Consumer Duty

Product & Services Review

Blackfinch Ventures EIS Portfolios

Product Details

Description of the product

Blackfinch Ventures EIS Portfolios is a discretionary portfolio management service that aims to provide long-term returns from investments held for a target period of 4–7 years whilst enabling investors to benefit from available EIS tax reliefs.

The Enterprise Investment scheme (EIS) has become a valuable tax planning tool since its launch by the UK Government to encourage investment in start-ups and early-stage companies.

Blackfinch Ventures EIS Portfolios investments are deployed into a diversified portfolio of at least 10 early-stage, high-growth technology companies throughout the UK.

Describe the key features and benefits of the product

The main benefits of EIS investments:

- Income tax relief of up to 30% (on a maximum investment of £1m per tax year), which can potentially be carried back to the tax year before the investment.
- Business Relief: up to 100% Inheritance Tax (IHT) exemption on qualifying investments held for at least two years (and at time of death).
- Capital Gains Tax (CGT) deferral relief (up to three years prior to investment and up to one year in advance).
- Exemption of CGT on investment growth (subject to income tax relief being claimed and retained at time of disposal).
- Offsetting of capital losses on the marginal rate of income tax at time of loss.

The features of the product:

- Investment into high-growth technology businesses, each with a strong founding team, good ESG values, and a product for which they have established there is a large market.
- Investment into at least 10 companies, diversified over stage and technology sector.
- A target (not guarantee) to deploy investments fully within 12 months. *Alternatively*: funds can be deployed fully within a given tax year but in that case the above diversification cannot be guaranteed.
- Potential for high returns (along with high risk) with a targeted base return of 3x over 4-7 years.

Describe the limitations of the product

- Investors are unable to control when they will receive returns from the product, which is targeted between 4-7 years for each investee company, but could be longer.
- To qualify for income tax relief and tax-free growth, investors must hold investments in underlying companies for a minimum of three years.
- Income tax Relief is available on a maximum investment in EIS schemes of £1m per tax year (plus up to £1m more in Knowledge-Intensive companies – not offered by this product)
- Investors must have a sufficient income tax liability to claim the relief
- The product is high risk and it is possible that the full investment would be lost.

Events

Has there been an event which could result in the product posing a risk to customers?

Event = any concerns identified during review about the product or its literature that may be perceived as a consumer harm.

No risks to customers were identified during this review.

If yes: explain the risks now posed to customers

1. Although apparent from the brochure, there remains a risk that clients may not understand that they cannot control how long they hold investments, and that returns will come at different times from holdings in different portfolio companies.

2. Clients may not understand that valuations are partly subjective, only updated quarterly, can be volatile, and are unlikely to show significant gains in the early years of an investment.

3. Clients may not understand that the product is not suitable for those with insufficient income tax liability to benefit from the full tax relief it offers.

4. Clients may not understand that 4 years' AMC is taken up-front and is retained even if the company fails or exits within 4 years.

Detail mitigating action taken [or to be taken]

1. Add a timeline to the brochure that shows returns from different companies at different times depending on when each exits.

2. Explain the nature of valuations in a separate 'welcome pack' document, provided to clients once they have invested.

3. State this point explicitly in the brochure.

4. Clarify this point in the brochure.

Following mitigating action, is the product still suitable?

☑ Yes ☐ No

Needs and Objectives

Describe the needs and objectives [including financial objectives] of the target market for the product [include vulnerable customers].

Investors in the target market will:

Be looking to reduce their UK tax burden within long-term schemes (more than 5 years) – at least to reduce income tax and potentially also inheritance tax and/or capital gains tax.

Have already accumulated a large element of savings and want the potential to generate a high return on part, whilst being prepared and able to bear the entire loss of that part.

Be willing to invest in small unquoted businesses and able to accept the associated long-term illiquidity.

Need financial advice, unless they are Sophisticated Investors who want and are able to assess the risks and potential benefits themselves.

