise and not accept the material deficiencies included in the Application Form.

If inaccurate, unclear and incorrect material information was made in the Application Form for Membership on such a key party it was only appropriate and in the best interests of the complainant, and reflective of the role as Trustee as a *bonus paterfamilias*, for MPM to raise and flag such matters to the Complainant and not accept such inadequacies in its form. **MPM had ultimately the prerogative whether to accept the application, the selected investment adviser and also decide with whom to enter into terms of business**.

The section titled '*Professional Adviser's Details*' in the Application Form for Membership for the Complainant indicated '*Continental Wealth Management'*/'*CWM'* as the company's name of the professional adviser.

In the same section of the Application Form, CWM was indicated as having a registered address in Spain and that it was regulated with '*Inter Alliance World Net*' ('*Inter-Alliance'*) being identified as the regulator of the professional adviser.

The Arbiter considers the reference to *Inter-Alliance* as regulator to be inadequate and misleading.

The reference to '*Inter-Alliance*' was not defined or explained in the Application Form. Neither was such reference ever explained or referred to during the comprehensive submissions made by the Service Provider during the proceedings of the case. It has not emerged either that Inter-

Alliance is, or was, a regulatory authority for investment advisers in Spain or in any other jurisdiction. It appears that '*Inter Alliance WorldNet Insurance Agents & Advisers Ltd*' was a service provider itself in Cyprus, but clearly it was not a regulatory authority.[63] N**o evidence was submitted by MPM of CWM being truly regulated.**

The reference to Inter-Alliance could not have reasonably provided any comfort to MPM that this was a regulator of CWM and neither that there was some form of regulation and adequate controls and/or supervision on CWM equivalent to that applicable for regulated investment services providers.

ii. *Lack of clarity/convoluted information*

It is noted that with respect to the policy issued by SEB Life International ('SEB'), the '*Endorsement Following Notice of Assignment*' letter sent by SEB to MPM makes reference to '*Inter-Alliance – Continental Wealth Management*' as '*Intermediary Name*'. There is lack of clarity of the rationale for references to both entities in the intermediary name.

The capacity in which CWM was acting, such as, as an agent of another firm, did not emerge either from the Application Form for Membership or other documentation indicated to have been received or provided to the Complainant.

iii. *No proper distinctions between CWM, Inter-Alliance and/or Trafalgar*

It has not emerged that the Complainant was provided with clear and adequate information regarding the respective roles and responsibilities between CWM, Inter-Alliance and/or Trafalgar.

If CWM was acting as an appointed agent of another party, such capacity, as an agent of another firm, should have been clearly reflected in the application forms and other documentation relating to the Scheme. Relevant explanations and implications of such agency

[63] https://international-adviser.com/iaw-fined-cypriot-regulator/

relationship and respective responsibilities should have also been duly indicated without any ambiguity.

During the proceedings of this case MPM has not provided evidence of any agency agreement between CWM and Inter-Alliance and/or between CWM and Trafalgar.

iv. *No regulatory approval in respect of CWM*

During the proceedings of this case no evidence was provided about the regulatory status of CWM. As indicated earlier, MPM provided no details about Inter-Alliance, and in its submissions only referred to the alleged links between CWM and Trafalgar. MPM only provided a copy of the authorisations issued to Trafalgar International GmbH in Germany which just indicated that Trafalgar (and not CWM) held an authorisation as at 05.02.2016 as '*Investment intermediary*' and '*Insurance intermediary and insurance consultant*' from IHK Frankfurt am Main, the Chamber of Commerce and Industry in Frankfurt, with the '*Insurance Mediation licence 34D Broker licence number: D-FE9C-BELBQ-24 and Financial Asset Mediator licence 34F: D-F-125-KXGB-53*'.[64]

With respect to authorisations issued by IHK, the Arbiter makes reference to Case 068/2018 and Case 172/2018 against MPM in which correspondence was produced involving replies issued by IHK in 2018 to queries made in respect of CWM. In this regard, it is noted that in an email from IHK dated 19 April 2018, IHK indicated *inter alia* that it was not aware of an official affiliation between CWM and Trafalgar and that Trafalgar held the financial investment intermediation licence (34f para. 1 GewO) from June 2013 until March 2016 where the licence was '*not extendable'* and *'even back then it did not cover the activities of another legal personality*'.[65]

[64] Copy of authorisations issued to Trafalgar were attached to the Reply of MPM submitted before the Arbiter for Financial Services and/or specifically referred to in para. 39 Section E, titled '*CWM and Trafalgar International GmbH*' in the affidavit of Stewart Davies.
[65] Email from IHK dated 19 April 2018 – *A fol.* 166/167 of Case 068/2018, decided today

Similarly, in a letter dated 20 April 2018 issued by IHK it was *inter alia* noted by IHK that '*Trafalgar International GmbH is a German limited company headquartered in Frankfurt am Main. The company currently holds a licence under 34d para.1 German Trade Law (German: Gewerbeordnung, GewO) (insurance intermediation). The German licence as an insurance intermediary cannot be extended to another legal personality and it does not authorize the licence holder to regulate other insurance or financial investment intermediaries.'*[66]

MPM's statement that CWM '*was operating under Trafalgar International GmbH licenses*'[67] has not been backed up by any evidence during the proceedings of this case and has actually been contradicted by communications issued by IHK as indicated above. It is accordingly clear that no comfort can be taken from the authorisation/s held by Trafalgar.

Indeed, no evidence of any authorisation held by CWM in its own name or as an agent of a licensed institution, authorising it to provide advice on investment instruments and/or advice on investments underlying an insurance policy has, ultimately been produced by the service provider to substantiate its defence on this matter, or emerged during the proceedings of this case.

In the absence of such evidence, **the mere explanations provided by MPM regarding the regulatory status of CWM, including that CWM '*was authorised to trade in Spain and in France by Trafalgar International GmbH*',[68] are rather vague, inappropriate and do not provide sufficient comfort of an adequate regulatory status for CWM to undertake the investment advisory activities provided to the Complainant**.

This also taking into consideration that:

[66] Letter from IHK dated 20 April 2018 – *A fol.* 12/13 of Case 172/2018, decided today

[67] Para. 39, Section E titled *'CWM and Trafalgar International GmbH'* of the affidavit of Stewart Davies.

[68] Pg. 1, Section A titled '*Introduction*', of the Reply of MPM submitted before the Arbiter for Financial Services.

