DEPOSITOR COMPENSATION SCHEME

Annual Report and Financial Statements

31 December 2018

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GENERAL INFORMATION

The Depositor Compensation Scheme was established by virtue of the Depositor Compensation Scheme Regulations, Legal Notice 369 of 2003 (amended) of the Laws of Malta.

On 4 December 2015, Legal Notice 383 of 2015 has been published in the Government Gazette. The legal notice replaces legal notice 369 of 2003 and transposes directive 2014/49/EU, the recast Depositor Guarantee Scheme Directive.

MEMBERS OF THE MANAGEMENT COMMITTEE

Mr. Robert Caruana - Chairman (appointed Chairman on 23 April 2018)
Dr. Anton Felice - Chairman (resigned from member and Chairman on 29 March 2018)
Mr. Benny Borg Bonello (resigned on 31 December 2018)
Mr. George Farrugia
Mr. Kenneth Farrugia
Dr. Massimo Vella (resigned on 31 December 2018)
Mr. James Bonello (resigned on 31 August 2018)
Mr. Silvio Galea (appointed on 23 April 2018)
Mr. Karol Gabarretta (appointed on 1 September 2018)
Dr. Mauro Magro (appointed on 8 May 2019)
Dr. Edmond Zammit Laferla (appointed on 8 May 2019)

COMMITTEE'S SECRETARY

Mr Aldo Giordano

ADDRESS

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Notabile Road
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INVESTMENT MANAGERS

Central Bank of Malta
Pjazza Kastilja
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BANKERS

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AUDITOR

Ernst & Young Malta Limited
Certified Public Accountants
Regional Business Centre
Achille Ferris Street
Msida MSD 1751
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REPORT OF THE MANAGEMENT COMMITTEE OF THE SCHEME

The Management Committee of the Scheme submit their annual report together with the audited financial statements for the year ended 31 December 2018.

Principal activity

The Depositor Compensation Scheme was established by virtue of the Depositor Compensation Scheme Regulations (the "Regulations"), Legal Notice 369 of 2003 (amended) of the Laws of Malta for the purposes of carrying out the functions defined in the said Regulations.

On 4 December 2015, Legal Notice 383 of 2015 has been published in the Government Gazette. The legal notice replaces Legal Notice 369 of 2003 and transposes directive 2014/49/EU, the recast Depositor Guarantee Scheme Directive. Legal notice 383 of 2015 was amended by legal notice 132 of 2017 and 43 of 2019.

The main objective of the Scheme is to provide a means of protection for depositors within the framework of the Regulations. The Scheme maintains a fund out of which payments will be made to depositors where it appears that a participant to such Scheme is unable to repay money owed to or belonging to depositors and held on their behalf in connection with the banking business.

Results

The results are shown in the Statement of Comprehensive Income, set out on page 7.

As at year end, the total contributions paid to the Scheme amounted to EUR19,386,678 (2017: EUR10,006,004). This is disclosed net of compensation payable amounting to EUR 34,625,489 (2017: EUR34,780,249) (note 19). Furthermore, as at year end, the participants, as part of their obligations in terms of Article 5 of Schedule 2 of the Regulations, had pledged in favour of the scheme EUR88,649,072 (2017: EUR91,895,382) and paid directly to the Scheme the amount of EUR7,083,833 (2017: EUR9,060,306).

Members of the Management Committee

The Members who served during the year under review and any changes thereof, were as noted on page 2.

In accordance with Regulation 3 of the Regulations, the Scheme is managed and administered by the Management Committee. Such committee is appointed by the Malta Financial Services Authority for a maximum period of not less than three years but not more than five years. Every member of the Committee shall be eligible for re-appointment.

Statement of committee members' responsibilities

The committee members are required by the Regulations, Legal Notice 383 of 2015 as amended by legal notice 132 of 2017 and 43 of 2019 of the Laws of Malta to prepare financial statements which give a true and fair view of the state of affairs of the Scheme as at the end of each financial year and of the income and expenditure for that year.

The Committee members are responsible to:

- Select suitable accounting policies and apply them consistently;
- Make judgements and estimates that are reasonable;
- Prepare the financial statements on a going concern basis, unless it is inappropriate to presume that the Scheme will continue as a going concern;
- Account for income and charges relating to the accounting period on the accruals basis;
- Value separately the components of asset and liability items; and
- Report comparative figures corresponding to those of the preceding accounting period.

The committee members are also responsible for designing, implementing and maintaining internal control relevant to the preparation and the fair presentation of the financial statements that are free from material misstatement, whether due to fraud and error, and that comply with the Regulations, Legal Notice 383 of 2015 of the Laws of Malta. They are also responsible for safeguarding the assets of the Scheme and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

REPORT OF THE MANAGEMENT COMMITTEE OF THE SCHEME - continued

Auditor

Ernst & Young Malta Limited have expressed their willingness to continue in office.

The report of the Members was approved and signed on their behalf by:

ROBERT CARUANA
Chairman

GEORGE FARRUGIA
Member

c/o Malta Financial Services Authority
Notabile Road
Attard

29 May 2019

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INDEPENDENT AUDITOR'S REPORT
to the members of the Investor Compensation Scheme

Report on the audit of the financial statements

Opinion
We have audited the financial statements of the Depositor Compensation Scheme ('the Scheme'), set on pages 7 to 25, which comprise the statement of financial position as at 31 December 2018, and the statement of comprehensive income, the statement of changes in funds and the statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements give a true and fair view of the financial position of the Scheme as at 31 December 2018, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the EU ("IFRS") and the Depositor Compensation Scheme Regulations, Legal Notice 383 of 2015 (the "Regulations").

