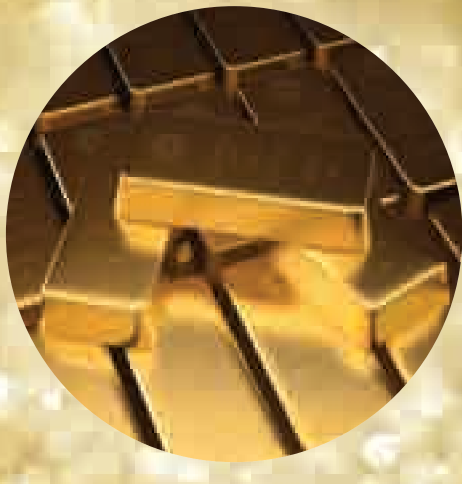

Jonathan Silverman reviews key steps to protect clients interested in being involved in alternative investment schemes

Alternative investment: all that glitters isn't gold

The general uncertainty about the stability of the banking sector combined with historically low interest rates has led to a rise in the number of alternative investment schemes for clients with cash to place. These range from precious stones, fine wines and classic cars.

Solicitors need to keep a wary eye when asked to advise clients seeking to become involved in this sector, either those putting a scheme together or those proposing to put money with them if all is not to end in tears. This is especially true when one realises that this is an area of investment that is not necessarily subject to any regulation whatsoever.

Alternative investment schemes that do not involve the sale of securities or equities to the investors are simply unregulated. They can be promoted as widely and aggressively as the commission-driven salesman determine, which brings with it all the inevitable risks of mis-selling.

First, you should carefully review the actual scheme on offer. The business models all differ so require thorough analysis – the more complex the structure then perhaps the more reason to exercise increased diligence, especially where more than one jurisdiction is involved.

Ask yourself: is the intention for the investors' funds to be pooled, that is to say applied towards the purchase of a class of assets to be held by or on behalf of a syndicate? Or are the promoters going to be advising investors to purchase specific assets whether a gem, bar of gold or a case of Bordeaux wine to be held in their name?

Different schemes give rise to different challenges for the practitioner asked to advise on these schemes. Simply reviewing a glossy brochure does not even start to address the issues. I have drawn up a series of steps that I find useful to follow as a minimum:

- Check whether the scheme falls within FSA regulation: this is essential. Could it possibly be construed or interpreted as an investment scheme?
- Carry out a careful review of the representations made about the scheme, whether in the form of the brochure or, as is often the case, online.
- If a rate of return is shown, is it indicative or guaranteed and if so by whom and for how long?
- Look carefully at the exit routes offered; while the return on capital placed within the scheme may appear attractive, if the underlying capital is locked in, or, more seriously, is at risk, then something is very wrong. If I'm unsure, I remind myself that the early investors in Charles Ponzi's and Bernard Madoff's arrangements eulogised over their investments – until they lost everything.
- Verify how the underlying assets are being held, what security exists for the parties and issues such as in whose name are the assets be registered.
- When it is proposed that individual assets are to be held for them check how they are allocated to individual investors, especially if there are assets that might vary in quality such as precious stones.
- Is there any way of checking on the assets in the scheme? Is it to be audited regularly and if so by whom?
- When establishing that trustees are being appointed to hold the assets, clearly there is a need to check that they are genuinely independent of the promoters of the scheme.

It is also worth ascertaining where the assets are being held – namely within the UK or overseas. In a number of cases the promoters, in order to mitigate any VAT exposure, seek to hold assets overseas, but if something does go wrong clearly trying to chase assets in overseas jurisdictions becomes more complex and costly.

Other aspects worth investigating are the reputation of the other professional advisers, whether the fund managers have a genuine proven track record, whether they are part of an established investment house or have sprung up without any genuine provenance.

And if in doubt, bear in mind the old adage that if something looks too good to be true it probably is!

Jonathan TR Silverman is a partner at Silverman Sherliker LLP (www.silvermansherliker.co.uk)