Vulnerable customers will be initially assessed and screened by their financial adviser, any specific needs will be raised and we will cater for these to the best of our ability. For example, we currently provide forms with bigger text for those with poor eyesight. The needs and objectives of vulnerable customers should not inhibit them using our product, due to staff training and policies we have in place.

Product Risks

Identify the risks posed by the complexity or nature of the product

Customers may not understand that:

1. They will not be able to control how long they hold the investment; any proceeds will be delivered as and when each underlying investee company achieves an exit, which is initially targeted between 4-7 years but could be longer.
2. The underlying investments are very high risk and it is likely that some will fail completely, with the overall return generated by those (if any) that succeed. Some failures are likely before successful exits.
3. Investment valuations are partly subjective, only updated quarterly, can be volatile, and are unlikely to show significant gains in the early years of an investment.
4. This product is not suitable for those with insufficient income tax liability to benefit from the full tax relief offered by the product.
5. In order to obtain and retain these tax reliefs investments must be held for a minimum of three years - noting that clients do not control the holding period for each underlying investment.
6. They cannot decide or change the investee companies in which their funds are deployed, even if they dislike a business or disagree with our assessment that it meets our criteria, e.g. regarding ESG.

Explain how these risks are mitigated

The risks are mitigated by clear client communication. This needs to come largely through advisers (for Advised clients). Our published Target Market Assessment (TMA) helps direct them to customers for which the product is appropriate, and to avoid sales where it would be inappropriate, but it is also reliant on their own expertise. In addition, our client documentation, especially the brochure help mitigate the potential misunderstandings, and is of particular importance for Direct clients.

1. Is apparent in the brochure and stated explicitly elsewhere, notably in our EIS vs VCT comparison (see 'Liquidity'). However, it could help to illustrate a timeline scenario explicitly in the brochure. And to be clearer that the 4-7 year target exit period is from investment into an individual company, rather than from the client investment into the product.
2. Stated and illustrated explicitly in the brochure – with even our higher return scenario showing 3 of 10 companies failing outright.
3. Information about the method and nature of valuations is provided where relevant with quarterly updates; reporting is stated as being quarterly in the brochure However, the nature of valuations could be stated explicitly in the brochure and/or a welcome pack.
4. Is covered explicitly in the TMA for Advisers but not in the brochure.
5. Is stated clearly in the brochure.
6. It is clearly stated in the KID and brochure that it is a portfolio management service, with a description of how we select companies.

Identify the risks posed to the target market by the Product

1. The capital invested is at risk, the value of the investment may go down as well as up, and investors may not get back the full amount invested.
2. There is no guarantee that the targeted return will be achieved.
3. Changes to the taxation environment or HMRC practice may affect investment returns (tax rates, benefits and allowances are personal to investors and they depend on personal circumstances.)
4. Investee companies may alter and so no longer qualify within the EIS legislation, which could result in the repayment of any tax rebate.
5. The investment will be spread over at least 10 companies. However, the failure of any individual company, which is likely, will have a significant impact on the overall value of the portfolio, and investors should be aware of the concentrated nature of the portfolio.

Explain how these risks are mitigated

Each investment is very high risk and Risks 1 and 2 are mitigated by investing in at least 10 companies as described in Risk 5. It maximises the chance of exposure to successful companies that can deliver a substantial return, while limiting the impact of companies that fail. Care is taken within the portfolio to reduce the correlation of risks affecting companies by diversifying by stage and sector. In addition downside risk with an individual company investment is reduced by the use of "A-Ordinary shares" that carry a priority to return at least the amount invested where there are sufficient proceeds to do so. Finally, loss relief provides some mitigation in the (likely) cases of companies that fail.

However, Risks 1,2 and 5 remain and clients must be aware of these risks, and willing and able to accept them. They are made clear in the brochure, TMA, and other documentation.

Risk 3 depends on the personal circumstances of clients, as well as government policy, and it is important that customers take professional advice or are able to assess their likely future circumstances and the regulatory environment themselves.

