

ADMINISTRATION COSTS AND COST ALLOCATION

What are the rules for costs and cost allocation?

Under the Special Administration rules, the costs of returning client assets and client money are to be paid for out of those client assets and that client money, or the client may have the option to pay for the costs themselves. The great majority of clients will be entitled to have these costs met by the FSCS (see below) and will not need to meet the costs of returning their assets and client money.

What do the costs include?

Costs comprise of:

- The remuneration and expenses of the administrators and their team;
- The remuneration of the administrators' legal advisers and other consultants;
- The costs of the Beaufort operations including people, premises, IT and other associated overheads;
- Interest and charges associated with the loan facility which the administrators negotiated pending any costs being recovered;
- A prudent reserve for potential additional costs; and
- VAT on the above where applicable.

The Administrators' fees are subject to review and approval by the Creditors' Committee (and a Costs Assessor, who has been appointed to advise the Committee) and, as necessary, by the Court.

The administrators have not yet drawn any fees and will not do so until after the first client assets transfer. They will in any event not draw any fees before such fees have been properly checked and approved by either the Creditors' Committee or the Court.

The initial costs reserve

When making distributions of client assets and money, it will be necessary for the administrators to maintain a reserve to pay for future costs until all the client assets and money have been returned. To do this the administrators need to make a prudent estimate of what the total costs might ultimately be, including both costs incurred to date and also a prudent estimate of costs that may be incurred up to the end of the client assets and client money return process. The administrators will review the amount needed to be kept for future costs and may reduce their estimate of future costs. When this happens some of the costs set aside for future costs will be released and returned to clients.

The administrators' current expectation is that the initial cost reserve will be set at £55m. At this stage it is not clear how many clients may be transferred to the nominated broker in September 2018 (although we expect the great majority to be transferred in this way), so we have cautiously estimated a two year process before all or nearly all client assets have been transferred or distributed.

We are hopeful that the majority of clients will in fact be able to transfer to the nominated broker in September 2018 or soon after. If that takes place, it should enable the administrators to update their prudent estimate of future costs and make a rebate to clients before the end of the calendar year.

How will the initial cost reserve be allocated among clients?

The Creditors' Committee and the FSCS have agreed a costs allocation formula to allocate costs across all clients. The intention is that the initial costs reserve will be allocated as follows:

- for client assets, a flat allocation per client account will be used, capped at the value of the assets held by that client but not more than £10,000 per client; and
- for client money, not more than 10% of the money held.

The above proceeds on the basis that around £50m of the costs reserve is allocated to client securities and the remaining £5m is allocated to client money. As noted above, these are just reserves and not the actual costs that will ultimately be paid by clients.

What if costs are lower than expected - will I get a cost rebate?

Estimated costs may reduce over time as the client asset return process develops. If the estimated costs reduce, the FSCS and clients who have paid costs themselves will receive a costs rebate. In the same way that the client asset costs may reduce and result in a cost rebate, so may the 10% figure for client money. Once all costs are known, a final rebate can then be paid.

What is the FSCS and what does it mean for me?

The FSCS is responsible for paying out to customers of financial services firms who have suffered losses after a firm has failed. It is an independent body and will cover your losses up to £50,000 if you meet its eligibility tests. Most of BACSL's clients meet these tests and will have their costs covered by the FSCS.

Although there are some 17,500 clients with client assets, many of these clients have client assets with values of less than £10,000. Since the costs to be charged for returning client assets are to be capped at £10,000 per client, the FSCS is expected to cover all of these costs for FSCS protected clients.

Because of the large number of clients who are eligible for FSCS compensation and in light of how the costs are allocated, we estimate that over 94% of the total costs will be met by the FSCS. Very few (less than 10) individual clients are expected to face a loss, since individuals are automatically eligible for FSCS compensation. There are less than 500 corporate clients, many of which are likely to be small businesses and therefore also FSCS eligible (see the FSCS eligibility rules at <https://www.fscs.org.uk/what-we-cover/eligibility-rules/>). For many larger

corporates, however, the costs will need to be paid for by the client or deducted from its client money or client assets.

