THE INVESTOR COMPENSATION COMPANY LIMITED

ARRANGEMENTS FOR FUNDING OF THE INVESTOR COMPENSATION SCHEME OPERATED BY ICCL

MAY 2004

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1. Introduction

Following public consultations in the course of 2003 as part of a review of the Investor Compensation Scheme, the Investor Compensation Company Limited (the "ICCL"), with the support of the Irish Financial Services Regulatory Authority ("IFSRA"), has now decided on certain revisions to its current funding arrangements as set out in its booklet of November 2001.

The ICCL is making these revisions in furtherance of its principal statutory objective to maintain a financially sound Scheme which provides statutory levels of compensation to eligible investors of failed authorised investment firms. It is furthermore doing so in ways which seek progressively to improve the actual and perceived equity of the contribution burden on contributor firms.

In arriving at its decisions on these changes, the Board of the ICCL, on this occasion as in the past, took particular account of the views expressed in the consultation process. However, it has had to steer a course through sometimes conflicting views on particular aspects. The Board, which is fortunate in having broad industry representation, has endeavoured, in so far as possible, to achieve a timely, balanced and workable compromise on such issues.

2. Legislative Background

The legislative background to the Scheme is set out in detail in Appendix 1.

The Investor Compensation Act, 1998 ("Act") provides that authorised investment firms must become members of an investor compensation scheme[1] and contribute to its funding. Following industry consultation, the first detailed funding arrangements were published in 1999. A subsequent consultation process was carried out in 2001 which resulted in certain revisions to the classifications of contributors and to rates of contribution.

The Act also provides that compensation shall be paid to eligible investors (as defined in the Act) to the extent of 90% of an investor's net loss, as defined in the Act, or €20,000, whichever is the lesser. The right of eligible investors to claim compensation is triggered by

(a) a determination of the supervisory authority that an investment firm is unable, and has no reasonably foreseeable opportunity of being able, to meet its obligations arising from claims by clients, or

(b) a court ruling which has the effect that clients of the firm are precluded for the time being from pursuing claims against the firm in relation to money or investment instruments owed to or belonging to them in connection with the provision of investment business services by the investment firm.

[1] Such scheme will either be one operated by the Investor Compensation Company Limited or a scheme operated by an approved professional body for certified persons which is approved by the IFSRA under the Act.

IFSRA is the supervisory authority for the purpose of the Act. IFSRA is a constituent part of the newly restructured Central Bank and Financial Services Authority of Ireland ("CBFSAI"), which was established following the commencement of the Central Bank and Financial Services of Ireland Act, 2003 on 1 May 2003.

The ICCL, having consulted with IFSRA, shall set the contributions to be paid by authorised investment firms to the fund(s) maintained by the ICCL and the appropriate size of the fund(s). The ICCL is required to "endeavour to ensure" that it is in a position to meet any reasonably foreseeable obligation under the Act and that it maintains a sufficient balance in the funds to enable it to meet such obligations. The ICCL is also obliged to have regard to the amount standing to the credit of the funds it maintains and the funding capacity of those authorised investment firms which are obliged to make contributions to the funds.

The Act also provides that the costs of administration and management of the ICCL shall be defrayed from the ICCL's resources, including the contributions paid to the funds maintained by the ICCL.

The ICCL's obligations to eligible clients of authorised investment firms under the Act date from 1 August 1998.

3. Funding Year

Currently, the ICCL's funding year is 1 August to 31 July with the sixth funding year ending on 31 July 2004. The ICCL's funding year will continue to run from 1 August to 31 July. However, as the ICCL is currently in discussions with IFSRA to develop a co-ordinated billing and collections system for both the IFSRA levy and the ICCL contribution, the ICCL's funding year may change in the future.

4. Description of Funds and Contributor Categories

At inception, the ICCL, following consultation with industry, established two funds:

Fund A

Fund A was established to meet claims from eligible investors of:

a) Investment Firms authorised under Section 10 of the Investment Intermediaries Act, 1995 ("IIA") that are not exempt under Section 2(5) of the Investor Compensation Act, 1998. Multi-Agency Intermediaries (MAIs), authorised under Section 10 of the IIA since 1 December 1998 are excluded from this categorisation, but are dealt with under Fund B;

b) Investment Firms authorised under Section 10 of the IIA and designated as Authorised Cash Handlers by IFSRA. Under the Insurance Act, 2000, IFSRA is responsible for the regulation of insurance intermediaries and introduced three categories of investment business firm into which insurance intermediaries will fall i.e. Multi-Agency Intermediaries ("MAIs"), Authorised Advisors and Authorised Cash Handlers. (MAIs and Authorised Advisors are required to contribute to Fund B);

c) Firms, including Authorised Cash Handlers, falling under Section 13 of the IIA (awaiting designation as Section 10 firms);
d) Stockbrokers;
e) Credit Institutions that provide investment services;
f) Certified persons who provide investment business services which include or comprise investment business services other than those provided by MAIs or Authorised Advisors (unless the approved professional body of which the certified person is a member has been granted approval under Section 25 of the Act for the establishment of a compensation scheme for a category of certified person to which the person belongs).