For Risk 4, we require each company to have EIS Advance Assurance from HMRC and we also commission an independent PI-backed opinion from tax specialists to confirm that each company is EIS qualifying. We further build obligations into the legal investment documents that requires companies and their foudners to maintain EIS qualification. Nonetheless, EIS compliance is at the discretion of HMRC and the risk remains; it is clearly stated in the brochure and elsewhere.

Identify the risks posed to vulnerable customers by the Product

Some vulnerabilities may make someone unsuitable for the product. For example, the long-term illiquidity of the product would make it unsuitable for those with low financial resilience, such as those likely to have insufficient or erratic income and who may need to withdraw funds on demand.

However, it may be suitable for those with many vulnerabilities, but there would be potential risks:

1. Lack of understanding of the product, whether arising from a long-term condition, low capability, or short-term stress. The risks above relating to the nature and complexity of the product would be particularly relevant.
2. Emotional stress or circumstances making it difficulty (whether realised or not) to make decisions, particularly a long-term decision, given that investing in this product would irreversibly tie up their funds for several years.
3. Life changing events, whether relating to work or a personal life, making it hard to predict circumstances some way ahead, again relevant for what is a long-term product. But noting that such changes in life may equally be a reason for the product to be appropriate, or to prompt a desire to make long-term financial plans.

Explain how these risks are mitigated

In most cases, the risks to vulnerable clients are mitigated with independent, advice from qualified financial advisers who assess the individual client's needs, desires and capabilities.

For advised clients we further mitigate the risk with clear, simple statements about the main attributes and risks of the product, particularly noting the points in the section above on the nature and complexity of the product.

We have a Vulnerable Customers policy in place and all staff are trained on how to identify and deal with vulnerable customers.

Testing

Is the product meeting the needs and objectives of its target market and vulnerable customers?	Testing is based on comments and questions from advisers and clients, and on the performance to date of the portfolios in delivering the stated objectives – noting that even the earliest portfolios are yet to reach the lower bound of the target exit period for their companies. A recent exercise looked at the return potential for typical client portfolios made at different times according to a range of scenarios based on the progress made by investee companies. While all are still at an early stage, there remained good potential to deliver the intended targets, albeit with the product's expected high level of risk. On both measures, the product is meeting its objectives so far.
Has a value assessment been completed, and does it demonstrate good value? (separate review document)	See separate document.
Has the product been distributed in accordance with the value assessment findings?	Yes, with the bulk of investments made on the recommendation of financial advisers.
Are communications being used as detailed within the product approval?	Yes, the product is being distributed according to the value assessment and third party reviews.
Does data demonstrate the communications are effective in allowing the target market to understand the key features and benefits of the product and make effective decisions?	The number and nature of queries received indicates that in general the target market does understand the product, with the exception of specific minor details, and specific clients. Blackfinch Investments Limited as the manufacturer of these types of solutions will distribute predominantly to registered Financial Advisers and professional intermediaries such as Solicitors and Accountants. This is done on the understanding that any advice given to the client has passed a rigorous due diligence process and an assessment has been made on the suitability, considering the clients attitude to risk and volatility.

Does testing demonstrate the communications are clear, fair and not misleading?	Yes, as above noting the opportunity for greater clarity in certain specific details.
Are customers adequately supported after the point of sale?	Yes, information is provided on a regular basis and ad hoc when appropriate, with documents available on a customer portal for those who wish to have this facility, and with responsive customer support for direct clients and advisers who route queries from clients. (Noting that we do not have good visibility of the support provided by advisers to clients.)
Have testing of the actions of distributors been undertaken?	As above, there is little visibility of the actions and support provided by advisers other than through their questions, discussions with them, and very occasional direct contact from advised clients.
Where testing identifies the product is not meeting the needs of some or all of its target market [including through identified issues with communications] has the following action been taken: • *Cease distribution* • *Mitigate failures* • *Inform distribution chain*	Testing indicates the product meets the needs of the target market.