Basis for opinion
We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Scheme in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code) together with the ethical requirements that are relevant to our audit of the financial statements in accordance with the *Accountancy Profession (Code of Ethics for Warrant Holders) Directive issued in terms of the Accountancy Profession Act, Cap. 281 of the Laws of Malta*, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Other Information
The Management Committee are responsible for the other information. The other information comprises the information included in the Annual Report, other than the financial statements and our auditor's report thereon.

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the Management Committee for the financial statements
The Management Committee is responsible for the preparation and fair presentation of the financial statements in accordance with IFRS and the requirements of the Regulations, and for such internal control as the Management Committee determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Management Committee is responsible for assessing the Scheme's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Management Committee either intend to liquidate the Scheme or to cease operations, or have no realistic alternative but to do so.

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INDEPENDENT AUDITOR'S REPORT
to the members of the Depositor Compensation Scheme - continued

Auditor's responsibilities for the audit of the financial statements
Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Scheme's internal control.
- evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Management Committee.
- conclude on the appropriateness of the Management Committee' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Scheme's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Scheme to cease to continue as a going concern.
- evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with the Management Committee regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

The partner in charge of the audit resulting in this independent auditor's report is Christopher Balzan for and on behalf of

Ernst & Young Malta Limited
Certified Public Accountants

29 May 2019

STATEMENT OF COMPREHENSIVE INCOME

	Notes	2018 EUR	2017 EUR
Income from available financial means	6	**418,148**	2,912,266
Management expenses	7	**(227,406)**	(157,974)
Surplus for the year		**190,742**	2,754,292
Other comprehensive income to be reclassified to profit or loss in subsequent periods			
Net loss on available-for-sale financial assets - Investments		**-**	(3,438,580)
Net loss on fair value though OCI financial assets - Investments		**(329,269)**	-
Total comprehensive loss for the year		**(138,527)**	(684,288)

The accounting policies and explanatory notes on pages 11 to 25 form an integral part of the financial statements.

STATEMENT OF FINANCIAL POSITION

	Notes	2018 EUR	2017 EUR
ASSETS			
Non-current assets			
Financial assets - Investments	9	**17,551,773**	25,054,757
Property, plant and equipment	10	**730,465**	105,758
		18,282,238	25,160,515
Current assets			
Financial assets - Investments	9	**13,171,297**	1,254,385
Receivables	11	**178,031**	340,131
Cash at bank		**9,081,122**	8,774,215
		22,430,450	10,368,731
TOTAL ASSETS		**40,712,688**	35,529,246
FUNDS AND LIABILITIES			
Funds and reserves			
Contributions fund	13	**17,789,268**	9,045,096
Other contributions fund	16	**1,597,410**	960,908
Special contribution fund	15	**7,083,833**	9,060,306
Revaluation reserve	9c/17	**1,346,336**	1,675,605
Accumulated fund	17	**9,914,725**	9,723,983
		37,731,572	30,465,898
Current liabilities			
Other payables	18	**339,551**	27,293
Repurchase agreements	9	**2,510,765**	4,870,919
Compensation payable	19	**130,800**	165,136
		2,981,116	4,916,373
TOTAL FUNDS AND LIABILITIES		**40,712,688**	35,529,246
MEMORANDUM ITEMS			
Assets pledged in favour of the Scheme	12	**88,649,072**	91,895,382

The accounting policies and explanatory notes on pages 11 to 25 form an integral part of the financial statements.

The financial statements on pages 7 to 25 have been approved by the Management Committee on 29 May 2019 and were signed on its behalf by:

ROBERT CARUANA
Chairman

GEORGE FARRUGIA
Member

STATEMENT OF CHANGES IN FUNDS

	Contributions fund EUR	Other contributions fund EUR	Special contribution fund EUR	Revaluation reserve EUR	Management expense contribution fund EUR	Accumulated fund EUR	Total EUR
At 1 January 2018	**9,045,096**	**960,908**	**9,060,306**	**1,675,605**	**-**	**9,723,983**	**30,465,898**
Surplus for the year	-	-	-	-	(227,406)	418,148	190,742
Other comprehensive income	-	-	-	(329,269)	-	-	(329,269)
Transfer between reserves (notes 13,16)	(636,502)	636,502	-	-	227,406	(227,406)	-
Contributions for the year	9,380,674	-	(1,976,473)	-	-	-	7,404,201
At 31 December 2018	**17,789,268**	**1,597,410**	**7,083,833**	**1,346,336**	**-**	**9,914,725**	**37,731,572**
At 1 January 2017	**32,683,339**	**765,483**	**3,039,767**	**5,114,185**	**-**	**6,969,691**	**48,572,465**
Surplus for the year	-	-	-	-	(157,974)	2,912,266	2,754,292
Other comprehensive income	-	-	-	(3,438,580)	-	-	(3,438,580)
Transfer between reserves (notes 13,16)	(195,425)	195,425	-	-	157,974	(157,974)	-
Contributions for the year	11,337,431	-	6,020,539	-	-	-	17,357,970
Compensation payable (note 19)	(34,780,249)	-	-	-	-	-	(34,780,249)
At 31 December 2017	**9,045,096**	**960,908**	**9,060,306**	**1,675,605**	**-**	**9,723,983**	**30,465,898**

The accounting policies and explanatory notes on pages 11 to 25 form an integral part of the financial statements.