Fund B

Fund B was established to meet the claims of eligible investors of firms defined in Section 36 of the Investor Compensation Act, 1998, namely:

a) Authorised Advisors;
b) Restricted Activity Investment Product Intermediaries ("RAIPIs"), including deposit agents. This includes RAIPIs authorised under Section 10 of the IIA since 1 December 1998;
c) Life Assurance Intermediaries;
d) Composite Insurance Intermediaries;
e) Non-life Insurance Intermediaries;
f) Tied Insurance Agents which are not RAIPIs or Authorised Advisors, as defined in the Insurance Act, 2000 (unless the undertaking to which they are tied takes full and unconditional responsibility for all their activities, even those activities which may exceed the extent of their authorisation by the institution concerned[2]), and
g) Certified Persons who do not provide investment business services of any kind other than provided by those firms listed at (a) to (f) above (unless the approved professional body of which the certified person is a member has been granted approval under Section 25 of the Act for the establishment of a compensation scheme for a category of certified person to which the person belongs).

5. Responsibilities of Product Producers

In the event of a default by a restricted intermediary, which is not a member of a compensation scheme operated by an approved professional body and approved by IFSRA, and where the ICCL pays compensation to the eligible investors of that intermediary, a product producer from which the restricted intermediary held a valid written appointment is obliged to make payment to the ICCL. This payment is in respect of the same proportion of the compensatable loss of an eligible investor of the restricted intermediary as "receipted monies" as defined in the Act, entrusted by that investor for transmission to the product producer, bears to that investor's net loss. Essentially "receipted monies" represents the value of client monies or investment instruments entrusted by an eligible investor to a restricted intermediary for transmission to an identifiable product producer and forming part of that client's net loss.

[2] The institution to which an agent is tied retains responsibility for investor compensation in respect of his/her tied agency activities.

The Central Bank and Financial Services Authority of Ireland Bill, 2003 amends the Investor Compensation Act, 1998, so as to extend the above obligations of product producers to all appointed intermediaries who hold letters of appointment as was applied generally prior to the introduction of the Insurance Act, 2000.

6. Section 25 Option for Certified Bodies

Certain approved professional bodies may apply to IFSRA, under Section 25 of the Act, for approval of proposals for the establishment of an investor compensation scheme for a specified category or categories of certified person. Certified persons are obliged to participate in the scheme operated by the ICCL, until such time as an investor compensation scheme is approved under Section 25 in respect of their operation.

7. Funding Targets and Projections

Background

When the Scheme was established an overall target funding level of €10.16 million, was set, to be achieved by the end of a five year period, which was to be divided equally between Fund A and Fund B. Annual contributions for Fund A consisted of a combination of a flat rate contribution and a variable rate contribution based upon the number of eligible clients. Annual contributions for Fund B were based on two flat rates depending upon the type of business undertaken. Provision was also made for additional "top up" funding in the event that any claim or claims on either fund required it. Following the 2001 consultation process, in order to introduce an element of progressivity, rates of contributions by certain Fund B contributors were related to income levels.

Impact of Claims on Funding Targets

Since the establishment of the Investor Compensation Scheme there have been two significant determinations made under the Act resulting in claims for compensation being made. Both relate to Stockbrokers covered by Fund A. There was one determination made under the Act in relation to Fund B resulting in a relatively modest amount of money (€20,000) being paid.

The first claim on Fund A, in February 1999, arose out of the insolvency of Money Markets International Stockbrokers Limited ("MMI") and has involved compensation payments, to the end of July 2003, of €745,273 out of Fund A. Total compensation payments could ultimately be as high as €800,000. The costs and expenses of the Administrator associated with this case are estimated to amount to a further €385,000 and will be payable by the ICCL.

The second claim on Fund A arose out of the insolvency of W&R Morrogh Stockbrokers ("Morrogh") and is, as yet, not fully resolved. In its financial statements to 31 July 2003, the ICCL made a provision of €7.7 million against claims, costs and expenses arising from the Morrogh case. To date, €2.8 million in compensation has been certified by the Administrator and paid out by the ICCL.