Consumer Support

Has the product been designed to support retail customers such that it meets the needs of retail customers, including those with characteristics of vulnerability?	Yes
Is there evidence demonstrating that retail customers can use the product as reasonably anticipated?	Based on the questions and comments received from clients and advisers (including positive ones about the quality of communication), and the low number of complaints (2 per year) there is reasonable evidence that retail customers are able to use the product as expected.
Is there evidence demonstrating appropriate friction in the customer journeys to mitigate the risk of harm and give retail customers sufficient opportunity to understand and assess their options, including any risks	Retail customers are only permitted to invest if advised or qualify as sophisticated investors, which significantly reduce the risks. With funds deployed as standard over 12 months, and with a default cooling off period before deployment commences, there is usually good opportunity to reverse a decision if it is reconsidered. The number of requests to withdraw funds or applications is low, suggesting overall that there is anyway appropriate friction. A significant number of cases require deployment of funds by the end of the tax year, some of which may come at short notice and waiving the cooling off period. However, this is always driven by client circumstances and at their request; more than 90% are anyway still advised.

Is there evidence demonstrating retail customers do not face unreasonable barriers (including unreasonable additional costs) during the lifecycle of the product, such as when they want to:

(a) make general enquiries or requests.
(b) amend or switch the product.
(c) transfer to a new product provider.
(d) access a benefit which the product is intended to provide.
(e) submit a claim.
(f) make a complaint; or
(g) cancel a contract, agreement or arrangement or otherwise terminate their relationship

The product is illiquid. Funds that have been deployed cannot practically be withdrawn or moved – or at least would incur very high additional costs. This is a necessary characteristic of the product that is made very clear up front. As such, (b), (c) and (g) are not feasible. (e) is not applicable.

However, there are examples to demonstrate there are no additional costs for (a), (d), or (f).

Findings

Is the product demonstrating a clear set of benefits for its target market [including vulnerable customers]	Yes, there is clear benefit for the target market, which may well include vulnerable customers.
Does the product provide fair value for the target market [including vulnerable customers]	Yes. The costs are fair compared both to the value provided (noting the high risks that may result in a poor return) and to providers of comparable products.
Have identified risks of the product been reasonably mitigated and distribution strategies designed to significantly reduce such risks?	Yes, notably a clear primary focus on serving clients through independent qualified advisers.
Is the product allowing identified groups of customers to pursue their financial objectives?	Yes.
Have customers been able to use the full benefits of the product?	Yes – as far as can be established at this stage, given that it is a relatively new, long-term product.
Is the product design avoiding foreseeable harm as set out in PRIN 2A.2.10 G?	Yes.

Consumer Duty

Price & Value Assessment

Blackfinch Ventures EIS Portfolios

Target Market

Identify the target market

Retail and professional clients who:

- Are looking to reduce their UK tax burden within long-term schemes (more than 5 years) – at least to reduce income tax and potentially also inheritance tax and/or capital gains tax.
- Have already accumulated a large element of savings and want the potential to generate a high return on part, whilst being prepared and able to bear the entire loss of that part.
- Are willing to invest in small unquoted businesses and able to accept the associated long-term illiquidity
- Have taken and are acting on the recommendation of a qualified financial adviser, or who qualify as Sophisticated Investors.

Detail the characteristics of the target market

Clients' knowledge and experience

Clients will need an understanding of the risks and benefits of the product. In particular, that the investments are high risk and that certain criteria need to be met to meet the tax benefit criteria, including that the underlying investments need to be held for at least 3 years. Ideally the investors should have prior experience of investing and will have taken advice or declared that this is an investment they can afford to lose, and that they have no immediate need to access their investment. They should be aware that the investments are in start-up companies, with high growth prospects but also high risks of not performing.

Clients' financial situation and ability to bear losses

The client will need to ensure that they can bear the full loss if the product were not to perform. They should have a favourable financial position and excess disposable income. Investors should be in a position to lock their money away for several years and should be comfortable with the fact that the investment term is completely outside their control.

Risk tolerance and compatibility of the risk/reward profile of the product with the target markets

Clients must be willing to invest their capital for what is targeted to be 4-7 years but could be longer. They must also understand the high risks involved and that they may not receive back their original investment.

