

<p style="text-align: center;">REPORT OF THE DEPOSITOR COMPENSATION SCHEME FOR 2003</p>
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Introduction

In terms of regulation 8 of LN 369 of 2003, the Compensation Schemes Management Committee of the Depositor Compensation Scheme (hereinafter referred to as “the Scheme”) is pleased to present its report on the discharge of its functions and its operations during 2003.

The Scheme’s audited financial statements for 2003 are also attached.

Establishment of the Scheme

The Deposit Guarantee Scheme, as the Scheme was originally named, was established by Legal Notice 7 of 2003 and came into effect on 3rd January 2003.

Those Regulations have been subsequently repealed and replaced by Legal Notice 369 of 2003, which came into effect on 21st November 2003. This Legal Notice renamed the Scheme as the Depositor Compensation Scheme. The repeal of Legal Notice 7 of 2003 has not affected the validity of any previous action taken by the Scheme, since any such previous action is deemed to have been taken under the new Regulations.

Management Committee

In accordance with regulation 3 of the Regulations, the Scheme is managed and administered by a Management Committee (hereinafter referred to as “the Committee”) appointed by the Malta Financial Services Authority. Under the old regulations, the Committee consisted of a chairperson and not more than six other persons, appointed by Malta Financial Services Authority. The following persons have served on the Management Committee during 2003:

Chairman

Mr Frank Xerri de Caro

[Mr Frank Xerri de Caro resigned from his post as Chairman of the Committee with effect from 1 June 2003.]

Dr Anton Felice

[Dr Anton Felice has been appointed Chairman of the Committee with effect from 1 June 2003.]

Members

Mr Charles Borg

Dr Louis Camilleri Preziosi

[Dr Louis Camilleri Preziosi resigned as member of the Committee on 3 September 2003.]

Mr George F Farrugia

Mr Rene Saliba

Mr Paul Vella

Mr Geoffrey Bezzina has served as Secretary of the Committee.

The Management Committee held 10 meetings during 2003.

Functions of the Scheme

In terms of regulation 4, the functions of the Scheme are:

- (a) To maintain a fund for the payment of claims for compensation by depositors;
- (b) To place contributions to the fund on deposit or to invest such funds;
- (c) To establish procedures and arrangements for the payment of claims for compensation by depositors;
- (d) To handle and pay claims for compensation by depositors;
- (e) To advise the Malta Financial Services Authority on matters relating to compensation of depositors.

Building the Fund

The first function of the Scheme is to build and maintain a fund for the payment of claims to depositors.

For the purpose of achieving this goal, the Second Schedule of both Legal Notice 7 and Legal Notice 369 of 2003 provides that all credit institutions which participate in the Scheme are to make the following contributions to the Scheme:

- (a) Initial Contribution;
- (b) Supplementary Contributions;
- (c) Special Contributions.

According to the original Regulations all credit institutions which are licensed under the Banking Act were to participate and contribute to the Scheme.

According to the new Regulations, only those credit institutions which are licensed to accept deposits from private individuals (“depositors”) in Maltese lira are required to participate and contribute to the Scheme. Therefore credit institutions which are solely licensed to receive deposits from professional or institutional entities are excluded from participation. Equally excluded are those credit institutions whose licence precludes them from receiving deposits from private individuals in Maltese Lira.

In consideration of these foreseen amendments, the Committee decided to postpone the payment of the Initial Contribution with regards to credit institutions which do not accept deposits in Maltese lira from retail clients. This policy is still being monitored by the Committee.

At 31 December 2003, the Committee was still corresponding with the MFSA's Banking Unit in respect of the participation of one other bank which was licensed in 2003.

Initial Contribution

According to the Regulations, the minimum amount of the Initial Contribution is Lm10,000 per participant.

We report that this Initial Contribution totalling Lm50,000 has been collected from participating credit institutions.

The Committee, in consultation with the Competent Authority, agreed to postpone the payment of the Initial Contribution payable by a local bank for as long as it continues to operate under a restricted banking licence. However, the bank is required to make Supplementary Contributions to the Scheme for as long as it remains a separate legal entity.

Supplementary Contribution

The Regulations provide that a minimum amount of Lm1 million is to be contributed proportionately over a period not exceeding five years in accordance with each participants' share of the total eligible deposits.

According to Legal Notice 7 of 2003, the amount of eligible deposits is defined as the total aggregate liability of a depositor (other than those excluded under regulation 18) in accounts denominated in Maltese Lira. This definition of "eligible deposits" broadly encompassed all those deposits appertaining to private individuals or non-profit institutions.

The Committee determined that credit institutions may not easily be in a position to distinguish between accounts held by sole traders and personal accounts; nor between the professional and private accounts held by an individual. On the other hand it was henceforth important to retain such record in order to enable subsequent quantification of the amount of eligible deposits.

Towards this objective the Committee liaised with the Central Bank, and sought an adaptation of a monthly form (forming part of a compendium of monthly returns) commonly known as "Liabilities LD2" with which banks declare their liabilities and deposits to the Central Bank and MFSA. This form was modified to require a declaration of deposits pertaining to "Households and non-profit institutions" in Maltese Lira.