Top-Up of Fund A

In the light of the substantial claim arising from the insolvency of Morrogh, the Board of the ICCL implemented a scheme for "top up" funding for Fund A to ensure that, in so far as possible, it would be in a position to meet its obligations to pay compensation to claimants in accordance with the Act. Fund A firms with eligible clients were required to contribute to the Morrogh top up. Stockbrokers contributed 50 per cent of the requirement with the other Fund A firms contributing the balance. It was determined that the "top up" payments would be phased over three years. Thus, in addition to the normal annual payments, additional "top up" payments to Fund A were invoiced in July 2002, April 2003 and April 2004. Notwithstanding the top up, Fund A reserves stood at just under €500,000 at 31 July 2003.

General Adequacy of Funds

The recent claims history experienced by the Scheme has demonstrated that funds can be quickly absorbed when claims arise (both in payment of compensation and in meeting costs associated with the claims). Therefore, the Board of the ICCL continues to believe that neither Fund A nor Fund B could be regarded as adequately funded at present. As indicated in the August 2003 Consultation Paper, it is felt that the continued payment of annual contributions is the best way of building up the levels of funds available. The Board has agreed revised rates and bands of contribution which will apply with effect from the funding year commencing 1 August 2004. These are set out in section 8 and appendices 2 and 3. Projected annual contribution rates to Fund A and Fund B under the revised terms are as shown in column 1 of the following tables. If no failures, giving rise to compensation payouts, arise in the periods set out in the tables, the reserves are projected to be as shown in column 3 of these tables.

(i) Fund A

Year ending 31 July	COLUMN 1 Annual Contributions € million	COLUMN 2 Top-up Contributions € million	COLUMN 3 Fund Reserve € million
2002 - Actual	1.84	1.73	(0.14)*
2003 - Actual	1.81	1.65	0.46
2004 -Projection	1.76	1.65	3.50
2005 -Projection	1.94	-	5.04
2006 -Projection	2.13	-	6.77
2007 -Projection	2.34	-	8.71

* Note that because these calculations include provisions for claims not yet paid out, this is not a cash deficit

(ii) Fund B

Year ending 31 July	COLUMN 1 Annual Contributions € million	COLUMN 2 Top-up Contributions € million	COLUMN 3 Fund Reserve € million
2002 - Actual	1.72	-	3.95
2003 - Actual	1.76	-	5.52
2004 -Projection	1.69	-	6.98
2005 -Projection	1.60	-	8.28
2006 -Projection	1.60	-	9.58
2007 -Projection	1.60	-	10.88

8. Contributions by Participating Firms

Fund A

Rates of Contribution

The new annual contribution rates for Fund A firms for the year 1 August 2004 to 31 July 2005 are set out in Appendix 2. The rates shown in Appendix 2 will increase by 10 per cent in each of the financial years ending 31st July 2006 and 2007, following which contributions will be increased by an inflation factor.

Basis of Contribution

1. Fixed rate
All authorised Fund A firms are liable to pay a fixed rate of contribution. Reduced flat rates apply to firms with no, or fewer than 2,500, eligible clients.

2. Variable rate
All firms with eligible clients are also liable to pay a variable rate of contribution which is determined by the band of eligible client numbers into which they fall. The number of bands has been expanded from seven to eight. The Board continues to believe that the use of eligible clients as a proxy for the potential level of exposure of participants remains the best method of allocating contributions for Fund A.

3. Marginal relief
With effect from the start of the financial year commencing 1st August 2004, marginal relief will be introduced for participants who fall into the next highest band in circumstances where the number of their eligible clients that cause them to fall into that higher band is less than 10 per cent of the total number of eligible clients specified for the relevant band. Firms that fall within the marginal relief area of a band will not have to pay the higher contribution for the first year. However, firms that continue within the marginal relief area of a band in subsequent years must pay the higher contribution for subsequent years.

Such marginal relief must be availed of in the year in which it first arises. Firms may avail of marginal relief on more than one occasion.

These contribution rates are applicable unless unforeseen circumstances arise.

Determination of Appropriate Variable Rate Band for Fund A Firms

In determining which variable rate band applies to them, and, consequently, which contribution rate is payable by them, participating firms should make an annual assessment of the numbers of eligible clients, including execution-only clients, with whom they have done business in their previous financial year.