(a) Trafalgar is itself no regulatory authority but a licensed entity itself. Similarly, Inter-Alliance was no regulatory authority;

(b) the lack of clarity as to the regulatory status of the investment adviser included in the Application Form for Membership;

(c) legislation covering the provision of investment advisory services in relation to investment instruments, namely the Markets in Financial Instruments Directive (2004/39/EC) already applied across the European Union since November 2007.

No evidence was provided that CWM, an entity indicated as being based in Spain, held any authorisation to provide investment advisory services, in its own name or in the capacity of an agent of an investment service provider under MiFID.

Article 23(3) of the MiFID I Directive, which applied at the time, indeed provided specific requirements on the registration of tied agents.[69]

No evidence of CWM featuring in the tied agents register in any EU jurisdiction was either produced or emerged.

Neither was any evidence produced of any exemption from licence under MiFID or that CWM held an authorisation or exemption under any other applicable European legislation for the provision of the contested investment advice.

The Service Provider noted *inter alia* that '*CWM was appointed agent of Trafalgar International GmbH*'.[70]

The nature of the agency agreement that CWM was claimed to have was not explained nor defined, and it was not indicated either in terms of which European financial services legislation such agency agreement was in force and permitted the provision of the disputed investment advice. Nor evidence of any agency agreement existing between CWM

[69] https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32004L0039&from=EN
[70] Para. 39, Section E, titled '*CWM and Trafalgar International GmbH'* of the affidavit of Stewart Davies.

and any other party was produced during the proceedings of these cases as indicated above.

Other observations and synopsis

As explained above, albeit being selected by the Complainant, the investment adviser was however accepted, at MPM's sole discretion, to act as the Complainant's investment adviser within the Scheme's structure.

The responsibility of MPM in accepting and allowing CWM to act in the role of investment adviser takes even more significance when one takes into consideration the scenario in which CWM was accepted by MPM. As indicated above, MPM accepted CWM when it was being stated in its own application form that CWM was a regulated entity, but no evidence has transpired that this was so, as amply explained above.

MPM allowed and left uncontested incorrect, misleading and unclear key information to feature in its own Application Form for Membership of the Retirement Scheme with respect to the regulatory status of the investment adviser. In so doing, it abetted a fundamentally wrong impression and perception that the investment adviser being selected was regulated when, in reality, no evidence has emerged that CWM was indeed a regulated entity.

The Service Provider argued *inter alia* in its submissions that it was not required, in terms of the rules, to require the appointment of an adviser which was regulated during the years 2013-2015 under the SFA regime and until the implementation of Part B.9 titled '*Supplementary Conditions in the case of entirely Member Directed Schemes*' of the Pension Rules for Personal Retirement Schemes issued in terms of the RPA updated in December 2018, where the latter clearly introduced the requirement for the investment adviser to be regulated.

However, the Arbiter believes that MPM as Trustee had in any case the obligation to act with the required diligence of a *bonus paterfamilias* throughout, and was duty bound to raise with the Complainant, and not

itself accept, material aspects relating to the investment adviser, which it should have reasonably been in a position to know that where incorrect, misleading and inappropriate. Instead it chose to allow and accept such material, incorrect, misleading and inappropriate information relating to the adviser to even prevail in its own application form.

The appointment of an entity such as CWM as investment adviser meant, in practice, that there was a layer of safeguard in less for the Complainant as compared to a structure where an adequately regulated adviser is appointed. An adequately regulated financial adviser is subject to, for example, fitness and properness assessments, conduct of business requirements as well as ongoing supervision by a financial services regulatory authority. MPM, being a regulated entity itself, should have been duly and fully cognisant of this. It is was only in the best interests of the Complainant for MPM to ensure that the Complainant had correct and adequate key information about the investment adviser.

Besides the issue of the regulatory status of the adviser, MPM also allowed and left uncontested important information, which was convoluted, misleading, unclear and lacking, with respect to the investment adviser, namely in relation to:

- **CWM's alleged role as agent of another party, and the respective responsibilities of CWM and its alleged principal/s;**
- **the entity actually taking responsibility for the investment advice given to the Complainant given the references to different parties;**
- **the distinctions between CWM and Inter Alliance/Trafalgar.**

It is also to be noted that apart from the above, MPM had itself a business relationship with CWM, having accepted it to act as its introducer of business. Such relationship gave rise to potential conflicts of interest, where an entity whose actions were subject to certain

oversight by MPM on one hand was, on the other hand, channelling business to MPM.

Even in case where under the previous applicable regulatory framework, an unregulated adviser was allowed by the trustee and scheme administrator to provide investment advice to the member of a member-directed scheme, **one would, at the very least, reasonably expect the retirement scheme administrator and trustee of such a scheme to exercise even more caution and prudence in its dealings with such a party.**

This is even more so, when the activity in question, that is one involving the recommendations on the choice and allocation of underlying investments, has such a material bearing on the financial performance of the Scheme and the objective to provide for retirement benefits.

In the case in question, it would have accordingly been only reasonable to expect MPM, as part of its essential and basic obligations and duties as a retirement scheme administrator and trustee of the Scheme, to have an even higher level of disposition in the probing and querying of the actions of an unregulated investment adviser in order to also ensure that the interests of the member of the scheme are duly safeguarded and risks mitigated in such circumstances.

The Arbiter does not have comfort that such level of diligence and prudence has been actually exercised by MPM for the reasons already stated in this section of the decision.

B. ***<u>The permitted portfolio composition</u>***

Investment into Structured Notes

Preliminary observations

The sale of, and investment into, structured notes is an area which has attracted various debates internationally including reviews by regulatory authorities over the years. Such debates and reviews have been occurring even way back since the time when the Retirement Scheme was granted registration in 2011.

The Arbiter considers that caution was reasonably expected to be exercised with respect to investments in, and extent of exposure to, such products since the time of the Scheme's registration. Even more so when taking into consideration the nature of the Retirement Scheme and its specific objective.

Nevertheless, the exposure to structured notes allowed within the Complainant's portfolio was extensive, with the insurance policy underlying the Scheme being at times fully or predominantly invested into such products.

A typical definition of a structured note provides that:

'*A structured note is a debt security issued by financial institutions; its return is based on equity indexes, a single equity, a basket of equities, interest rates, commodities or foreign currencies. The return on a structured note is linked to the performance of an underlying asset, group of assets or index*'.[71]

A structured note is further described as:

'*a debt obligation – basically like an IOU from the issuing investment bank – with an embedded derivative component; in other words, it invests in assets via derivative instruments'*.[72]

The Arbiter notes that the fact sheets presented by the Complainant in respect of structured notes that featured in his portfolio as well as the fact sheet of the original RBC Investment highlighted a number of risks in respect of the capital invested into these products.