STATEMENT OF CASH FLOWS

	2018 EUR	2017 EUR
Operating activities		
Surplus for the year	**190,742**	2,754,292
Adjustment to reconcile surplus to net cash flow		
Non cash:		
Interest receivable	**(1,276,508)**	(1,495,343)
Amortisation of net premiums	**805,012**	856,201
Gain on sale of investments	**-**	(2,323,826)
Working capital adjustment:		
Increase in other payables	**14,607**	3,228
Interest received	**1,451,427**	1,518,018
Net cash flow from operating activities	**1,185,280**	1,312,570
Investing activities		
Payments to acquire financial assets	**(6,752,496)**	(268,658)
Proceeds on maturity/sale of financial assets	**1,204,287**	18,882,178
Purchase of Property, plant and equipment	**(322,204)**	(105,758)
Net cash flows used in investing activities	**(5,870,413)**	18,507,762
Financing activities		
Repo	**(2,360,154)**	4,870,919
Interest paid on Repo	**(17,671)**	(20,150)
Contributions received	**7,404,201**	17,357,970
Compensation paid	**(34,336)**	(34,615,113)
Net cash flows used in financing activities	**4,992,040**	(12,406,374)
Net movement in cash and cash equivalents	**306,907**	7,413,958
Cash and cash equivalents at 1 January	**8,774,215**	1,360,257
Cash and cash equivalents at 31 December	**9,081,122**	8,774,215

The accounting policies and explanatory notes on pages 11 to 25 form an integral part of the financial statements.

NOTES TO THE FINANCIAL STATEMENTS

1. SCOPE AND FUNCTIONS OF THE SCHEME

The Depositor Compensation Scheme ("the Scheme") was established on 23 November 2003 by virtue of the Depositor Compensation Regulations, ("the Regulations") Legal Notice 369 of 2003 (amended) of the Laws of Malta.

On 4 December 2015, Legal Notice 383 of 2015 has been published in the Government Gazette. The legal notice replaces legal notice 369 of 2003 and transposes directive 2014/49/EU, the recast Depositor Guarantee Scheme Directive. Legal notice 383 of 2015 was amended by legal notice 132 of 2017 and 43 of 2019. The scheme may require members to pay a Compensation Contribution and/or a Management Expenses Contribution commencing from the financial year ending 31 December 2016. The Compensation Contribution is allocated to the available financial means which shall amount to at least 1.3% of the covered deposits of its members.

The Scheme is intended to promote confidence in licensed banks by providing a means of protection for depositors within the framework of the Regulations. The Scheme shall also carry out various other related functions and duties as set out in Regulation 4(1) of the Regulations.

2. BASIS OF PREPARATION AND STATEMENT OF COMPLIANCE

These financial statements have been prepared under the historical cost convention except for investments financial assets that have been measured at fair value. These financial statements are in accordance with International Financial Reporting Standards as adopted by the EU and comply with Legal Notice 369 of 2003 (amended) of the Laws of Malta.

3. CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES

Standards, interpretations and amendments to published standards as endorsed by the European Union effective in the current year

The accounting policies adopted are consistent with those of the previous financial year, except for the following amendments to IFRS effective during the year:

- IFRS 9 Financial Instruments
- Amendments to IFRS 2 Classification and measurement of share-based payment transactions
- IFRS 15 Revenue from Contracts with customers including amendments to IFRS 15
- Clarifications to IFRS 15 Revenue from contracts with customers
- Amendments to IFRS 4 Applying IFRS 9 Financial Instruments with IFRS 4 insurance contracts
- IFRIC Interpretation 22 Foreign Currency Transactions and advance consideration
- Amendments to IAS 40 Transfers of Investment property
- Annual Improvements to IFRSs 2014-2016 Measuring an associate or joint venture at fair value
- Annual Improvements to IFRSs 2014-2016 Deletion of short term exemptions for first time adopters

Other than disclosed below, the adoption of these standards, where applicable, did not have significant impact on the financial statements or performance of the Scheme. The nature and effect of the changes as a result of the adoption of IFRS 9 are described below.

IFRS 9 – Financial instruments

In July 2014, the IASB issued IFRS 9 Financial Instruments, the standard that has replaced IAS 39 for annual periods on or after 1 January 2018. The Scheme have initially adopted IFRS 9 Financial Instruments in the current period from 1 January 2018. The standard was applied retrospectively using the cumulative effect method with the effects of initially applying this standard recognised in equity at the date of initial application at 1 January 2018. Accordingly, the comparative information for 2017 has not been restated and continues to be reported under IAS 39 Financial Instruments: Recognition and Measurement. Additionally, the disclosure requirements resulting from the consequential amendments to IFRS 7 have not generally been applied to comparative information. The significant accounting policies under IAS 39 continue to apply to the 2017 comparative figures.

NOTES TO THE FINANCIAL STATEMENTS - continued

3. CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES – continued

Standards, interpretations and amendments to published standards as adopted by the European Union effective in the current year - continued

IFRS 9 – Financial instruments - continued

Classification and measurement

From a classification and measurement perspective, the new standard requires all financial assets, except equity instruments and derivatives, to be assessed based on a combination of the entity's business model for managing the assets and the instruments' contractual cash flow characteristics. The IAS 39 measurement categories have been replaced by: Fair value through profit or loss (FVPL), fair value through other comprehensive income (FVOCI), and amortised cost. IFRS 9 allows entities to continue to irrevocably designate instruments that qualify for amortised cost or fair value through OCI instruments as FVPL, if doing so eliminates or significantly reduces a measurement or recognition inconsistency. Equity instruments that are not held for trading may be irrevocably designated as FVOCI, with no subsequent reclassification of gains or losses to the income statement.