Guidelines for the Calculation of Eligible Client Numbers when Assessing the Appropriate Contribution Rate

The ICCL is aware that some participants in Fund A have encountered difficulties in determining which of their customers fall within the definition of eligible clients.

The ICCL has updated its guidelines for the assessment of eligible client numbers and these are available on the 'Funding the Scheme' section of the ICCL's website in the form of 'Questions & Answers' (www.investorcompensation.ie). These guidelines are also included in Appendix 4 of this document.

Verification of Eligible Client Numbers

All Fund A firms will be required to confirm their number of eligible clients, other than excluded investors, when contributing each year. The ICCL advises IFSRA of the level of eligible clients as confirmed by Fund A firms. These figures may be subject to verification by IFSRA as part of its ongoing supervisory process.

Subsequent to the issuing of the November 2001 Funding Arrangements document, the ICCL has engaged with a number of participants to assist them in reaching an accurate assessment of their eligible client numbers. In this regard, a review of stockbroking clients, carried out by IFSRA in 2001, raised further issues with regard to the consistency of treatment across the industry on the assessment of eligible client numbers in relation to "Bed and Breakfast" clients, Employee Share Option Schemes, Pension Funds, Eircom clients, solicitors and accountants and clients referred by banks. The ICCL has further clarified how these matters should be assessed for the purposes of calculating eligible client numbers. A number of specific queries, raised by contributors in response to the ICCL's Consultation Paper, are being addressed.

The ICCL will continue to be available to give guidance to participants where there is any question of doubt or uncertainty.[3]

[3] There are certain firms that are authorised under Section 10 of the Act and which are required to contribute to the Scheme even though they have no eligible clients at present – although they could have such clients in the future. The nature of the authorisation of such firms brings them within the Directive and the Act. As a result of this, the ICCL has devised arrangements where such firms pay a flat rate fee. Such firms are not subject to any "top up" arrangements unless the failure arises from a firm reporting that it has no eligible clients.

Fund B

Rates of Contribution

The new annual contribution rates for authorised Fund B firms are set out in Appendix 3.

These contribution rates are effective for each of the financial years commencing 1st August 2004, 2005 and 2006, following which contributions will be increased by an inflation factor. However, as noted below, any changes which IFSRA may introduce in the future in relation to the authorisation categories for intermediaries may have implications for the way in which the ICCL treats these entities for contribution purposes.

The flat contribution rate for non-life intermediaries has been removed and all firms will now contribute on the basis of the turnover bands into which they fall.

These contribution rates are applicable unless unforeseen circumstances arise.

Basis of Contribution

The Board of the ICCL believes that the continued building up of reserves in Fund B must be its objective for the next 5 year period.

The existing contribution categories for Fund B intermediaries are Authorised Advisors, Multi Agency Intermediaries which are RAIPIs ("MAI RAIPIs"), Tied Agents and Multi Agency Intermediaries that are not RAIPIs ("MAI non-RAIPIs"). These contribution categories derive directly from the IFSRA authorisations which are notified to the ICCL. Any changes which IFSRA may introduce in the future in relation to the authorisation categories for intermediaries may have implications for the way in which the ICCL treats these entities for contribution purposes.

The total income, from investment business and insurance business, determines the level at which each firm contributes. The previous five income bands have been expanded to eight income bands in order to spread the obligation to make contributions on a more equitable basis.

9. Invoicing of Annual Contributions

Invoices for annual contributions will be issued in August each year i.e. the first month of the ICCL's financial year. Invoices issued by the ICCL are payable within 35 days. Contributors that fail to contribute in a timely manner will be reported to IFSRA, under the Act, for failure to comply with their obligations. Failure to pay on time will result in the firm being assessed for interest on the outstanding amounts. Under Section 21(4) of the Act, an investment firm which does not comply with its obligations to pay its contribution to the Funds maintained by the ICCL may be liable to pay interest of 1.25 per cent per month to the ICCL on all or any part of a contribution which has not been paid by the specified date(s). Interest is calculated from the date upon which the contribution becomes due.

The ICCL is currently in discussions with IFSRA in relation to the development of a co-ordinated billing and collections system for both the IFSRA levy and the ICCL contribution. This may give rise to some changes to the way in which ICCL invoices are currently issued, and if so, contributors will be notified in a timely manner.

10. Annual Adjustment for Inflation

As indicated under item 8 of this document, annual contribution rates beyond the year 2007 will be adjusted for inflation. This is to take account of the effects of inflationary increases on claims of under €20,000 and on all costs arising for the Scheme.

