

Investor Compensation Company DAC publishes its 2017 Annual Report

Introduction

The principal objective of the Investor Compensation Company DAC ["ICCL"] is to pay compensation to eligible investors when an investment firm fails and is unable to return client money and/or investment instruments. To support that objective, the ICCL collects annual levies from investment firms, retail intermediaries and accountants in order to build the reserves from which compensation can be paid. The ICCL is not funded by the State.

Results for the year

The ICCL has recorded a surplus for the year to 31 July 2017 of €4.8 million, representing an increase of €72,000 on the previous year. Total levies received from investment firms participating in the Compensation Scheme were €6.4 million, which was unchanged for the previous year, signifying a collection rate of 99.9 per cent from contributing firms. This involved €5 million from large investment firms (such as banks and stockbrokers) that contribute to an earmarked fund (Fund A) and €1.4 million for smaller investment firms including insurance brokers, retail intermediaries and accountants that are members of a separate fund - Fund B

At the financial year-end, the accumulated reserves of the ICCL stood at €52.8 million. This comprised of Fund A reserves of €28.6 million and Fund B reserves of €24.2 million. In both instances, the reserves are net of all estimated liabilities arising from ongoing compensation cases which have been fully provided for. These resources will be built on further in accordance with the Company's latest three year funding cycle which runs to mid-2019.

Funding

The ICCL is obliged to maintain sufficient resources out of which compensation can be paid to clients of failed investment firms for losses suffered. The primary source of funds are the cash reserves of the Company, which comprise accumulated levies collected from authorised investment firms. Those reserve levels have been replenished steadily in recent years following provisions made for projected aggregate compensation payable of €19.7 million relating to the ongoing Custom House Capital case. The amount of reserves available for future cases currently stands at €52.8 million as set out above. This is in line with targets outlined in the current three-year funding programme with Fund A and Fund B on course to grow to €35 million and €25 million respectively during 2019.

The total contributor base stands at 3,500, of which 95 per cent are Fund B firms. The latter includes more than 450 member firms of Chartered Accountants Ireland authorised to conduct investment business activities that became affiliated to the Scheme on 1 August 2017.

The reserves are augmented by a bespoke Excess of Loss insurance policy in place which offers cover of €100 million in respect of Fund A failures and €10 million for Fund B failures in circumstances where losses exceed a threshold of €15 million. When taken together, the ICCL's reserves and the insurance policy currently provides funding capacity of the order of €129 million for Fund A firms and of €34 million for Fund B firms without the need to impose supplementary levies on contributing investment firms.

Custom House Capital Limited (in Liquidation) [“CHC”] - Fund A Firm

CHC is the largest known failure of an investment firm since the establishment of the ICCL with total investor losses estimated at €56 million and compensatable losses of €20 million, which has been fully provided for in the ICCL's accounts.

On 21st October 2011, the High Court placed CHC into liquidation and the Court appointed Mr Kieran Wallace of KPMG as Liquidator and Administrator to the firm, in accordance with section 33A of the Investor Compensation Act, 1998 (the Act). Mr Wallace, in his capacity as Administrator, has estimated that the ICCL may be required to pay compensation, on foot of claims from eligible investors of CHC, of up to €19.7 million. The impact that this would have on the ICCL's reserves has been fully recognised in prior year financial accounts.

The role of the Administrator to CHC, is to determine the extent to which clients of the firm had suffered losses. The Administrator achieves this by leveraging on his work as Court-appointed Liquidator whereby he reconciles the position of each client of the firm, through an examination of the books and records of the firm. He is then required to certify the individual losses of eligible investors to the ICCL. Once an investor's claim has been certified by the Administrator, the ICCL will make a compensation payment to that investor in accordance with the Act.

The ICCL has received nearly 2,000 claims for compensation from clients of the firm. Although the liquidation of CHC is now nearing the end of its sixth year, only 567 claims - one quarter of the all claims received - have been dealt with by the Administrator. This has resulted in compensation of €7.4 million being paid to date by the ICCL to clients of the firm. During the past year, Mr Wallace certified 20 claims resulting in compensation paid of €387,000. A large body of work has still to be completed by the Liquidator including the potential recovery and distribution of significant amounts of client monies that were the subject of misappropriation and unauthorised diversion by CHC into a number of property-related investments. This in turn is likely to delay confirmation of the extent of compensatable losses of the investors concerned and the related certification of their claims.