Clients' objectives and needs are covered in the description of the target market above.

Explain why the target market has been selected	This target market has been chosen because these customers will be able to derive most value from the product, including its tax reliefs and long-term potential return, whilst being willing and able to accept its limitations and high risks, including its long-term illiquidity and potential for losing the entire investment.
Identify any characteristics of vulnerability in the target market which may impact the value received by those customers	Vulnerabilities may impair a client's ability to plan or make a decision about the longer-term, or to understand the risks and limitations of the product. However, such vulnerabilities would place them outside the target market. The risk is that potential clients incorrectly believe they are in the target market. But where it is established that they are in the target market, notably where their purchase of the product is on the recommendation of a qualified financial adviser, then they would receive the expected value from the product.
Identify the drivers of vulnerability in the target market	The main drivers of vulnerability that could relate to the target market including: • Health, possibly affecting understanding of the risks and limitations of the product, which may be mitigated by appropriate advice and support, or a lack of clarity about long-term circumstances. • Life-changing events, with similar impacts above, noting that such changes may also be a trigger for potential benefit from the product. • Financial limitations, either in the short or longer term, which would typically place someone outside the target market • Poor communication or ability to understand, that again might be possible to be mitigated by additional support and advice.
Could the customers vulnerabilities impact full/ value use of the product	Vulnerabilities could impact the value received by customers, particularly considering its long-term illiquidity and high risks. However, such vulnerabilities would place the potential client outside the target market, as appropriate understanding, acceptance and capacity for these characteristics are essential elements of that market.
Do cognitive or behavioral biases of customers impact on the value of the product to the customer?	Such biases may affect the decision to select the product, but providing the elements of the target market are satisfied then the customer will still receive the appropriate value from the product.

Nature and costs of the Product

Does the design of the product [i.e.the key features] enable use by the target market ensuring they are able to pursue their financial objectives?	Yes, considering the characteristics of the target market, the product will help the target market to achieve its financial objectives.
Do any aspects/limitations of theproduct prevent the average target customer from fully enjoying the product?	No. Understanding the limitations is an important element of the target.
Does the product allow for comparison to other products in the market?	Yes. EIS products can be compared through their published fees and with reference to independent reviewers such as Micap, Churchill and Hardman.
Does the product allow for easy switching to another provider or product?	No. Funds are deployed into illiquid private companies from which it is not practically possible to withdraw funds until the company achieves an exit such as sale or IPO. This is a necessary characteristic of the product in order to secure the EIS tax reliefs.
Total maximum cost, including all fees / commission payments	Excluding adviser and performance fees, the max cost would be: 3% initial + 2% AMC for 4 years only + <~2% ancillary investment fees = ~13% of amount invested The performance fee as 20% of the amount returned above 130% is unbounded, based on the return.
Maximum possible cost of contingent charges [i.e. late payment fees]	None.

Non-financial costs [i.e. data use by the firm]	None.
Will the product have a finite lifespan? If yes, explain the relationship between the lifespan and the price to the customer. Explain why the overall price is good value.	No, the product is evergreen and does not have a finite lifespan.
Is it likely the customer will renew at the end of the contract period? If so, explain why the overall price is good value [must factor in any price increases at renewal].	The product is long-term, with proceeds being generated at different times and a contract continuing whilst any funds are deployed. When proceeds are returned, it is likely that some clients will reinvest those proceeds. However, others will choose not to, either because their circumstances have changed or in order to diversify risk by investing in an alternative product while they still have funds in this one. Reinvesting proceeds will deliver further tax reliefs, and therefore the value delivered – subject to the high risk of the product – will be expected to be the same.
Taking all of the above into account, explain why the product offers fair value to the target customer	The product offers fair value because in return for the costs, there is the potential for capital gains (tax free), up to 30% income tax relief, up to 100% Inheritance Tax exemption on qualifying investments after two years, and the offsetting of capital losses on underlying investee companies at the marginal tax rate. The tax reliefs more than outweigh the costs (exc. performance fee), and there remains the potential for high returns, albeit with high risk.
Taking all of the above into account, explain why the product offers fair value to vulnerable customers	Vulnerable customers are no less able to obtain value from the product providing they are able, with appropriate advice, to meet the conditions of the target market.