Apart from *inter alia* the credit risk of the issuer and the liquidity risk, the fact sheets of the said structured products also highlighted risk warnings about the notes not being capital protected, warning that the investor could possibly receive less than the original amount invested, or potentially even losing all of the investment.

[71] https://www.investopedia.com/terms/s/structurednote.asp
[72] https://www.investopedia.com/articles/bonds/10/structured-notes.asp

A particular feature emerging of the type of structured notes invested into, involved the application of capital buffers and barriers. In this regard, the fact sheets of such products described and included warnings that the invested capital was at risk in case of a particular event occurring. Such event typically comprised a fall, observed on a specific date of more than a percentage specified in the respective fact sheet, in the value of any underlying asset to which the structured note was linked. The fall in value would typically be observed on maturity/final valuation of the note. The specified percentage in the fall in value mentioned in the relevant fact sheets presented was of 50% of the initial value as indicated by the Service Provider itself in its submissions. The underlying asset to which the structured notes were linked comprised listed companies.

The said fact sheets further included a warning, on the lines of, '*If any stock has fallen by more than 50% (a Barrier breach) then investors receive the performance of the Worst Performing Stock at Maturity*'.[73] Such features and warnings featured, in essence, in the fact sheets of similar structured notes.

It is accordingly clear that there were certain specific risks in various structured products invested into and there were material consequences if just one asset, out of a basket of assets to which the note was linked, fell foul of the indicated barrier. The implication of such a feature should have not been overlooked nor discounted. Given the particular features of the structured notes invested into, neither should have comfort been derived regarding the adequacy of such products just from the fact that the structured notes were linked to a basket of fully quoted shares.

The Arbiter would also like to make reference to a particular communication presented in another separate case made against MPM which is relevant to the case in question. In this regard, it is particularly revealing to note the statements made by Trafalgar itself, in its email communication dated 17 September 2017 to CWM, **wherein MPM was in copy**, and which communication was presented in Case Number 185/2018 against MPM,

[73] Example – Fact Sheet of the RBC Diversified Blue Chip Income Notes – Series 1 - https://www.yumpu.com/en/document/read/38731551/rbc-diversified-blue-chip-income-notes-series-1-fund-platform

decided today. In the said case, MPM did not contest that such communication was untrue or did not exist, but only challenged the way in which the said email was obtained by the complainant.

The email sent by Trafalgar's official *inter alia* stated the following:

'***Structured Notes – It is my opinion we need to get as far away from these vehicles as possible. They have no place in an uneducated investor's portfolio and when they breech their barriers untold amounts of damage is done***'.[74]

Such a statement indeed summarily highlighted the pertinent issues with respect to investments in structured notes which are relevant to the case in question.

Excessive exposure to structured products and to single issuers

As indicated above, the portfolio of investments in respect of the Complainant at times comprised solely and/or predominantly of structured products. Such excessive exposure to structured products occurred over a long period of time. This clearly emerges from the Table of Investments forming part of the '*Investor Profile*' provided by the Service Provider.

In addition, the said table indicates investments resulting in high exposures to the same single issuer/s, either through a singular purchase and/or through cumulative purchases in products issued by the same issuer.

Even in case where the issuer of the structured product was a large institution, the Arbiter does not however consider this to justify or make the high exposure to single issuers acceptable even more in the Scheme's context. The maximum limits relating to exposures to single issuers outlined in the MFSA rules and MPM's own Investment Guidelines did not make any distinctions according to the standing of the issuer. Hence, the maximum exposure limits to single counterparties should have been applied and ensured that they are adhered to across the board. The credit risk of the respective issuer was indeed still one of the risks highlighted in various fact

[74] Emphasis added by the Arbiter.

sheets, as presented to and sourced by the OAFS, of structured products invested into.

In Specie Transfer and subsequent investments

The Arbiter has considered the overall portfolio allowed by MPM within the Scheme's structure, that is, the *in specie* investment accepted by MPM upon the Complainant becoming a member of the Scheme and also the subsequent investments made following the assignment of the SEB Policy to MPM.

It is noted that upon the assignment of the SEB Policy to MPM as trustee of the Retirement Scheme, the SEB Policy already had a substantial exposure to a single investment, the RBC Investment, which was over 70% of the policy value at the time.

Despite such substantial investment, the portfolio still continued to be constructed predominantly with structured products.

As to the investment undertaken prior to membership and transferred *in specie* to the Scheme, it is noted that MPM, as Trustee and Retirement Scheme Administrator, accepted the said investment within the Scheme's structure and also allowed it to be retained within the Retirement Scheme.

MPM was ultimately in a position not to accept such investment at the time when it considered whether to accept or not the Complainant as member of the Scheme. Accordingly, it is considered that MPM cannot completely wash its hands from such investment with the excuse that this was undertaken prior to membership.

Furthermore, it has not been indicated, nor any evidence has emerged that MPM, as Trustee and Retirement Scheme Administrator of the Scheme, expressed, at any time, any reservations or warnings to the Complainant about the said substantial RBC Investment. It has neither been indicated that the sale of such product prior to its maturity was not possible and/or that the early redemption of such investment was not in the Complainant's best interests. During the proceedings of this case it was neither indicated nor proven that the Complainant risked sustaining a greater loss on such investment had such product been redeemed prior to maturity.

In the particular circumstances of this case, it is accordingly considered that whilst MPM cannot be held responsible for the loss in value of the investment prior to the transfer and assignment of the policy to the Service Provider, MPM should, however, be responsible for the position starting from the date since it took over as Trustee and Retirement Scheme Administrator. Accordingly, in the particular circumstances, it is considered that responsibility should be attributed to MPM from the date when the investment was accepted by it within the Scheme's structure and until the said RBC Investment remained under MPM's control in its capacity as Trustee and Scheme Administrator.