11. Contributions by Newly Authorised Firms

With effect from 1st August 2004, investment firms, which are authorised during the ICCL's funding year and subsequent to the ICCL's annual billing process (which takes place in August each year), will be required to pay the annual contribution in full.

As eligible client numbers or turnover figures will not be available at the time of raising the first invoice, the contribution rate for the first year will be agreed on a case by case basis with each firm.

12. Contributions by Firms whose Authorisation changes during the Funding Year

With effect from 1st August 2004, there will be no adjustment in contributions to reflect any changes in authorisation (including revocation) which occur during the funding year. The new rate of contribution will apply from the following funding year on the basis of the firm's authorisation status at that time.

13. Publication of Contributors

The ICCL's website contains a list of firms who contributed to the Scheme in the year ended 31 July 2003. The ICCL will update the list of contributors annually after publication of its Annual Report. It should be noted that this is a static list of contributors to the scheme in a particular year and is not to be viewed as confirmation that a firm is currently authorised.

The ICCL's database of contributors is updated on the basis of information supplied to the ICCL by IFSRA and certain other bodies (e.g. insurance companies). It is not possible for the ICCL's database to be 'real-time' due to the fact that the lists, from which the ICCL's database is compiled, are maintained separately by these other bodies.

IFSRA expect that the Register of Regulated Firms will be available on its website in the near future. In the meantime, the authorisation status of a regulated firm may be checked by contacting IFSRA by email at sesregisters@ifsra.ie or by contacting the lo-call telephone line: 1890-200-469.

14. Contribution Obligation on Investment Firms

Section 21 of the Act provides that authorised investment firms (excluding certified persons in respect of whom an investor compensation scheme has been approved under Section 25) shall pay to the ICCL such contribution to the fund(s) as the ICCL may specify from time to time.

As set out previously, the Act also provides that, where an investment firm does not comply with its obligations under Section 21, the firm shall be liable to pay interest to the ICCL on all or any part of a contribution which has not been paid by the date or dates specified by the ICCL at a rate of 1.25% per month (or part of a month) on and from the date on which the contribution becomes due or such other amount of interest as may be prescribed by the Minister for Finance.

Other consequences of failure by investment firms to comply with their obligations under Section 21 are set out in Sections 27 and 28 of the Act. Under the Act, IFSRA may issue a direction requiring the firm to comply with its obligations and failure to comply with this direction could result in the firm being prohibited from engaging in investment or insurance business.

15. Handling of Claims on Funds

The ICCL proposes, without prejudice, that in the event of a determination or ruling, as described in Appendix 1, affecting an authorised investment firm, claims would be handled through some or all of the following methods:

- Payments would be made out of Fund A or Fund B, as appropriate.
- Under Section 19 of the Act, interfund borrowing is permitted as stipulated. The Act does not prescribe a limit or a rate of interest which shall apply to such borrowings. The Board has decided that 'no margin' rates should apply and, as a guideline, borrowing should be up to a maximum of one third of the Funds in total, with a repayment schedule of not more than three years. As prescribed by Section 19 (7) of the Act, the ICCL must consult with IFSRA regarding any interfund borrowing.
- Utilisation may be made of borrowing facilities arranged under the ICCL's statutory borrowing powers. As prescribed by Section 13 (1) of the Act, the IFSRA must approve any borrowing.

16. Top-Up Funding in the event of a Major Default

Contributors have expressed a wish that the Scheme's ability to meet its payment obligations be funded mainly by annual contributions, supplemented as appropriate by borrowings and that the liability burden be smoothed over time. This is a particular concern in the context of the small number of firms with eligible clients in Fund A. Contributors expressed a wish to avoid open ended special top-up levies in the event of significant claims arising.

The Board recognises these legitimate concerns of contributors and its continued building of the Scheme's reserves is in response to this concern.

The ICCL is currently in discussion with IFSRA, the CBFSAI and the Department of Finance regarding satisfactory, last-resort funding arrangements. If these can be put in place, the ICCL will seek to introduce a cap on the amount that may be raised in any one year in the event of a top-up call on Fund A contributors. Such a cap would be equal to twice the annual contribution rate.

Pending the implementation of such a cap, the existing arrangements will continue to apply. In the event of top-up funding:

- Should the default be attributable to a participating firm in Fund A, additional funding will be obtained through a special levy and/or increases in the annual fees payable by participating firms in Fund A with eligible clients pro-rata to their annual contribution for the previous year.

- Should the default be attributable to a participating firm in Fund A, which had declared itself to have no eligible clients, additional funding will be obtained through a special levy and/or increases in the annual fees payable by all participating firms in Fund A, including firms with no eligible clients, pro-rata to their annual contribution for the previous year.