Although the level of supplementary contributions for each participant is calculated on eligible deposits held by the participant as at its most recent financial year end, the Committee decided to establish October 2003 as the basis for the assessment given that this was the first time that a declaration of such deposits had been made.

We report that at 31 December 2003 all participating licence holders, with the exception of one local bank, have duly fulfilled their obligation in respect of 2003 to transfer their supplementary contribution to the Fund, and that as at 31 December 2003, the total accumulated supplementary contribution amounted to Lm394,793.

We must also report that the basis of computation, assessed as it is on the amount of “eligible deposits”, has undergone a substantial modification by virtue of Legal Notice 369 of 2003. Whilst it had previously encompassed all deposits pertaining to private individuals as well as non-profit institutions, it is now only limited to deposits pertaining to private individuals. This change has had a substantial bearing on the treatment of deposits belonging to charitable and religious institutions. It is one factor which has led to the delay in the payment of the Supplementary Contribution by this local bank.

Special Contribution

There was no special commitment of the Scheme for which it was necessary to raise a Special Contribution.

Protection of funds

The Committee is required to deposit or invest the contributions that are made to the fund, until such time as they are required for the payment of claims for compensation by depositors.

In the performance of this task and in accordance with regulation 7 of Legal Notice 7 of 2003, the Committee appointed the Central Bank of Malta to provide investment management services including financial, accounting and other related support services. This appointment has been affected in terms of an agreement dated 2nd April 2003 which established the parameters for the investment of funds of the Scheme.

These parameters apply prudent investment criteria that take account of both the short and long term liquidity requirements of the Scheme.

In the furtherance of this Agreement, Mr Charles Borg and Mr Rene Saliba have been nominated by the Committee to liaise with the Central Bank as appropriate from time to time, as an Investment Management sub-Committee.

The Committee has also appointed Grant Thornton as auditors of the Scheme. Their audited financial statement of the accounts of the Scheme for 2003 is attached as a Schedule to this report.

Procedures for the payment of claims

The third function of the Scheme is to establish procedures for the payment of claims for compensation by depositors.

Eligibility to compensation

According to regulation 18 of Legal Notice 7 of 2003 only depositors could make a claim against the Scheme. Although the First Schedule contained a list of persons who were excluded from claiming against the Scheme, the Committee did experience certain doubts as to the correct interpretation of “depositor” and in particular whether certain non-profit making entities were excluded from making a claim against the Scheme.

The Malta Financial Services Authority has issued appropriate amendments, incorporated in Legal Notice 369 of 2003, as a result of which regulation 18 has been reworded to ensure that “only persons being individuals falling within the definition of “depositor” in Regulation 2 may make a claim against the Scheme.....”

Information booklet

The Committee is required to inform the general public about the procedures and arrangements for claiming against the Scheme. For this purpose it has set out to draft an information booklet that describes how depositors may claim against the Scheme and in which circumstances. The text of this booklet has been completed and is awaiting publication on the website of the Scheme once this is established.

Claim making Procedures

The Committee has also started deliberating on the need for establishing appropriate procedures and time limits governing the making and handling of claims.

Towards this goal, preliminary enquiries were made during 2003 with similar Schemes in other European territories with a view to sharing their experiences.

Compensation under foreign Schemes

Regulation 11 and 34 require the Committee to consult the relevant compensation schemes in other countries for the purpose of facilitating the procedures by which depositors may claim against the respective Schemes.

Towards this goal, the Committee has obtained a specimen Memorandum of Understanding from the UK Financial Services Compensation Scheme and this is presently being studied by the Committee.

The conclusion of bilateral agreements with other schemes in EEA territories will be particularly relevant following Malta's accession to the European Union. This is because overseas EU-based providers of investment services will not be required to participate to the Scheme even though they may be providing their services to Maltese residents. The availability of such Memorandum of Understanding with the relevant Schemes in these EEA territories will facilitate the procedures to be followed by Maltese residents in the event of a claim against the Schemes of these territories.

Depositors' Claims

The fourth function of the Scheme is to handle and pay claims to depositors.

We are pleased to report that during 2003 there have been no defaults of payments by participating credit institutions which give rise to a claim against the Scheme.

Consultation

The fifth function of the Scheme is to advise the Malta Financial Services Authority on matters relating to depositors' compensation.

This report has already summarised some of the more important proposals which the Committee for the strengthening of the Scheme. These have also included an amendment to the Banking Act to exempt the Scheme from payment of income tax.

These proposals have been accepted by the Malta Financial Services Authority and incorporated in Legal Notice 369 of 2003. However the Malta Financial Services Authority has not favoured other proposals which were made by the Committee including that the management committee of the Depositor Compensation Scheme should be separate and distinct from the Committee of the Investor Compensation Scheme.

List of Participants

APS Bank Limited
Bank of Valletta p.l.c.
HSBC Bank Malta plc
Lombard Bank Malta plc
Volksbank Malta Limited
HSBC Home Loans Limited



Dr Anton Felice
Chairman – Compensation Schemes Management Committee

Monday, April 26, 2004