With respect to the RBC Investment, the Service Provider argued that '*any capital loss suffered by the Complainant (which was substantial) for this investment cannot be attributed to Momentum*'.[75]

The Service Provider further argued *inter alia* that '*Whilst the product did provide coupons … the capital loss … was nevertheless £84,011*' on this product and that this was '*why the portfolio has overall suffered a loss*'.[76]

The Service Provider seems to attribute the overall loss on the portfolio to the RBC Investment. Whilst a loss has been indicated on such investment, the documents produced during this case indicate that this was not the only loss experienced by the Complainant, as material losses were also experienced on various other investments within the portfolio. In the Table of Investments, the Service Provider indicated one sale of a structured product, the Leonteq 1.5yrs Multi Barrier Express Cert on 3 Companies 9% Coupon, which sale is indicated as yielding a capital gain of GBP352.[77] The statement presented by the Complainant of the SEB Policy as at March 2018, however, also indicated the sale of various structured products on which substantial capital losses were experienced such as:[78]

- the Leonteq (EFG) Express Cert on 4 Companies Multi Barrier AC Quanto EUR which was purchased for EUR9,000 and sold at a value of EUR333.96;

[75] *A fol.* 193
[76] *Ibid.*
[77] *A fol.* 196 – Sale value of GBP10,780 less Purchase value of GBP10,428
[78] *A fol.* 18-19 & 27

- the Leonteq (EFG) 8.4%pa Multi Barrier Reverse Conv on 4 Companies AC Quanto EUR which was purchased for EUR8,000 and sold at a value of EUR1,060.63;
- the Leonteq 2yr Multi Barrier Express Cert on 3 Companies 10% pa which was purchased for GBP5,000 and sold at nil value;
- the Leonteq 1.5yrs 50% Multi Barrier Express Cert 9% pa which was purchased for GBP10,725 and sold at a value of GBP5,941.63.

Portfolio not reflective of the MFSA rules

The high exposure to structured products as well as high exposure to single issuers, which was allowed to occur by the Service Provider in the Complainant's portfolio, jars with the regulatory requirements that applied to the Retirement Scheme at the time, particularly Standard Operational Condition ('SOC') 2.7.1 and 2.7.2 of the '*Directives for Occupational Retirement Schemes, Retirement Funds and Related Parties under the Special Funds (Regulation) Act, 2002'*, ('the Directives') which applied from the Scheme's inception in 2011 until the registration of the Scheme under the RPA on 1 January 2016. The applicability and relevance of these conditions to the case in question was highlighted by MPM itself.[79]

SOC 2.7.1 of Part B.2.7 of the Directives required *inter alia* that the assets were to '*be invested in a prudent manner and in the best interest of beneficiaries …*'.

SOC 2.7.2 in turn required the Scheme to ensure *inter alia* that, the assets of a scheme are '*invested in order to ensure the security, quality, liquidity and profitability of the portfolio as a whole*'[80] and that such assets are '*properly diversified in such a way as to avoid accumulations of risk in the portfolio as a whole*'.[81]

SOC 2.7.2 of the Directives also provided other benchmarks including for the portfolio to be '*predominantly invested in regulated markets*';[82] to be '*properly*

[79] Para. 21 & 23 of the Note of Submissions filed by MPM in 2019.
[80] SOC 2.7.2 (a)
[81] SOC 2.7.2 (b)
[82] SOC 2.7.2 (c)

diversified in such a way as to avoid excessive exposure to any particular asset, issuer or group of undertakings'[83] where the exposure to single issuer was: in the case of investments in securities issued by the same body limited to no more than 10% of assets; in the case of deposits with any one licensed credit institution limited to 10%, which limit could be increased to 30% of the assets in case of EU/EEA regulated banks; and where in case of investments in properly diversified collective investment schemes, which themselves had to be predominantly invested in regulated markets, limited to 20% of the scheme's assets for any one collective investment scheme.[84]

Despite the standards of SOC 2.7.2, MPM allowed the portfolio of the Complainant to, at times, comprise solely and/or predominantly of structured products. Individual exposures to single issuers were at times higher than 20% and in certain instances, such as the investment into the RBC Diversified Blue Chip Income Notes – Series 1 ('the RBC Investment'), even higher than 30%, the latter being the maximum limit applied in the Rules to relatively safer investments such as deposits as outlined above.

The structured products invested into were also not indicated, during the proceedings of this case, as themselves being traded in or dealt on a regulated market. The portfolio also included, on a cumulative basis, material positions into high risk investments. The high risk is reflected in the high rate of returns of 8.4%, 9% and 10% p.a. which featured in the name of various structured products invested into.

*Portfolio not reflective of MPM's **own** Investment Guidelines*

In its submissions MPM produced a copy of the Investment Guidelines marked '*January 2013'* and '*Mid-2014'*, which guidelines featured in the Application Form for Membership, and also Investment Guidelines marked '*2015'*, *'2016', '*Mid-2017'*, '*Dec-2017'* and '*2018'* where, it is understood the latter respectively also formed part of the Scheme's documentation such as the Scheme Particulars issued by MPM.

[83] SOC 2.7.2 (e)
[84] SOC 2.7.2 (h)(iii) & (v)

Despite that the Service Provider claimed that the investments made were in line with the Investment Guidelines, **MPM has however not adequately proven such a claim**.

As indicated, the investment portfolio in the case reviewed in this decision was at times either solely and/or predominantly invested in structured notes for a long period of time. It is unclear how such a portfolio composition truly satisfied certain conditions specified in MPM's own Investment Guidelines such as:

(i) **The requirement that the member's assets had to be '*predominantly invested in regulated markets*'**

This was a condition which prevailed in all of the presented MPM's Investment Guidelines since January 2013 till that of 2018.[85]

The said requirement of being '*predominantly invested in regulated markets*' meant, and should have been construed to mean, that investments had to be predominantly invested in listed instruments, that is financial instruments that were admitted to trading. With reference to industry practice, the terminology of '*regulated markets*' is referring to a regulated exchange venue (such as a stock exchange or other regulated exchange). The term '*regulated markets*' is in fact commonly referred to, defined and applied in various EU Directives relating to financial services, including diversification rules applicable on other regulated financial products.[86] Hence, the interpretation of '*regulated markets*' has to be seen in such context.

The reference to '*predominantly invested in regulated markets*' cannot be interpreted as referring to the status of the issuers of the products and it is typically the product itself which has to be traded on the regulated market and not the issuer of the product.

[85] Investment Guidelines attached to the affidavit of Stewart Davies.

[86] Such as UCITS schemes - the Undertakings for Collective Investments in Transferable Securities (UCITS) Directive (Directive 2009/65/EC as updated). The Markets in Financial Instruments Directive (MiFID) (Directive 2004/39/EC as repealed by Directive 2014/65/EU) also includes a definition as to what constitutes a 'r*egulated market'.*

Moreover, a look through approach could not either be sensibly applied to the structured notes for the purposes of such condition taking into consideration the nature and particular features of the structured notes invested into.

No evidence was submitted that predominantly the portfolio, which at times comprised solely or predominantly of structured notes, constituted listed structured notes. The fact sheets sourced and presented by the Complainant of structured notes forming part of the portfolio, actually indicated that the products in question were not listed on an exchange.

On its part, the Service Provider did not prove that the portfolio of the Complainant was '*predominantly invested in regulated markets*' on an ongoing basis.