Costs

Total costs for manufacturing the product per unit sold	The total cost of the Blackfinch Ventures EIS and Spring VCT, including salaries, legal, operational and support functions is currently circa £3.1million. This is against annual fees of around £3.71million. Therefore, for each £1 sold in terms of overall income, the cost is 83.6 pence. Dividing the costs pro rata by income between the EIS and VCT would keep the figures in proportion. Therefore for the EIS, for each £1 sold in terms of overall income, the cost is 83.6p.
Identify the market rate for the product	The Micap review indicates that the average initial fee out of 49 EIS products is 3.8%, while the average ongoing fee is 1.9%. Over 4 years, we are slightly cheaper (more significantly thereafter as we charge no AMC after 4 years). The average performance fee is 19% but above an average hurdle of 101.3%
Is the final price paid by the customer significantly higher than either the total cost for manufacturing and distribution or above the market rate? *If so, is there an added benefit to the service which means the customer is receiving fair value?*	The final price paid by the customer is competitive in the market as shown above. It is also appropriate to the costs incurred in manufacturing the product, with costs running at 83.6p for each £1 of income. The performance fee is not linked to costs but ensures our alignment with clients in picking investments to deliver the best return for clients.

Pricing

Is differential pricing used by the firm and if so explain the objective and justifiable reasons for doing so?	None.
List each group where the pricing is different and explain why the value is fair, factoring in cost and market rate for that group of customers.	None.
Is there another product offered by the firm which offers similar benefits for a lower cost? *Explain the reasons for the difference [i.e. enhanced customer service]*	None.

Distribution Arrangements

Does the distributor have access to all appropriate information from the manufacturer to be able to understand the value that the product is intended to provide for the customer?	Yes, all relevant information is provided through Blackfinch and to advisers, notably including the product brochure and the target market assessment but also including other collateral. See the product review for a more detailed review of the content. BF100 clients additionally get a paper and short presentation on each company in which they are able to invest.
Does the distributor understand: • *Intended benefit of the product* • *Value to be provided to customer by the product* • *Characteristics, financial goals and needs of the target market* • *The level of pricing set* • *Quality of service required to represent good value* • *Potential impact of distribution arrangements*	Yes, distributors including advisers have access to information as described above to cover all these points, including BF100 clients.
Are there any renumeration arrangements with the distributor which may impact the value customers receive?	Advisers are able to charge their own initial and ongoing fees (for 4 years). These fees are at their discretion and reduce the funds invested, hence decreasing the value received. However, the average adviser fees are 0.67% initial and 0.19% ongoing – representing additional costs of just 1.43%. This is reasonable and proportionate given the importance of the advice in assessing clients' individual circumstances as regards the target market.
Are proposed distribution arrangements consistent with the value of the product?	Yes. It is important that, other than with a minority of direct clients who are sophisticated investors, clients receive advice appropriate to their individual circumstances to ensure the product's suitability.
Explain how the distribution arrangements support the value of the product	As above.

Findings

Does the product in its current form offer fair value?	Yes.
Explain why the product provides value for the target market	The product offers the generous EIS tax reliefs to those who can benefit from them, whilst offering the potential for high returns for those who can afford to risk the loss of the capital invested with no liquidity over several years – all criteria in the target market. The costs are reasonable compared to the tax reliefs available and the potential return – with the biggest cost potentially being the performance fee which is directly linked to the value provided to the customer.
Explain why the product provides value for the vulnerable customers in the target market	Vulnerable customers who satisfy the conditions of the target market are no less able to benefit from the product, and will receive the same long-term value.
If the product is sold as part of a package, does the overall package offer fair value?	N/A
Are there any adverse findings in this assessment?	No.
Set out mitigating actions to occur prior to distribution or remedial action to prevent foreseeable harms to current customers	N/A

IMPORTANT INFORMATION