The Liquidator has proposed a timetable for the completion of his remaining work, principally the reconciliation and distribution of property funds, the recovery and distribution of misappropriated funds and the reconciliation and transfer of pooled asset accounts. It is envisaged that this will extend to at least mid-2019, however a timeline for the recovery of all misappropriated monies remains uncertain due to the complexities involved including legal and other impediments, such as the sale of some properties into which these monies had been diverted. He has indicated that he intends to complete certification of compensation claims contemporaneously with the reconciliation and distribution of remaining client assets. However in some cases, it may be necessary to await the outcome of future recoveries of misappropriated funds before certification can be completed and compensation paid. The ICCL has continued to seek the acceleration of the claims certification process.

The intricacies of the CHC case, which involved the deliberate and organised concealment of the large scale embezzlement of investors' funds coupled with the maintenance of false accounting records and the issuance to clients of incorrect portfolio statements, have undoubtedly contributed to the protracted timespan of the liquidation and the associated claims certification process, which is highly unsatisfactory for the many CHC clients affected.

It is the view of the ICCL that some measures need to be implemented to ensure a more speedy resolution of such cases to accord with the spirit of investor compensation legislation, thereby alleviating the position of investors who have the misfortune to be involved. The ICCL has made a number of recommendations to the Department of Finance and to the Central Bank aimed at addressing the factors causing such delays. In the absence of any action, investors are likely to experience similar delays in a future failure, despite the enhanced Client

Asset protections that have been introduced by the Central Bank as regulatory authority in the intervening period.

Asset Management Trust Limited (AMT) – Fund B Firm

The AMT case dates from early 2016 when the Central Bank made a determination under the Act in respect of this former investment firm. This followed a lengthy investigation by the Bank into the firm, culminating in allegations of the overcharging of portfolio management fees and resulting claims for compensation from a small number of clients. The majority of these claims have now been certified by the Administrator, Mr Des Ritchie. It is expected that the total compensation payable by the ICCL will amount to around €77,000 with the process being concluded by the end of this year.

Rush Credit Union Limited (RCU) – Fund B Firm

The High Court appointed joint liquidators to RCU in November 2016. RCU was an investment firm and member of the Compensation Scheme. The ICCL advised all RCU members known to have transacted investment business through the credit union to make contact in the event that they considered that they have suffered a compensatable loss. No claims for compensation were submitted.

Chairperson's comments

Speaking on the publication of the Annual Report, the Chairperson of the ICCL, Mr Jim Bardon, said:

"I am pleased to report that the Company has seen another year when its reserves have strengthened significantly following an excellent levy collection outturn. Our available resources are now approaching the medium term target of €60 million. When these are taken in conjunction with existing insurance arrangements, the ICCL is well placed to discharge potential compensation liabilities that would arise from the failure of any large investment firm.

Since the financial year-end, the number of firms covered by the Compensation Scheme has increased following the accession of member firms of Chartered Accountants Ireland that are authorised to provide investment services.

Progress in the certification of claims in the largest ongoing case, Custom House Capital (CHC), has continued to be slow. However, in his latest report to the High Court, the Liquidator has provided an outline timetable for the completion of the outstanding work in the liquidation, principally the recovery and distribution of misappropriated monies, and the reconciliation and distribution of pooled client assets, with the major component of these tasks foreseen to be concluded during the next eighteen months. The Liquidator has also signalled that certification of the related compensation claims will be dealt with contemporaneously. I can assure the CHC investors involved that the Company remains committed to seeking the acceleration of the claims process and that on receipt of certifications, the ICCL will arrange for payment of compensation promptly.

While CHC was a complex case involving systematic fraud on a large scale, the nature of which has impacted on the timeframe for the certification of claims, it is possible that similar delays could arise following a future failure of an investment firm. The ICCL remains of the view that measures are needed to address issues that impede a more speedy resolution of such cases. "

The ICCL Annual Report for 2017 is now available online at www.investorcompensation.ie