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In response to the EU Commission's call for evidence on the review of the application of the Investor Compensation Directive ("ICDS") in line with parallel initiatives concerning the Deposit Guarantee Schemes Directive and insurance guarantee schemes, I outline below the position put forward for consideration by the Investor Compensation Company Limited ("ICCL").

Background to the ICCL

Following the introduction by the European Union of the Investor Compensation Directive (the "Directive") in 1997, the Irish Government executed the Investor Compensation Act (the "Act") on 1 August 1998. The Act provides for the establishment of the Investor Compensation Company Limited and sets out as a principal objective of the ICCL the putting in place of arrangements (e.g. funding and payment procedures) to ensure that eligible clients of a failed firm receive compensation, within the parameters set down in the Act, as expeditiously as possible. Our 2008 Annual Report is available on our website¹ and provides further background on our Scheme.

Questions raised in the call for evidence and ICCL's responses

1) *Should the operation of multilateral trading facilities be excluded from the scope of the ICSD?*

An MTF is essentially a trading platform bringing together multiple third-party interests in accordance with certain rules: due to this specific nature, this service

¹ <http://www.investorcompensation.ie/publications.php>

receives a peculiar treatment under MiFID and is assimilated to a regulated market. In fact, many relevant rules of MiFID do not apply to the transactions concluded under the rules governing an MTF; in addition, already in the case of MTFs operated by market operators, the membership of an investor compensation scheme is not required.

ICCL Response: The ICCL notes that MTFs are platforms which facilitate trading between market participants (which in certain member states are restricted to professional investors) rather than investment products. The ICCL does not believe that these products could give rise to compensatable losses for eligible (essentially retail) investors and therefore does not believe that they should come within the scope of the ICSD.

- 2) Would it be appropriate to include in the scope of the ICSD all investment firms seeking authorisation to the provision of investment services, although their authorisation would not allow holding clients' assets?

ICCL Response: The authorisation process for investment firms is a matter for Financial Regulators. However, our experience has shown us that default can occur due to investment firms acting outside of their authorisation, for example, in cases of fraud. In our view, the key issue to be decided is whether clients of particular firms should be protected in all circumstances where their investment monies or instruments cannot be returned to them in a timely manner.

- 3) Would it be appropriate to include in the scope of the ICSD all investment firms seeking authorisation to the provision of investment services, although they provide their services only to non-retail clients?

ICCL Response: (Please refer to our response to question 2 above)

- 4) a) Should investors be able to claim compensation in the case of default of the third party where their assets had been deposited?

ICCL Response: This issue has not arisen in cases handled by the ICCL. Nonetheless, we believe that this gap in consumer protection needs to be addressed either by providing compensation in case of default of the third party or by ensuring that clients are appropriately informed of where their assets are deposited and to what extent they are protected by compensation arrangements.

4 b)

Should investors (such as UCITS or a UCITS unit holder) be able to claim compensation for loss of assets under the ICSD in those cases where the UCITS depositary or the institution which has been mandated to safe keep the assets, fail to perform its duty?

ICCL Response: (Please refer to our response to question 4a) above)

5) Should loss events include also any losses suffered by (retail) investors as a consequence of the violation of conduct of business rules?

ICCL Response: Given the 'hits' taken by the Irish scheme in compensating for physical losses of investor monies and securities, we would not be advocating an early extension of the Scheme to cover losses from the violation of conduct of business rules. Perhaps the risks should be addressed by strengthening the alternative regulatory and institutional mechanisms rather than by relying on the last resort protection mechanism i.e. compensation.

6) Do you agree with the idea that the amount covered by the ICSD should be adapted following the updating of the DGSD?

ICCL Response: There are two key factors to be considered in deciding whether to increase the minimum harmonised compensation limit from €20,000. Firstly, an analysis is required to establish to what extent the current limit has covered clients' losses. Secondly, consideration must be given to the capacity of Schemes to fund the increased compensation payouts which will result from increasing the limit.

The ICCL has experienced two significant failures since the scheme was established in 1998. The first failure occurred in 1999 and has cost the ICCL €772k in direct compensation payouts. The second failure occurred in 2001 and has cost the Scheme €7.45 million to date in direct compensation payouts. Approximately 2,900 claims have been dealt with in these cases and the existing limit (i.e. 90% of the client's loss up to a maximum limit of €20,000 per claimant) has satisfied 99% of the claims. While our experience does seem to point to the adequacy of the current minimum limits, we accept that the limits need to be increased to take account of inflation and in the general levels of increased retail client investment activity.

7) *The ICSD does not harmonize the funding systems of the schemes. Should the ICSD provide for some general principles concerning the funding of the schemes?*

ICCL Response: On 15 March 2006, the ICCL submitted a letter in response to the EU Commission's invitation to National Investor Compensation Schemes to provide the Commission with comments on the Oxera Report, its conclusions and policy recommendations. A copy of this letter is attached for information. In relation to funding for schemes, the ICCL supports many of Oxera's findings, namely:

1. Compensation schemes need to have backup funding in place and a guarantee from the State or other forms of State funding (e.g. direct lending) may be required (even if never activated).
2. Explicit guarantees are considered best practice for the deposit guarantee schemes.
3. There is a necessity for operating an annual cap on contributions from members to mitigate the open-ended liability on firms to fund the schemes. This is a particular problem if the scheme is reliant on a small number of firms to provide funding. The operation of such an annual cap requires that compensation schemes need to have backup funding in place.