Furthermore, when investment in unlisted securities was itself limited to 10% of the Scheme assets, as stipulated throughout MPM's own Investment Guidelines for 2013 to 2018, it is unclear how the Trustee and Scheme Administrator chose to allow much higher exposures (as will be indicated further below) to structured notes, a debt security, which were themselves unlisted.

(ii) **The requirement relating to the liquidity of the portfolio**

The Investment Guidelines of MPM marked January 2013 required no more than a '*maximum of 40% of the fund*[87] *in assets with liquidity of greater than 6 months.*' This requirement remained, in essence, also reflected in the Investment Guidelines marked 'Mid-2014' which read '*Has a maximum of 40% of the fund in assets with expected liquidity of greater than 6 months*', as well as in the subsequent Investment Guidelines marked 2015 till 2018 which were updated by MPM and tightened further to read a '*maximum of 40% of the fund in assets with expected liquidity of greater than 3 months but not greater than 6 months*'.

[87] The reference to *'fund'* is construed to refer to the member's portfolio.

It is evident that the scope of such requirement was to ensure the liquidity of the portfolio as a whole by having the portfolio predominantly (that is, at least 60%) exposed to liquid assets which could be easily redeemed within a short period of time, that is 3-6 months (as reflected in the respective conditions) whilst limiting exposure to those assets which take longer to liquidate to no more than 40% of the portfolio.

With reference to the Complainant's portfolio, it is noted that the structured notes invested into typically had a maturity or investment term of 1-2 years and, at times, even higher up to 5 years as evidenced in the product fact sheets. The bulk of the assets within the policy was, at times, invested into just one or very few structured notes. It is unclear how the 40% maximum limit referred to above could have been satisfied in such circumstances where the portfolio was predominantly invested into structured notes which themselves had long investment terms.

It is further noted that the fact sheets of the said unlisted structured products included reference to the possibility of a secondary market existing for such structured notes. In this regard, a buyer had to be found in the secondary market in case one wanted to redeem a holding into such structured note prior to its maturity.

The secondary market could, however, not have provided an adequate level of comfort with respect to liquidity.

There were indeed various risks highlighted in relation to the secondary market as amply reflected in the risk warnings emerging in the said fact sheets.

The said risk warnings highlighted the risks related to the availability of such market (as the secondary market had to be in the first place offered by the issuer), as well as the limitations of the said market. They also highlighted the lower price that could be sought on this market.

In this regard, there was the risk that the price of the structured note on the secondary market could be well below the initial capital invested.

For example, the note issued by RBC included the risk disclaimer that:

'***Any secondary market provided by Royal Bank of Canada is subject to change and may be stopped without notice and investors may therefore be unable to sell or redeem the Notes until their maturity. If the Notes are redeemed early, they may be redeemed at a level less than the amount originally invested***'.

Similar warnings feature in other fact sheets.

MPM should have been well aware of the risks associated with the secondary market. It has indeed itself seen the material lower value that could be sought on such market in respect of the structured notes invested into. The lower values of the structured notes on the secondary market was indeed affecting the value of the Scheme as can be deduced from the respective Annual Member Statements that MPM itself produced.

Hence, no sufficient comfort about liquidity could have possibly been derived with respect to the secondary market in case of unlisted structured notes.

The Arbiter is not accordingly convinced that the conditions relating to liquidity were being adequately adhered to, nor that the required prudence was being exercised with respect to the liquidity of the portfolio, when considering the above-mentioned aspects and when keeping into context that the portfolio of investments that was allowed to develop within the Retirement Scheme was at times solely and/or predominantly invested in the said structured notes.

Even if one had to look at the composition of the portfolio purely from other aspects, there is still undisputable evidence of non-compliance with other requirements detailed in MPM's own Investment Guidelines. This is particularly so with respect to the requirements applicable regarding the proper diversification, avoidance of excessive exposure and permitted maximum exposure to single issuers.

In addition to the exposure of 76.20% of the policy value to the RBC Investment that was accepted and allowed by MPM in the Scheme's portfolio, Table A below shows another example of excessive single exposures allowed within the portfolio at the time of purchase. The excessive exposure to single counterparties clearly emerges from the '*Table of Investments*' forming part of the '*Investor Profile*' produced by MPM as part of its submissions.

Table A – Example of Excessive Exposure to a Single Issuer of Structured Notes ('SNs')

Exposure to single issuer in % terms of the policy value at time of purchase	*Issuer*	*Description*
20.08%	EFG	2 SNs issued by EFG both purchased in September 2014 respectively comprised 10.18%, and 9.90% of the policy value at the time of purchase thus resulting in an overall exposure to the same issuer of 20.08% of the policy value at the time of purchase.

Irrespective of whether or not the particular investment indicated had actually yielded a profit, **the fact that such high exposure to a single counterparty was allowed in the first place indicates, in itself, the lack of prudence and excessive exposure and risks to single counterparties that were allowed to be taken on a general level**.

The fact that such high exposure to a single counterparty was allowed in the first place indicates, in itself, the lack of prudence and excessive exposure and risks to single counterparties that were allowed to be taken.

The Arbiter notes that the Service Provider has along the years revised various times the investment restrictions specified in its own '*Investment Guidelines*' with respect to structured products, both in regard to maximum exposures to structured products and maximum exposure to single issuers of such products.

The exposure to structured notes and their issuers was indeed progressively and substantially reduced over the years in the said Investment Guidelines.

The specified maximum limit of 66% of the portfolio value in structured notes having underlying guarantees which featured in the '*Investment Guidelines*' marked 2015[88] was reduced to 40% of the portfolio's value in the '*Investment Guidelines*' marked December 2017[89] and, subsequently, reduced further to 25% in the '*Investment Guidelines*' for 2018.[90]

Similarly, the maximum exposure to single issuers for '*products with underlying guarantees*', that is, structured products as referred to by MPM itself in the '*Investment Guidelines*' marked Mid-2014 and 2015, specifically limited maximum exposure to the same issuer default risk to no more than (33.33%), one third of the portfolio. The maximum limit to such products was subsequently reduced to 25%, one quarter of the portfolio, in the '*Investment Guidelines'* marked 2016[91] and mid-2017,[92] reduced further to 20% in the '*Investment Guidelines*' marked December 2017 and, subsequently, to 12.5% in the '*Investment Guidelines*' for 2018. Even before the Investment Guidelines of Mid-2014, MPM's Investment Guidelines of January 2013 still limited exposure to individual investments (aside from collective investment schemes) to 20%.