Some clients may also be affected by shortfalls in client assets and/or client money because BACSL did not hold all the client assets and client money which it should have held for these clients. These shortfalls are not expected to be material and are likely to be covered by the FSCS for eligible clients.

Some examples of costs allocations (for FSCS eligible clients) are set out below

<u>CLAIMANT</u>	CLIENT MONEY			CLIENT ASSETS		TOTAL	
	VALUE HELD	COST ALLOCATION	COST ALLOCATION MET BY FSCS	VALUE HELD	COST ALLOCATION MET BY FSCS	TOTAL ASSET VALUE RETURNED	TOTAL FSCS COMPEN-SATION*
	£	<i>Note 1</i> £	£	£	<i>Note 2</i> £	£	£
A	20,000	2,000	2,000	100,000	10,000	120,000	12,000
B	300,000	30,000	30,000	100,000	10,000	400,000	40,000
C	-	-	-	100,000	10,000	100,000	10,000
D	20,000	2,000	2,000	5,000	5,000	25,000	7,000
E	300,000	30,000	30,000	5,000	5,000	305,000	35,000
F	-	-	-	5,000	5,000	5,000	5,000
G	600,000	60,000	40,000	1,000,000	10,000	1,580,000	50,000

TABLE NOTES

1. Cash assets cost allocation calculated as a 10% levy on the value of the cash held for you by Beaufort. This may be the subject of a rebate when the costs estimate is revised or the final Administration costs are known.
2. Client assets cost allocation calculated at a flat £10,000 per account, unless the value of the assets held in the account is less than £10,000, in which case the allocation is “capped” at the value of the assets in the account. This £10,000 may also be the subject of a rebate when the final administration costs are known.
3. The only Claimant in these examples who fails to have all his/her/its assets returned (typically by a transfer to a new, solvent broker) is Claimant G, whose cash balance percentage of 10% means that the total costs of £60,000 (cash) and £10,000 (investment assets) exceeds the FSCS maximum coverage of £50,000 by £20,000. This Claimant accordingly recovers £20,000 less than the total value of the assets (£600,000 + £1,000,000 - £20,000 = £1,580,000). No investments need to be sold as the £20,000 can be deducted from the cash held.

If all these clients were eligible for FSCS compensation, the only one with an additional costs contribution would be client G, who would have to pay an extra

£20,000 (calculated by deducting the FSCS maximum compensation of £50,000 from the total costs allocation of £70,000). If there were a rebate, the first £20,000 of the rebate for client G would be paid for the benefit of client G himself, rather than the FSCS.

What effect will this have on tax wrappers?

Where the FSCS meets costs, the aim is for that to be paid directly to the administrators. This should enable clients who are fully covered by the FSCS to have their client assets and client money transferred to an account held by the nominated broker in full with no impact on tax wrappers such as SIPP and ISAs.

Note: the above is on the basis that the Distribution Plan which incorporates these matters is duly approved by the Court in July 2018 and the first assets transfer occurs in September 2018.

Russell Downs, Douglas Nigel Rackham, and Dan Yoram Schwarzmenn have been appointed as joint administrators by the High Court to manage the affairs, business and property of Beaufort Asset Clearing Services Limited. The Administrators act as agents of the company, without personal liability. All are licensed in the United Kingdom to act as Insolvency Practitioners by the Institute of Chartered Accountants in England and Wales. The Administrators are bound by the Insolvency Code of Ethics which can be found at: <https://www.gov.uk/government/publications/insolvency-practitioner-code-of-ethics>.

The Administrators may act as Data Controllers of personal data as defined by UK data protection law depending upon the specific processing activities undertaken. PricewaterhouseCoopers LLP may act as a processor on the instructions of the Administrators. Personal data will be kept secure and processed only for matters relating to the Administrators' appointment. Further details are available in the privacy statement on the PwC.co.uk website or by contacting the Administrators.