The accounting for financial liabilities is largely the same as the requirements of IAS 39, except for the treatment of gains or losses arising from an entity's own credit risk relating to liabilities designated at FVPL. Such movements are presented in OCI with no subsequent reclassification to the income statement, unless an accounting mismatch in profit or loss would arise.

The Scheme has concluded that the financial assets previously classified as available-for-sale investments under IAS 39 are classified at fair value through OCI under IFRS 9. There is no financial impact arising as the accounting measurement is the same as under IAS39.

Impairment of financial assets

IFRS 9 has fundamentally changed the impairment methodology. The standard replaces IAS 39's incurred loss approach with a forward-looking expected credit loss (ECL) approach. The Scheme is required to record an allowance for expected credit losses for all loans and other debt financial assets not held at FVPL, together with loan commitments and financial guarantee contracts. The allowance is based on the expected credit losses associated with the probability of default in the next twelve months (12-month ECL) unless there has been a significant increase in credit risk since origination, in which case, the allowance is based on the probability of default over the life of the asset (lifetime ECL).

The general principle of IFRS 9 is that ECL accounting requires that the credit risk of financial instruments within the scope of impairment to be assessed for significant increase since initial recognition at each reporting sheet date. If there is a significant increase in credit risk, lifetime ECL is recognised. The principle of significant deterioration in credit risk can be achieved by performing an assessment to compare the risk of default occurring at the reporting date with the risk of default occurring at the date of initial recognition.

IFRS 9 did not materially impact the impairment calculation of the Scheme.

NOTES TO THE FINANCIAL STATEMENTS - continued

3. CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES – continued

Standards, interpretations and amendments to published standards as adopted by the EU which are not yet effective

Up to date of approval of these financial statements, certain new standards, amendments and interpretations to existing standards have been published but which are not yet effective for the current reporting year and which the Scheme has not early adopted, but plans to adopt upon their effective date. The new and amended standards follow:

- IFRS 16 Leases (effective for financial year beginning on or after 1 January 2019)
- IFRIC 23 Uncertainty over Income Tax Treatments (effective for financial year beginning on or after 1 January 2019)
- Amendments to IFRS 9: Prepayment Features with Negative Compensation (effective for financial year beginning on or after 1 January 2019)
- Amendments to IAS 19: Plan Amendment, Curtailment or Settlement (effective for financial year beginning on or after 1 January 2019)
- Amendments to IAS 28: Long-term Interests in Associates and Joint Ventures (effective for financial year beginning on or after 1 January 2019)
- Amendments to IAS12 Income tax consequences of payments on financial instruments classified as equity (effective for financial year beginning on or after 1 January 2019)
- Amendments to IAS23 Borrowing costs eligible for capitalisation (effective for financial year beginning on or after 1 January 2019)
- Amendments to IFRS 3 and IFRS 11 Previously held interest in a joint operation (effective for financial year beginning on or after 1 January 2019)

Standards, interpretations and amendments that are not yet endorsed by the EU

- IFRS 17 – Insurance Contracts (effective for financial year beginning on or after 1 January 2021)
- IFRIC 23 – Uncertainty over Income Tax Treatments (effective for financial year beginning on or after 1 January 2019)
- IAS 28 (Amendments) – Long-term Interests in Associates and Joint Ventures (effective for financial year beginning on or after 1 January 2019)
- Amendments to IAS19: Plan Amendment, Curtailment or Settlement (effective for financial year beginning on or after 1 January 2019)
- Annual Improvements to IFRS Standards 2015-2017 Cycle (effective for financial year beginning on or after 1 January 2019)
- Amendments to references to the Conceptual framework in IFRS Standards (effective for financial year beginning on or after 1 January 2020)

The Scheme is still assessing the impact that these new standards will have on the financial statements.

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Interest income

For all financial instruments measured at amortised cost and interest bearing financial assets classified as available-for-sale, interest income is recorded using the effective interest rate (EIR), which is the rate that exactly discounts the estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or liability. Interest income is included in income in the statement of comprehensive income.

NOTES TO THE FINANCIAL STATEMENTS - continued

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continued

Financial instruments

Policies applicable after 1 January 2018

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.

Financial assets

From 1 January 2018 the Scheme had adopted the following accounting policies to its financial instruments:

Initial recognition and measurement

Financial assets are classified, at initial recognition, as subsequently measured at amortised cost, fair value through other comprehensive income (OCI), and fair value through profit or loss.

The classification of financial assets at initial recognition depends on the financial asset's contractual cash flow characteristics and the Scheme's business model for managing them. With the exception of trade receivables that do not contain a significant financing component or for which the Scheme has applied the practical expedient, the Scheme initially measures a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss, transaction costs.

In order for a financial asset to be classified and measured at amortised cost or fair value through OCI, it needs to give rise to cash flows that are 'solely payments of principal and interest (SPPI)' on the principal amount outstanding. This assessment is referred to as the SPPI test and is performed at an instrument level.