The ICCL believes that the ICSD should incorporate some general principles to deal with the core issue raised by the ICCL, namely, in the event of a default of such magnitude that ICCL is unable to meet its compensation commitments from its own resources and from borrowings from the market, it should be permissible for the State to lend the shortfall at commercial rates or to provide a guarantee so as to enable the scheme to borrow the necessary funds. The scenario presupposes that the member firms would not be able to substantially increase their contributions to the scheme without precipitating further failures. The effect of such State facilities would be to enable the member firms to meet their obligations to the scheme over a longer time frame.

8) a) *Does the legislation of the Member State you know the best provide mechanisms aimed at limiting compensation schemes' obligations over time? If yes, how many clients saw their compensation unpaid as a result of such mechanisms?*

ICCL Response: Sections 35(2)(a) and 35(2)(b) of the Investor Compensation Act, 1998 provide for the postponement, in exceptional circumstances, of the

payment of compensation. Such postponement is subject to the approval of the supervisory authority and shall have regard to the requirements of Article 9 of the ICSD. To date, this mechanism has not been activated in Ireland and consequently no clients saw their compensation unpaid as a result of this mechanism.

8 b) Should this kind of mechanisms be prohibited?

ICCL Response: The ICCL supports the timely payment of compensation to claimants and believes that the matters raised in our response to question 7 above need to be addressed. If sufficient funds are available to facilitate the payment of compensation, then we do not foresee a need for the mechanisms referred to in 8 a).

9) a) Should the process of recognizing the eligibility of the claim be regulated for the purposes of the ICSD?

b) Should, at least, a mechanism be introduced providing for provisional partial compensation based on a summary assessment of clients' positions?

c) Irrespective of the harmonisation of their funding systems, should compensation schemes ensure that they have minimum reserve funds in order to comply rapidly with any immediate needs?

The deadlines for establishing the eligibility and the amount of the claim are determined by national law (notably insolvency law). The responsibility to establish the eligibility of the claim and its amount lies with different persons (mainly the liquidator or receiver of the insolvent firm or the scheme itself). In some Member States these deadlines can extend to several years, prolonged also through court proceedings in which the conclusions of the insolvency administrator are contested.

ICCL Response:

- The ICCL's experience demonstrates that significant delays, which were encountered in the certification of claims process, were due primarily to uncertainties surrounding both the accuracy of the books and records of the failed investment firm and the outcomes of legal actions being taken by the insolvency practitioner. The delays gave rise to higher than anticipated compensation costs. For example, due to considerable legal and receivership costs, client assets were accessed to defray these costs thus increasing the value of a client's claim for compensation and, as a

consequence, the level of compensation paid. The ICCL supports the development of pre-determined rules for the distribution of client assets in circumstances where investments firms fail.

- The ICCL's experience demonstrates that there are tangible benefits in the same person fulfilling the roles of insolvency practitioner as well as compensation claims administrator.
- Under certain defined conditions, the ICCL is in favour of facilitating, if possible, the early certification of low value claims, e.g. claims under €1,000, on the basis of a lesser standard of checking than is currently required. However, given the significant risks associated with this approach, the ICCL believes that it needs to be legally feasible and needs to be implemented at the discretion of and to the extent determined by Schemes on a case-by-case basis.
- Given the extensive measures taken by the ICCL to contact clients, the ICCL considers that the timeframe for the acceptance of late claims for compensation should be limited to a period no longer than 24 months from the date specified by the ICCL for receipt of claims, except in very exceptional circumstances.
- **Our views in relation to funding are outlined in our response under question 7.**

10) Do you think special attention should be given to money market funds?

The question has arisen whether some form of guarantee or investor compensation scheme should be extended to cover investments in these schemes in order to avoid competitive distortion between different types of savings or investment products. Money market funds have been perceived to be a safe investment within the global financial landscape, providing funds' shareholders with a constant value on their shares. They act as a means of helping governments and important institutions to raise short-term capital and providing a secure short-term and liquid investment for institutions with surplus cash.

In response to the recent crisis, the U.S. authorities announced in September 2008 a temporary guarantee program for the U.S. money market mutual fund industry, allowing money market funds to sell their illiquid assets to special purpose vehicles to release them from liquidity pressure they've been facing from shareholders redemption requests.

ICCL Response: The ICCL does not believe that these products could give rise to compensatable losses for eligible (essentially retail) investors and therefore does not believe that they should come within the scope of the ICSD.

11) Based on the concrete application of the ICSD do you see further issues other than the ones mentioned in the present document that might be of relevance to this analysis?

ICCL Response: The ICCL has no further comments.

We hope that you find these comments useful and we are happy to further discuss or clarify any of these matters if you require.

Yours sincerely,

A handwritten signature in blue ink, appearing to read 'P. Fitzgerald', written over the printed name.

Patricia Fitzgerald

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