The Arbiter considers that the high exposure to structured products and single issuers in the Complainant's portfolio jarred and did not reflect to varying degrees with one or more of MPM's own investment guidelines applicable at the time, most particularly with respect to the following guidelines:[93]

Investment Guidelines marked 'Mid-2014':
• *Where products with underlying guarantees are chosen,* ***no more than one third of the overall portfolio to be subject to the same issuer default risk****.*

[88] MPM's Investment Guidelines '*2015*' as attached to the affidavit of Stewart Davies
[89] MPM's Investment Guidelines '*Dec-2017'* as attached to the affidavit of Stewart Davies
[90] MPM's Investment Guidelines *'2018'* as attached to the affidavit of Stewart Davies
[91] MPM's Investment Guidelines '*2016'* as attached to the affidavit of Stewart Davies
[92] MPM's Investment Guidelines '*Mid-2017'* as attached to the affidavit of Stewart Davies
[93] Emphasis in the mentioned guidelines added by the Arbiter.

*In addition, **further consideration needs to be given to** the following factors:* • *…* • ***Credit risk of underlying investment*** • *…*
• *In addition to the above, the portfolio must be constructed in such a way as to **avoid excessive exposure**:* • *…* • ***To any single credit risk***
<u>Investment Guidelines marked '2015':</u>
• *Where products with underlying guarantees are chosen, i.e. **Structured Notes**, these will be **permitted up to a maximum of 66% of the portfolio's values**,*
*with **no more than one third** of the portfolio to be **subject to** the **same issuer default risk**.*
*In addition, **further consideration needs to be given to** the following factors:* • *…* • ***Credit risk of underlying investment*** • *…* …
• *In addition to the above, the portfolio must be constructed in such a way as to **avoid exposure**:* • *…* • ***To any single credit risk**.*
<u>Investment Guidelines marked '2016' & 'Mid-2017':</u>

• *Where* ***products with underlying Capital guarantees*** *are chosen,* ***i.e. Structured Notes****, these will be* ***permitted up to a maximum of 66% of the portfolio's values****,*
with ***no more than one quarter*** *of the portfolio to be* ***subject to*** *the* ***same issuer/ guarantor default risk****.*
• ***Where no such Capital guarantee exists****, investment will be* ***permitted up to a maximum of 50% of the portfolio's value****.* …
• *In addition,* ***further consideration needs to be given to*** *the following factors:* • *…* • ***Credit risk of underlying investment****;* …
• *In addition to the above, the portfolio must be constructed in such a way as to* ***avoid exposure****:* • *…* • ***To any single credit risk****.*

Besides the mentioned excessive exposure to single issuers, it is also noted that additional investments into structured notes were observed[94] to have been allowed to occur within the portfolio, in excess of the limits allowed on the maximum exposure to such products. MPM's Investment Guidelines of 2015, 2016 and mid-2017 specifically mentioned a maximum limit of 66% of the portfolio value to structured notes. In the case reviewed, the Service Provider still continued to allow further investments into structured products at one or more instances when the said limits should have applied.

The additional investments also occurred despite the portfolio being already exposed to structured notes more than the said percentage at the time when the additional purchase was being made.

[94] '*Table of Investments*' in the '*Investor Profile*' provided by MPM refers.

For the reasons amply explained, the Arbiter has no comfort that in its role as a Scheme Administrator and Trustee, MPM has truly ensured that the Scheme's investments were generally, and at all times, managed in accordance with relevant legislation and regulatory requirements, as well as in accordance with the rules and terms and conditions of the Trust.

The Service Provider did not help its case by not providing detailed information on the underlying investments as already stated in this decision. Although the Service Provider filed a Table of Investments, it did not provide adequate information to explain the portfolio composition and justify its claim that the portfolio was diversified. It did not provide fact sheets in respect of the investments comprising the portfolio of the Complainant and it did not demonstrate the features and the risks attached to the investments.

The Service Provider's mere indication that it made in its submissions, that the portfolio was diversified through a number of structured notes with a range of issuers and with diversified listed underlyings, cannot reasonably provide in itself sufficient and adequate comfort on the level of diversification/adequacy of such investments. Various other aspects cannot be ignored by the Service Provider.

Such aspects include, but are not limited to:

- the nature of the structured products being invested into and the effects any events or barriers that may form part of the key features of such products, would have on the investment if and when such events occur as already detailed above;
- the potential rate of returns as indicative of the level of risk being taken;
- the level of risks ultimately exposed to in the respective product and in the overall portfolio composition; and
- not the least, the issuer/counterparty risk being taken.

The extent of losses experienced on the capital of the Complainant's portfolio, as indicated by MPM itself,[95] is in itself indicative of the failure in adherence with the applicable conditions on diversification and avoidance of excessive exposures. Otherwise, material losses, which are reasonably not expected to occur in a pension product whose scope is to provide for retirement benefits, would have not occurred.

Apart from the fact that no sensible rationale has emerged for limiting the composition of the pension portfolio solely and/or predominantly to structured products, no adequate and sufficient comfort has either emerged that such composition reflected the prudence expected in the structuring and composition of a pension portfolio. Neither that the allocations were in the best interests of the Complainant despite his selected risk profile.

In the circumstance where the portfolio of the Complainant was at times solely and/or predominantly invested in structured products with a high level of exposure to single issuer/s, and for the reasons amply explained above, the Arbiter does not consider that there was proper diversification nor that the portfolio was at all times '*invested in order to ensure the security quality, liquidity and profitability of the portfolio as a whole*'[96] and '*properly diversified in such a way as to avoid accumulations of risk in the portfolio as a whole*'.[97]

Apart from the fact that the Arbiter does not have comfort that the portfolio was reflective of the conditions and investment limits outlined in the MFSA's Rules and MPM's own Investment Guidelines, **it is also being pointed out that over and above the duty to observe specific maximum limits relating to diversification as may have been specified by rules, directives or guidelines applicable at the time, the behaviour and judgement of the Retirement Scheme Administrator and Trustee of the Scheme is expected to, and should have gone beyond compliance with maximum percentages and was to, in practice, reflect the spirit and principles behind the regulatory framework and in practice promote the scope for which the Scheme was established.**

[95] '*Investor Profile*' attached with the Additional Submissions made by MPM in 2019.
[96] SOC 2.7.2(a) of Part B.2.7 of the Directives.
[97] SOC 2.7.2(b) of Part B.2.7 of the Directives

The excessive exposure to structured products and their issuers nevertheless clearly departed from such principles and cannot ultimately be reasonably considered to satisfy and reflect in any way a suitable level of diversification nor a prudent approach.