Subsequent measurement

For purposes of subsequent measurement, financial assets are classified in four categories:

- Financial assets at amortised cost (debt instruments)
- Financial assets at fair value through OCI with recycling of cumulative gains and losses (debt instruments)
- Financial assets designated at fair value through OCI with no recycling of cumulative gains and losses upon derecognition (equity instruments)
- Financial assets at fair value through profit or loss

Financial assets at amortised cost (debt instruments)

This category is the most relevant to the Scheme. The Scheme measures financial assets at amortised cost if both of the following conditions are met:

- The financial asset is held within a business model with the objective to hold financial assets in order to collect contractual cash flows
  and
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Financial assets at amortised cost are subsequently measured using the effective interest (EIR) method and are subject to impairment. Gains and losses are recognised in profit or loss when the asset is derecognised, modified or impaired.

NOTES TO THE FINANCIAL STATEMENTS - continued

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continued

Financial instruments - continued

Financial assets - continued

Financial assets at fair value through OCI (debt instruments)

The Scheme measures debt instruments at fair value through OCI if both of the following conditions are met:

- The financial asset is held within a business model with the objective of both holding to collect contractual cash flows and selling
  and
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

For debt instruments at fair value through OCI, interest income, foreign exchange revaluation and impairment losses or reversals are recognised in the statement of profit or loss and computed in the same manner as for financial assets measured at amortised cost. The remaining fair value changes are recognised in OCI. Upon derecognition, the cumulative fair value change recognised in OCI is recycled to profit or loss.

Financial assets designated at fair value through OCI (equity instruments)

Upon initial recognition, the Scheme can elect to classify irrevocably its equity investments as equity instruments designated at fair value through OCI when they meet the definition of equity under IAS 32 Financial Instruments: Presentation and are not held for trading. The classification is determined on an instrument-by-instrument basis

Gains and losses on these financial assets are never recycled to profit or loss. Dividends are recognised as other income in the statement of profit or loss when the right of payment has been established, except when the Scheme benefits from such proceeds as a recovery of part of the cost of the financial asset, in which case, such gains are recorded in OCI. Equity instruments designated at fair value through OCI are not subject to impairment assessment.

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss include financial assets held for trading, financial assets designated upon initial recognition at fair value through profit or loss, or financial assets mandatorily required to be measured at fair value. Financial assets are classified as held for trading if they are acquired for the purpose of selling or repurchasing in the near term. Derivatives, including separated embedded derivatives, are also classified as held for trading unless they are designated as effective hedging instruments. Financial assets with cash flows that are not solely payments of principal and interest are classified and measured at fair value through profit or loss, irrespective of the business model. Notwithstanding the criteria for debt instruments to be classified at amortised cost or at fair value through OCI, as described above, debt instruments may be designated at fair value through profit or loss on initial recognition if doing so eliminates, or significantly reduces, an accounting mismatch.

Financial assets at fair value through profit or loss are carried in the statement of financial position at fair value with net changes in fair value recognised in the statement of profit or loss.

NOTES TO THE FINANCIAL STATEMENTS - continued

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continued

Financial instruments - continued

Financial assets - continued

Derecognition

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is primarily derecognised when:

- The rights to receive cash flows from the asset have expired
  or
- The Scheme has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass-through' arrangement; and either (a) the Scheme has transferred substantially all the risks and rewards of the asset, or (b) the Scheme has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the Scheme has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, it evaluates if, and to what extent, it has retained the risks and rewards of ownership. When it has neither transferred nor retained substantially all of the risks and rewards of the asset, nor transferred control of the asset, the Scheme continues to recognise the transferred asset to the extent of its continuing involvement

Impairment of financial assets

The Scheme recognises an allowance for expected credit losses (ECLs) for all debt instruments not held at fair value through profit or loss. ECLs are based on the difference between the contractual cash flows due in accordance with the contract and all the cash flows that the Scheme expects to receive, discounted at an approximation of the original effective interest rate. The expected cash flows will include cash flows from the sale of collateral held or other credit enhancements that are integral to the contractual terms.

ECLs are recognised in two stages. For credit exposures for which there has not been a significant increase in credit risk since initial recognition, ECLs are provided for credit losses that result from default events that are possible within the next 12-months (a 12-month ECL). For those credit exposures for which there has been a significant increase in credit risk since initial recognition, a loss allowance is required for credit losses expected over the remaining life of the exposure, irrespective of the timing of the default (a lifetime ECL).

Impairment of financial assets – continued

For trade receivables and contract assets, the Scheme applies a simplified approach in calculating ECLs. Therefore, the Scheme does not track changes in credit risk, but instead recognises a loss allowance based on lifetime ECLs at each reporting date. The 12-month ECL is calculated by multiplying the 12-month PD, LGD, and EAD. Lifetime ECL is calculated on a similar basis for the residual life of the exposure.

Financial liabilities

Initial recognition and measurement

Financial liabilities are classified, at initial recognition, as financial liabilities at fair value through profit or loss, loans and borrowings, payables, or as derivatives designated as hedging instruments in an effective hedge, as appropriate.

All financial liabilities are recognised initially at fair value and, in the case of loans and borrowings and payables, net of directly attributable transaction costs.

NOTES TO THE FINANCIAL STATEMENTS - continued

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continued

Financial instruments - continued

Financial liabilities - continued

Subsequent measurement

The measurement of financial liabilities depends on their classification, as described below:

Financial liabilities at fair value through profit or loss

Financial liabilities at fair value through profit or loss include financial liabilities held for trading and financial liabilities designated upon initial recognition as at fair value through profit or loss.