- Should the default be attributable to a participating firm in Fund B, additional funding will be obtained through a special levy and/or increases in the annual fees payable by participating firms in Fund B pro rata to their annual contribution for the previous year.

Given its statutory obligations, the ICCL reserves the right to make alternative arrangements to those proposed above should the circumstances warrant it. Contributors will be consulted should such circumstances arise.

17. Procedures for making Compensation Payments to Eligible Investors

The procedures to be followed in relation to the payment of compensation are laid down in the Act. The following is a broad summary:

After IFSRA has made a determination, or a court has made a ruling as described above, the ICCL is required to inform clients of the investment firm concerned of the determination or ruling and invite applications for payment by a date which shall not be less than five months from the date of the determination or ruling.

The ICCL is also required to publish notices to the above effect in any of the newspapers circulating in the State or elsewhere or in Iris Oifigiuil.

Subsequent to a determination, IFSRA may appoint an administrator to the investment firm, or, in the case of a liquidation or bankruptcy, the liquidator or official assignee appointed by the court will be the administrator. The administrator shall give to the ICCL and to IFSRA, as soon as is practicable, the names of eligible investors and a statement of the net loss of each such client.

The ICCL is then required to make payment to those eligible investors. This has to be done as soon as practicable and, at the latest, within three months.

A client may appeal to the Courts against any refusal to make a payment or against the amount of any payment made.

With regard to the treatment of late claims, (claims which are received by the ICCL after the five month deadline), the ICCL operates within the provisions of the Directive and the Act.

Article 9 of the Directive states:
"The fact that that[4] period has expired may not, however, be invoked by the scheme to deny cover to an investor who has been unable to assert his right to compensation in time."

Section 32(2) of the Investor Compensation Act, 1998 states:
"Where the supervisory authority is satisfied that an investor was unable for good reason to make an application for a payment under Section 34 within the period of time stipulated by the Company or compensation scheme, the supervisory authority shall direct the Company or compensation scheme to treat the application as if it were made within the period of time stipulated."

18. Subrogation

Under Section 35 of the Act, where the ICCL has paid compensation to a claimant, the ICCL shall be subrogated to the rights of that claimant in the liquidation proceedings for the amount of the compensation paid. This means that the ICCL steps into the shoes of the claimant in the liquidation proceedings and after compensating the claimant, awaits the payment of a dividend, if any, from the liquidation.

The Board of the ICCL will take a balanced approach bearing in mind the interests of claimants and contributors when assessing whether the ICCL will take any action to realise value under its subrogated position.

The Investor Compensation Company Limited
May 2004

[4] i.e. the period fixed during which investors shall be required to submit their claims

APPENDIX 1

LEGISLATIVE BACKGROUND [5]

In March 1997 the European Council enacted a directive in relation to the establishment of investor compensation schemes in Member States. This directive, Council Directive 97/9/EC, is known as the Investor Compensation Scheme Directive (the "Directive") and was seen as an integral part of the framework for the establishment of a single market in financial services.

The Directive had its genesis in another key directive, Council Directive 93/22/EC on investment services in the securities field, known as the Investment Services Directive. The Investment Services Directive laid down certain regulatory and prudential rules governing investment firms throughout the EU. These rules were aimed at protecting investors' money and securities. The Investment Services Directive did not, however, offer any protection to investors in circumstances where fraud or insolvency resulted in the inability of an investment firm to return securities or money to investors. The purpose of the Investor Compensation Directive is to provide a minimum level of protection for investors in these circumstances.

The Investor Compensation Directive applies to all investment firms (including Credit Institutions authorised to provide investment services) and is modelled on Council Directive 94/19/EU, known as the Deposit Guarantee Scheme Directive. The latter directive aims to give depositors a minimum level of compensation where a Credit Institution becomes insolvent.

The Investor Compensation Directive lays down certain basic requirements for investor compensation schemes in order to provide a harmonised minimum level of investor protection across the community. It is left to each individual Member State to implement an appropriate scheme and it is also left to each Member State to determine the most appropriate way of organising and financing such schemes.

Thus, whilst all current Member States have implemented the Directive, the manner in which the Directive has been interpreted and applied varies quite considerably.

In Ireland, the Directive was given effect on 1st August 1998 through the introduction of the Investor Compensation Act, 1998. Under the Act, the ICCL was established as a company limited by guarantee. The Directors are nominated by such bodies prescribed by the Minister for Finance as appear to represent the financial services industry or the interests of clients of investment firms. The Governor of the CBFSAI nominates and appoints the chairperson and the deputy chairperson of the Board.