This is even more so when considering the crucial aim of a retirement scheme being that to provide for retirement benefits – an aspect which forms the whole basis for the pension legislation and regulatory framework to which the Retirement Scheme and MPM were subject to. The provision of retirement benefits was indeed the Scheme's sole purpose as reflected in the Scheme Particulars.

C. *The Provision of information*

With respect to reporting to the member of the Scheme, MPM mentioned and referred only to the Annual Member Statement in its submissions. The said annual statements issued by the Service Provider to the Complainant are, however, highly generic reports which only listed the underlying life assurance policy and included no details of the underlying investments that is the structured notes comprising the portfolio of investments.

Hence, the extent and type of information sent to the Complainant by MPM as a member of the Scheme in respect of his underlying investments is considered to have been lacking and insufficient.

SOC 9.3(e) of Part B.9 of the Pension Rules for Personal Retirement Schemes of 1 January 2015 already provided that, in respect of member directed schemes, '*a record of all transactions (purchases and sales) occurring in the member's account during the relevant reporting period should be provided by the Retirement Scheme Administrator to the Member at least once a year and upon request …*'. [98]

It is noted that the Pension Rules for Personal Retirement Schemes under the RPA became applicable to MPM on 1 January 2016 and that, as per the MFSA's

[98] The said condition was further revised and updated as per condition 9.5(e) of Part B.9 of the Pension Rules for Personal Retirement Schemes indicated as *'Issued: 7 January 2015/Last updated: 28 December 2018'*

communications presented by MPM,[99] Part B.9 of the said rules did not become effective until the revised rules issued in 2018.

Nevertheless, it is considered that even where such condition could have not strictly applied to the Service Provider from a regulatory point of view, the Service Provider as a Trustee, obliged by the TTA to act as a *bonus paterfamilias* and in the best interests of the members of the Scheme, should have felt it its duty to provide members with detailed statements and information on the underlying investments.

Moreover, prior to being subject to the regulatory regime under the RPA, the Service Provider was indeed already subject to regulatory requirements relating to the provision of adequate information to members such as the following provisions under the SFA framework:

- Standard Operating Conditions 2.6.2 and 2.6.3 of Section B.2 of the Directives for Occupational Retirement Schemes, Retirement Funds and Related Parties under the Special Funds (Regulation) Act, 2002[100] respectively already provided that:

  '2.6.2 *The Scheme Administrator shall act with due skill, care and diligence in the best interests of the Beneficiaries. Such action shall include:*

  …

  b) ensuring that contributors and prospective contributors are provided with adequate information on the Scheme to enable them to take an informed decision…';

  '2.6.3 *The Scheme Administrator shall ensure the adequate disclosure of relevant material information to prospective and actual contributors in a way which is fair, clear and nor misleading. This shall include:*

[99] MFSA's letter dated 11 December 2017, attached to the Note of Submissions filed by MPM in 2019.
[100] Condition 2.2 of the Certificate of Registration issued by the MFSA to MPM dated 28 April 2011 included reference to Section B.2 of the said Directives.

…

b) *reporting fully, accurately and promptly to contributors the details of transactions entered into by the Scheme…*'.

There is no apparent and justified reason why the Service Provider did not report itself on key information such as the composition of the underlying investment portfolio, which it had in its hands as the trustee of the underlying life assurance policy held in respect of the Complainant.

The general principles of acting in the best interests of members and those relating to the duties of trustee as already outlined in this decision[101] and to which MPM was subject to, should have prevailed and should have guided the Service Provider in its actions to ensure that the Member was provided with an adequate account of the underlying investments within his portfolio.

In view of the Complainant's remarks that he was never asked to sign one of the dealing instructions, the provision of details on the underlying investments could have ultimately enabled the member of the Scheme to highlight any transactions on which there was an issue.[102]

Causal link and Synopsis of main aspects

The actual cause of the losses experienced by the Complainant on his account within the Retirement Scheme **cannot** just be attributed to the under-performance of the investments as a result of general market and investment risks and/or the issues alleged against one of the structured note providers, as MPM has *inter alia* suggested in these proceedings.

There is sufficient and convincing evidence of deficiencies on the part of MPM in the undertaking of its obligations and duties as Trustee and Retirement Scheme Administrator of the Scheme as amply highlighted above which, at the very least, impinge on the diligence it was required and reasonably expected to be exercised in such roles.

[101] The section titled '*Responsibilities of the Service Provider*'
[102] *A fol.* 6

It is also evidently clear that such deficiencies prevented the losses from being minimised and in a way contributed in part to the losses experienced. The actions and inactions that occurred, as explained in this decision, enabled such losses to result within the Scheme, leading to the Scheme's failure to achieve its key objective.

Had MPM undertaken its role adequately and as duly expected from it, in terms of the obligations resulting from the law, regulations and rules stipulated thereunder and the conditions to which it was subject to in terms of its own Retirement Scheme documentation as explained above, such losses would have been avoided or mitigated accordingly.

The actual cause of the losses is indeed linked to and cannot be separated from the actions and/or inactions of key parties involved with the Scheme, with MPM being one of such parties.

In the particular circumstances of this reviewed case, the losses experienced on the Retirement Scheme are ultimately tied, connected and attributed to events that have been allowed to occur within the Retirement Scheme which MPM was duty bound and reasonably in a position to prevent, stop and adequately raise as appropriate with the Complainant.

Final Remarks

As indicated earlier, the role of a retirement scheme administrator and trustee does not end, or is just strictly and solely limited, to the compliance of the specified rules. The wider aspects of its key role and responsibilities as a trustee and scheme administrator must also be kept into context.

Whilst the Retirement Scheme Administrator was not responsible to provide investment advice to the Complainant, the Retirement Scheme Administrator had clear duties to check and ensure that the portfolio composition recommended by the investment adviser provided a suitable level of diversification and was *inter alia* in line with the applicable requirements in order to ensure that the portfolio composition was one enabling the aim of the Retirement Scheme to be achieved with the necessary prudence required in respect of a pension scheme. The oversight function is an essential aspect in the context of personal retirement schemes as part of the safeguards supporting the objective of retirement schemes.

It is considered that, had there been a careful consideration of the contested structured products and extent of exposure to such products and their issuers, the Service Provider would and should have intervened, queried, challenged and raised concerns on the portfolio composition recommended and not allow the overall risky position to be taken in structured products as this ran counter to the objectives of the retirement scheme and was not in the Complainant's best interests amongst others.

The Complainant ultimately relied on MPM, as the Trustee and Retirement Scheme Administrator of the Scheme, as well as other parties within the Scheme's structure, to achieve the scope for which the pension arrangement was undertaken, that is, to provide for retirement benefits and also reasonably expect a return to safeguard his pension.