Financial liabilities are classified as held for trading if they are incurred for the purpose of repurchasing in the near term. This category also includes derivative financial instruments entered into by the Scheme that are not designated as hedging instruments in hedge relationships as defined by IFRS 9.

Gains or losses on liabilities held for trading are recognised in the statement of profit or loss.
Financial liabilities designated upon initial recognition at fair value through profit or loss are designated at the initial date of recognition, and only if the criteria in IFRS 9 are satisfied.

Loans and borrowings

After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost using the EIR method. Gains and losses are recognised in profit or loss when the liabilities are derecognised as well as through the EIR amortisation process. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the EIR. The EIR amortisation is included as finance costs in the statement of profit or loss.

Prior to its adoption of IFRS 9 in 2018, the Scheme had applied IAS 39. As a result the comparative information provided continues to be accounted for in accordance with the Scheme's previous accounting policy.

Derecognition

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires. When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as the derecognition of the original liability and the recognition of a new liability. The difference in the respective carrying amounts is recognised in the statement of profit or loss.

Offsetting of financial instruments

Financial assets and financial liabilities are offset and the net amount is reported in the statement of financial position if there is a currently enforceable legal right to offset the recognised amounts and there is an intention to settle on a net basis, to realise the assets and settle the liabilities simultaneously.

Policies applicable before 1 January 2018

Financial assets

Financial assets in the scope of IAS 39 are classified as, either financial assets at fair value through profit or loss, loans and receivables, held-to-maturity financial assets and available-for-sale financial assets, as appropriate. All financial assets are initially recognised at cost, being the fair value of the consideration given, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs. The Scheme determines the classification of its financial assets after initial recognition and, where allowed and appropriate, re-evaluates this designation at each financial year-end.

NOTES TO THE FINANCIAL STATEMENTS - continued

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continued

Financial instruments - continued

Financial assets - continued

The Scheme has classified its financial assets as 'available-for-sale' financial assets. The latter are debt securities which are intended to be held for an indefinite period of time and which may be sold in response to needs for liquidity and in response to changes in market conditions.

After initial recognition, financial assets which are classified as 'available-for-sale' are measured at fair value, without any deduction for transaction costs that may be incurred on sale or other disposal. Unrealised gains or losses on available-for-sale securities are reported as a separate component of reserves until the financial asset is sold, collected or otherwise disposed of, or until the investment is determined to be impaired, at which time the cumulative gain or loss previously reported in reserves is included in income.

For financial assets actively traded in organised financial markets, fair value is generally determined by reference to quoted market bid prices at the close of business on the reporting date. For investments where there is no quoted market price, a reasonable estimate of the fair value is determined using valuation techniques. Such techniques include using recent arm's length market transactions, reference to the current market value of another instrument which is substantially the same, discounted cash flow analysis based on the expected cash flows of the underlying net asset base of the investment and option pricing models.

Impairment of financial assets

The Scheme assesses, at each reporting date, whether there is objective evidence that a financial asset or a group of financial assets is impaired. An impairment exists if one or more events that has occurred since the initial recognition of the asset (an incurred 'loss event'), has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that the debtors or a group of debtors is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation and observable data indicating that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

Derecognition of financial assets

A financial asset is derecognised (or, where applicable a part of a financial asset or part of a group of similar financial assets) when:

- the right to receive cash flows from the asset has expired;
- the right to receive cash flows from the asset is retained, but the Scheme has assumed an obligation to pay them in full without material delay to a third party under a 'pass through' arrangement; or
- the rights to receive cash flows from the asset have been transferred and either the Scheme (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Property, plant and equipment

Property, plant and equipment are stated at historical cost less accumulated depreciation and accumulated impairment losses.

NOTES TO THE FINANCIAL STATEMENTS - continued

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continued

Property, plant and equipment - continued

Depreciation is provided on a straight-line basis to write off the cost of property, plant and equipment less any residual value over the expected useful lives. The annual rates used for this purpose, which are consistent with those used in the previous year, are as follows:

Computer equipment	5 years
Computer software	10 years

The depreciation method applied and the useful life are reviewed, and adjusted if appropriate, at the end of each reporting year. Depreciation of an asset ceases when the asset is either classified as held for sale or derecognised. Assets in the course of construction are not depreciated.

Property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected from their use or disposal. Gains or losses arising from derecognition represent the difference between the net disposal proceeds, if any, and the carrying amount of the asset. These are included in the statement of comprehensive income in the year of derecognition.

Subsequent costs are included in the asset's carrying amount when it is probable that future economic benefits associated with the item will flow to the Scheme and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the profit and loss account during the financial period in which they are incurred.

Cash and cash equivalents

Cash in hand and at banks are carried at cost.

Cash and cash equivalents are defined as cash in hand, demand deposits and short-term, highly liquid investments readily convertible to known amounts of cash and subject to insignificant risk of changes in value. For purposes of the Statement of cash flows, cash and cash equivalents consist of cash in hand and deposits at banks.

Other payables

Liabilities for other amounts payable are carried at cost which is the fair value of the consideration to be paid in the future for goods and services received, whether or not billed to the Scheme.

5. SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS

In preparing the financial statements, the management committee is required to make judgements, estimates and assumptions that affect reported income, expenses, assets, liabilities and disclosure of contingent assets and liabilities. Use of available information and application of judgment are inherent in the formation of estimates. Actual results in the future could differ from such estimates and the differences may be material to the financial statements. These estimates are reviewed on a regular basis and if a change is needed, it is accounted for in the period the changes become known.