A number of sections, within the Investor Compensation Act, 1998, have been amended by the Central Bank and Financial Services Authority of Ireland Act, 2003.

[5] This is not a legal interpretation of the Act and other legislation referred to in this document.

APPENDIX 2

FUND A

ANNUAL CONTRIBUTION RATES [6]

Firms with fewer than 2,500 eligible clients

Band	Number of eligible clients	Flat Rate €	Variable Rate €	Total Rate €
0	Zero	2,930	0	2,930
A	1 - 9	4,180	420	4,600
B	10 - 499	6,300	1,050	7,350
C	500 - 2,499	9,100	5,900	15,000

Firms with 2,500 or more eligible clients

Band	Number of eligible clients	Flat Rate €	Variable Rate €	Total Rate €
D	2,500 - 4,999	10,500	21,000	31,500
E	5,000 – 24,999	10,500	39,700	50,200
F	25,000 – 49,999	10,500	42,100	52,600
G	over 50,000	10,500	73,600	84,100

[6] With effect from the start of the financial year commencing 1st August 2004, marginal relief will be introduced for participants who fall into the next highest band in circumstances where the number of their eligible clients that cause them to fall into that higher band is less than 10 per cent of the total number of eligible clients specified for the relevant band.

Firms that fall within the marginal relief area of a band will not have to pay the higher contribution for the first year. However, firms that continue within the marginal relief area of a band in subsequent years must pay the higher contribution for subsequent years.

Such marginal relief must be availed of in the year in which it first arises. Firms may avail of marginal relief on more than one occasion.

APPENDIX 3

FUND B

ANNUAL CONTRIBUTION RATES

Authorised Advisors and Multi-Agency Intermediaries (non-RAIPIs)

Level	Income band €	Rate €
1	Up to €75,000	550
2	€75,001-€150,000	700
3	€150,001-€700,000	950
4	€700,001-€1.5m	1,200
5	€1,500,001-€3m	2,450
6	€3,000,001-€6m	3,150
7	€6,000,001-€15m	4,450
8	Over €15m	5,950

Multi-Agency Intermediaries (RAIPIs) and Tied Agents [7]

Level	Income band €	Rate €
1	Up to €75,000	300
2	€75,001-€150,000	375
3	€150,001-€700,000	525
4	€700,001-€1.5m	725
5	€1,500,001-€3m	1,475
6	€3,000,001-€6m	2,075
7	€6,000,001-€15m	3,175
8	Over €15m	3,775

The above rates also apply to Certified persons who will be required to contribute on the basis of their authorisation from the relevant Approved Professional Body.

[7] Tied Agents that are not Authorised Advisors or Multi-Agency Intermediaries and are not investment business firms regulated by IFSRA

APPENDIX 4

THE ASSESSMENT OF 'ELIGIBLE CLIENT' NUMBERS: QUESTIONS & ANSWERS

The variable rate contribution for firms in Fund A has, from the beginning, been based on broad bands to minimise the need for detailed logging and verification of eligible client numbers.

The following guidelines and answers to frequently asked questions are intended to clarify certain issues in respect of which clarification has been requested by participating firms. These guidelines may be varied or added to in the future, as the ICCL considers necessary or desirable.

The following fundamental principles should be used when assessing if a client should be counted as "an eligible client":

A. *the assessment should be done annually*
B. *the 'period of assessment' should be the firm's own financial year which ends prior to the ICCL's funding year (which currently runs from 1 August to 31 July each year) i.e. the firm's previous financial year*
C. *the firm should count all clients who at any stage throughout the firm's financial year met the definition of eligible investor*[8] *under Article 2 of the Investor Compensation Act, 1998 (the "Act"). This will include execution-only clients.*

The answers to the frequently asked questions outlined below should be of further assistance to firms in determining if clients of the firm should be counted as "eligible clients" for the purposes of calculating the appropriate annual contribution to the ICCL. The ICCL will continue to be available to give guidance to participants where there is any question of doubt or uncertainty

[8] In effect, the ICCL's definition of "eligible client" *is a person, not being an excluded investor, who has entrusted money or investment instruments to an investment firm in connection with the provision of an investment business service by the investment firm.*

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1. Should execution-only clients be included?
   YES

2. What is the timeframe for including clients?
   You should include all clients, who at any stage throughout the firm's financial year met the definition of eligible investor under the Act. The relevant firm's financial year is the financial year which ends immediately prior to the ICCL's funding year. For example, when calculating the appropriate annual contribution to pay the ICCL for the funding year commencing 1 August 2004 and where the firm's financial year runs from January to December, then the correct reference period to use is the 1 January 2003 to 31 December 2003 financial year.