Whilst losses may indeed occur on investments within a portfolio, a properly diversified and balanced and prudent approach, as expected in a pension portfolio, should have mitigated any individual losses and, at the least, maintain rather than substantially reduce the original capital invested.

For the reasons amply explained, it is accordingly considered that there was, at the very least, a clear lack of diligence by the Service Provider in the general administration of the Scheme in respect of the Complainant and in carrying out its duties as Trustee, particularly, when it came to the dealings and aspects involving the appointed investment adviser; the oversight functions with respect to the Scheme and portfolio structure; as well as the reporting to the Complainant on his underlying portfolio.

It is also considered that there are various instances which indicate non-compliance by the Service Provider with applicable requirements and obligations as amply explained above in this decision. The Service Provider

failed to act with the prudence, diligence and attention of a *bonus paterfamilias*.[103]

The Arbiter also considers that the Service Provider did not meet the '*reasonable and legitimate expectations*'[104] of the Complainant who had placed his trust in the Service Provider and others, believing in their professionalism and their duty of care and diligence.

Conclusion

For the above-stated reasons, the Arbiter considers the complaint to be fair, equitable and reasonable in the particular circumstances and substantive merits of the case[105] and is accepting it in so far as it is compatible with this decision.

Cognisance needs to be taken however of the responsibilities of other parties involved with the Scheme and its underlying investments, particularly, the role and responsibilities of the investment adviser to the Member of the Scheme.

Hence, having carefully considered the case in question, the Arbiter considers that the Service Provider is to be only partially held responsible for the losses incurred.

Compensation

Being mindful of the key role of Momentum Pensions Malta Limited as Trustee and Retirement Scheme Administrator of the Momentum Malta Retirement Trust and in view of the deficiencies identified in the obligations emanating from such roles as amply explained above, which deficiencies are considered to have prevented the losses from being minimised and in a way contributed in part to the losses experienced on the Retirement Scheme, the Arbiter concludes that the Complainant should be compensated by Momentum Pensions Malta Limited for part of the net realised losses on his pension portfolio.

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[103] Cap. 331 of the Laws of Malta, Art. 21(1)
[104] Cap. 555, Article 19(3)(c)
[105] Cap. 555, Article 19(3)(b)

In the particular circumstances of this case, considering that the Service Provider had the last word on the investments and acted in its dual role of Trustee and Retirement Scheme Administrator, the Arbiter considers it fair, equitable and reasonable for Momentum Pensions Malta Limited, to be held responsible for seventy per cent of the net realised losses sustained by the Complainant on his investment portfolio as stipulated hereunder.

The Arbiter notes that the latest valuation and list of transactions provided by the Service Provider in respect of the Complainant is not current. Besides, no detailed breakdown was provided regarding the status and performance of the respective investments within the disputed portfolio of the Complainant.

The Arbiter shall accordingly formulate how compensation is to be calculated by the Service Provider for the Complainant for the purpose of this decision.

Given that the Complaint made by the Complainant principally relates to the losses suffered on the Scheme at the time of Continental Wealth Management acting as adviser, compensation shall be provided solely on the investment portfolio existing and constituted under Continental Wealth Management in relation to the Scheme.

The Service Provider is accordingly being directed to pay the Complainant compensation equivalent to 70% of the sum of the Net Realised Loss incurred within the whole portfolio of underlying investments existing and constituted under Continental Wealth Management and allowed within the Retirement Scheme by the Service Provider.

The Net Realised Loss calculated on such portfolio shall be determined as at the date of this decision and calculated as follows:

(i) For every such investment within the said portfolio which, at the date of this decision, no longer forms part of the Member's current investment portfolio (given that such investment has matured, been terminated or redeemed and duly settled), it shall be calculated any realised loss or profit resulting from the difference in the purchase value and the

sale/maturity value (amount realised) inclusive of any realised currency gains or losses.

Any realised loss so calculated on such investment shall be reduced by the amount of any total interest or other total income received from the respective investment throughout the holding period to determine the actual amount of realised loss, if any;

With respect to the RBC Diversified Blue Chip Income Notes-Series 1 only, which was made prior to membership and which was accepted and retained by MPM within the Scheme's portfolio following membership, reference should not be made to the purchase value but the value applicable for this investment as at 12 September 2014, this being the date of assignment of the SEB Policy to MPM. Accordingly, for this investment it shall be calculated any realised loss or profit resulting from the difference in the value of the RBC Diversified Blue Chip Income Notes-Series 1 as at 12 September 2014 and its sale value (amount realised).

Similarly, any realised loss on such investment calculated over the aforesaid period shall be reduced by the amount of any total interest or other total income received from such investment throughout the holding period.

The holding period shall comprise the date from when such investment constituted part of the Retirement Scheme's portfolio until the sale of this investment.

(ii) In case where an investment in (i) above is calculated to have rendered a profit after taking into consideration the amount realised (inclusive of any total interest or other total income received from the respective investment and any realised currency gains or losses) such realised profit shall be accumulated from all such investments and netted off against the total of all the realised losses from the respective investments calculated as per (i) above to reach the figure of the Net Realised Loss within the indicated portfolio.

The computation of the Net Realised Loss shall accordingly take into consideration any realised gains or realised losses arising within the portfolio, as at the date of this decision.

In case where any currency conversion/s is/are required for the purpose of (a) finally netting any realised profits/losses within the portfolio which remain denominated in different currencies and/or (b) crystallising any remaining currency positions initiated at the time of Continental Wealth Management, such conversion shall, if and where applicable, be made at the spot exchange rate sourced from the European Central Bank and prevailing on the date of this decision. Such a direction on the currency conversion is only being given in the very particular circumstances of such cases for the purposes of providing clarity and enabling the calculation of the compensation formulated in this decision and avoid future unnecessary controversy.

(iii) Investments which were constituted under Continental Wealth Management in relation to the Scheme and are still held within the current portfolio of underlying investments as at, or after, the date of this decision are not the subject of the compensation stipulated above. This is without prejudice to any legal remedies the Complainant might have in future with respect to such investments.

In accordance with Article 26 (3)(c)(iv) of Chapter 555 of the Laws of Malta, the Arbiter orders Momentum Pensions Malta Limited to pay the indicated amount of compensation to the Complainant.

A full and transparent breakdown of the calculations made by the Service Provider in respect of the compensation as decided in this decision, should be provided to the Complainant.

With legal interest from the date of this decision till the date of payment.

Because of the novelty of this case each party is to bear its own legal costs of these proceedings.

Dr Reno Borg
Arbiter for Financial Services