In the opinion of the management committee, the accounting estimates, assumptions and judgements made in the course of preparing these financial statements are not difficult, subjective or complex to a degree which would warrant their description as significant in terms of the requirements of IAS 1 (revised)- 'Presentation of financial statements'.

NOTES TO THE FINANCIAL STATEMENTS - continued

6. INCOME

	2018 EUR	2017 EUR
Interest on investments	**1,276,508**	1,495,343
Amortisation of net premiums	**(805,012)**	(856,201)
Gain on sale of investments	**-**	2,323,826
Interest expense	**(53,348)**	(50,702)
Income from available financial means	**418,148**	2,912,266

7. EXPENSES BY NATURE

	2018 EUR	2017 EUR
Committee members' honoraria	**30,485**	27,752
Salaries	**132,647**	83,043
Auditor's remuneration	**2,500**	2,500
Membership fees	**2,500**	1,626
Broker's Commission	**-**	11,691
Legal and professional fees	**23,735**	11,501
Travelling expenses	**3,626**	666
Central Bank of Malta management fee	**5,015**	5,015
Other Staff costs	**8,278**	8,537
I.T. related expenses	**16,749**	2,313
Others	**1,871**	3,329
Total management expenses	**227,406**	157,974

8. TAXATION

The Depositor Compensation Scheme is exempt from taxation under section 28A of the Banking Act, Cap 371 of the Laws of Malta.

9. FINANCIAL ASSETS - INVESTMENTS

Until 1 January 2018, Investments were classified as Available-for-sale financial assets. Following the adoption of IFRS 9 - Financial instruments (note 4), Investments were classified as fair value through OCI.

a. The fair value of the financial assets is as follows:

	2018 EUR	2017 EUR
Non-current		
Malta Government Stocks	**17,551,773**	25,054,757
Current		
Malta Government Stocks	**13,171,297**	1,254,385
Total financial assets	**30,723,070**	26,309,142

NOTES TO THE FINANCIAL STATEMENTS - continued

9. FINANCIAL ASSETS - INVESTMENTS - continued

b. The amortised cost of the financial assets is as follows:

	2018 EUR	2017 EUR
Non-current		
Malta Government Stocks	**16,133,305**	23,413,699
Current		
Malta Government Stocks	**13,243,428**	1,219,838
Total financial assets	**29,376,733**	24,633,537

c. The accumulated fair value movements of the financial assets is as follows:

	2018 EUR	2017 EUR
Non-current		
Malta Government Stocks	**1,418,468**	1,641,058
Current		
Malta Government Stocks	**(72,132)**	34,547
Total financial assets	**1,346,336**	1,675,605

The carrying amount of securities sold under agreements to repurchase as at 31 December 2018 amounted to EUR2.46m (2017: EUR4.77m).

Fair value hierarchy

As at 31 December 2018 and 2017, the Scheme held the following financial instruments measured at fair value. The Scheme uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities

Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly

Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

	Total EUR	Level 1 EUR	Level 2 EUR	Level 3 EUR
Financial assets - Investments				
31 December 2018	**30,723,070**	**30,723,070**	**-**	**-**
31 December 2017	26,309,142	26,309,142	-	-

During the reporting years ended 31 December 2018 and 2017, there were no transfers between Level 1 and Level 2 fair value measurements, and no transfers into and out of Level 3 fair value measurements.

NOTES TO THE FINANCIAL STATEMENTS - continued

10. PROPERTY, PLANT AND EQUIPMENT

In 2018, the Scheme capitalised an amount of EUR730,465 (2017: EUR 105,758) in respect of Computer Software and Computer Equipment. The asset is not yet put into use. The total committed expenditure as at 31 December 2018 amounted to EUR1.2m (2017: EUR1.5m)

11. RECEIVABLES

	2018 EUR	2017 EUR
Accrued income	**170,150**	340,131
Other receivables	**7,881**	-
Total receivables	**178,031**	340,131

12. COMPENSATION CONTRIBUTION

As at 31 December 2018, the total compensation contribution required in terms of Article 23 of S.L. 371.09 amounted to EUR143,602,075 (2017: EUR141,372,082). This amount is required to be made up of cash contributions of EUR52,414,757 (2017: EUR43,825,345 and payment commitments of EUR91,187,318 (2017: EUR97,546,736). Cash contributions are allocated to the contribution fund (note 13). As at 31 December 2018 the total payments commitments were met as follows:

- Deposits made directly with the Scheme of EUR7,083,833 (2017: EUR9,060,306) included in the special contribution fund (note 15)
- Deposits of EUR7,020,320 (2017: EUR6,307,390) pledged in favour of the Scheme
- Securities of EUR77,083,165 (2017: EUR82,179,040) pledged in favour of the Scheme

The market value of the Securities as at 31 December 2018 amounted to EUR81,628,752 (2017: EUR85,587,992).

13. CONTRIBUTIONS FUND

As at 31 December, the Contributions fund represented the total cash contributions as disclosed in note 12, net of compensation payable amounting to EUR34,625,489 (2017: EUR34,780,249) (note 19).

Initial contributions made by participants until 31 December 2015, other contributions from credit institutions which are no longer part of the scheme and cash contributions in excess of the required cash contributions as at 31 December 2018 were reclassified to the other contributions fund (note 16).

14. MANAGEMENT EXPENSE CONTRIBUTION FUND

The management expenses contribution fund represents contributions from participants to meet management expenses in terms of Article 26 of S.L. 371.09. No management expense contribution was imposed in 2018. An amount of EUR227,406 (2017: EUR157,974) was allocated from the accumulated fund to the Management expense contribution fund in terms of Article 32 (4) of S.L. 371.09.

15. SPECIAL CONTRIBUTION FUND

The special contribution fund represents special contributions from participants who have elected to deposit their payment commitment directly with the scheme (note 12).

16. OTHER CONTRIBUTIONS FUND

The other contributions fund includes initial contributions made by participants until 31 December 2015 and other contributions from credit institutions which are no longer part of the scheme. In 2018, an amount representing the cash contributions in excess of the required cash contributions as at 31 December 2018 were also reclassified from the contributions fund.

NOTES TO THE FINANCIAL STATEMENTS - continued

17. OTHER RESERVES

Revaluation reserve

This reserve represents the unrealised gains or losses on the financial assets (investments) recognised in other comprehensive income.

Accumulated fund

The accumulated fund represents accumulated surpluses over the years. These are net of an amount of EUR273,806 (2017: EUR157,974) was allocated from the accumulated fund to the Management expense contribution fund in terms of Article 32 (4) of S.L. 371.09.

18. OTHER PAYABLES

	2018 EUR	2017 EUR
Accruals	**339,551**	27,293

19. COMPENSATION PAYABLE

On the 30 March 2017, the Malta Financial Services Authority ("MFSA") made a determination in terms of Article 8(1) of Legal Notice 383 of 2015 regarding the inability of a credit institution to repay deposits placed by its depositors.

On the basis of information disclosed by this credit institution to the Malta Depositor Compensation Scheme pursuant to regulation 20 of the Depositor Compensation Scheme Regulations, the Compensation payable was estimated at EUR35,222,715, out of which EUR130,800 remain unpaid. Compensation payable is disclosed net of payment commitments pledged by this credit institution which were liquidated by the Scheme amounting to EUR442,466.

20. ADDITIONAL PLEDGE REQUIREMENT

The Malta Financial Services Authority required a number of credit institutions to ensure that an amount calculated on credit institutions' covered deposits is deposited and pledged in favour of the Scheme over and above the requirements of the Regulations. The amount required to be pledged in favour of the Scheme as at 31 December 2018 amounted to EUR101,581,865 (2017: EUR103,682,524). As at 31 December 2018, the total amount pledged was EUR109,095,706 (2017: EUR97,633,194) of which EUR99,389,323 were the effective amounts pledged to the Scheme

21. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

As at year end, the Scheme's main financial assets include investments, receivables and cash held at bank. Financial liabilities consist of other payables. As at year end, there were no off-balance sheet financial assets and financial liabilities.

The main risks arising from the Scheme's financial assets and liabilities are credit risk, liquidity risk, interest rate risk and fair value risk. The Management Committee reviews and agrees policies for managing each of these risks which are summarised below.

NOTES TO THE FINANCIAL STATEMENTS - continued

21. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES - continued

Risk management policies

Credit risk

Financial assets which potentially subject the Scheme to concentrations of credit risk consist primarily of investments and cash at bank. Investments include Malta Government Stock and Treasury Bills. The Scheme's exposure to credit risk is limited to the carrying amounts of financial assets recognised.

Credit risk - continued

The credit risk relating to investments financial assets is considered to be low in view of management's policy of investing only in high quality sovereign securities which are listed on a recognised stock exchange. The Scheme's cash is placed with quality credit institutions.

Liquidity risk

Liquidity risk is limited as the Scheme has sufficient funding resources to meet its financial obligations as these arise. However, the Scheme may be required to seek substantial borrowings and extraordinary funding assistance from third party entities in the event of a claim by depositors following a bank default.

Interest rate risk

All interest-bearing financial assets have fixed interest rates. The Scheme's incoming and operating cash flows are substantially independent of changes to market interest rates. Up to the reporting date, the Scheme did not have a hedging policy with respect to interest rate risk as exposure was not deemed to be significant by the Management Committee.

Fair value risk

The Scheme is exposed to fair value risk in respect of its investments. However, such instruments are held for strategic rather that trading purposes and the Scheme's Management Committee does not consider that its exposure to fair value risk is significant.

22. CAPITAL MANAGEMENT POLICIES AND PROCEDURES

The objective of the Scheme is to provide a means of protection for depositors within the framework of the regulation. The Managements Committee, which manages and administers the Scheme, is required to work in the best interest of the Scheme and shall pursue and promote its objective.

The Scheme's capital management objectives are:

- to ensure the Scheme's ability to continue as a going-concern. For this purpose, it is required to maintain a fund or funds out of which payments shall be made to depositors and to meet such other payments or expenses as may be paid out of the fund or funds in accordance with the Regulations.

- to process claims for compensation by depositors as expeditiously as possible and to ensure that compensation is paid out without undue delay. To this end, the Scheme is required to consult with the competent authority (i.e. Malta Financial Services Authority) as to arrangements for the making of payments to depositors in terms of the Regulations.

NOTES TO THE FINANCIAL STATEMENTS – continued

22. CAPITAL MANAGEMENT POLICIES AND PROCEDURES - continued

The capital structure of the Scheme consists of a contributions fund made up of accumulated contributions paid by participants since its inception in 2003. In terms of the Regulations, participants are required to maintain a fund "on call" either as a capital reserve or a contingent liability.

The Committee is committed to strengthen the Scheme's capital base in line with European and international best practices. To this end, it will continue to advise the competent authority on methods related to the strengthening of the financing of the Scheme.