3. Should a client who invests a once-off lump sum with a product producer via a firm be included?
   This client should be included in "eligible client" numbers in the year in which the lump sum is invested.

4. Should BES clients be included?
   You should include eligible clients who have entered or exited the BES scheme during the year in question.

5. Should a client who deals with more than one entity within a group be included?
   YES. You should include clients for whom a receipt and transmission service was provided by one group entity even if the order was passed to another group entity for execution.

6. Why should clients covered for Deposit Protection Scheme purposes also be included in eligible clients for the Investor Compensation Scheme?
   The number of different and separate interactions which entities within a group have with an eligible investor increases the overall risk profile of the group. Therefore, firms must include all relevant interactions with clients for the purposes of calculating eligible clients for the Investor Compensation Scheme.

7. How should clients investing in Tracker bonds be dealt with?
   Tracker bonds are investment instruments for the purposes of the Investment Intermediaries Act, 1995 and therefore clients who deal in these instruments would be "eligible clients" should that firm fail. On this basis these clients must be included when determining the number of eligible clients of each firm.
   Tracker Deposit Investors should be included in eligible clients numbers at initial investment and at maturity stages.

8. Should Professional investors be included in eligible client numbers?
   Professional and institutional investors are specifically excluded under Article 2 of the Act.
   A professional investor is a client of an investment firm whom the investment firm can show has sufficient and appropriate expertise in investment instruments to be categorized as a professional investor.
   - If the firm categorises investors as Professional investors, then these can be excluded from eligible client numbers only in the following circumstances:
     a) If the firm writes to the professional investor and makes them fully aware of the consequences of being designated professional i.e. they are not entitled to participate in the Investor Compensation Scheme and

b) If the investor acknowledges in writing to the investment firm that they have been made aware of the consequences of being categorized as a professional investor.
c) The investor must have met the criteria to be treated as a professional investor for the entire financial year i.e. this acknowledgement must be in place for all such investors either from inception or from the commencement of the firm's relevant financial year, whichever is earlier.

9. Should Bed and Breakfast clients be included?
Bed and breakfast clients must be included in eligible clients unless the firm does not at any time hold/control cash or investment instruments.

10. Should accountants be included in eligible client numbers?
YES. An Accountant should be included unless:
a) the accountant is acting as a provider of investment business services, or
b) the accountant is a professional investor as referred to in 8 above.

11. Should clients which have been referred by an accountant be included?
YES. Clients, which are referred by accountants to brokers, do qualify to be treated as eligible investors by those brokers and should be included in the assessment of eligible client numbers by those brokers.

12. Should solicitors be included in eligible client numbers?
YES. A Solicitor should be included unless:
a) the solicitor is acting as a provider of investment business services, or
b) the solicitor is a professional investor as referred to in 8 above.

13. Should clients which have been referred by a solicitor be included?
YES. Clients, which are referred by solicitors to brokers, do qualify to be treated as eligible investors by those brokers and should be included in the assessment of eligible client numbers by those brokers.

14. How should investment clubs be treated?
A club is an association or grouping without legal personality within the meaning of Section 37 (3) of the Act. Therefore, each investment club should be treated as a single eligible client.

15. Are pension funds excluded investors and therefore should they be excluded from eligible client numbers?
In general, Pension Funds meet the definition of professional and institutional investors as referred to in 8 above. However, for the purposes of calculating eligible client numbers, Pension Funds of individuals operating a personal retirement account should be included.

[9] In effect, the ICCL's definition of "eligible client" is a person, not being an excluded investor, who has entrusted money or investment instruments to an investment firm in connection with the provision of an investment business service by the investment firm.

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16. How should members of Employee Share Ownership Plans ("ESOPs") be treated when determining eligible client numbers?

Due to the variety of ESOP arrangements which exist, firms should adopt a 'principles' based approach when deciding how to calculate eligible client numbers in relation to their ESOP arrangements. Firms should count all ESOP members who at any stage throughout the firm's financial year met the definition of eligible investor[10] under Article 2 of the Investor Compensation Act, 1998 (the "Act"), including execution-only clients.

In general, ESOPs comprise three elements:

1) an Employee Share Ownership Trust ("ESOT" - a trust),
2) an Approved Profit Sharing Scheme ("APSS" - a trust) and
3) Beneficiaries

When shares are transferred from an ESOT to an APSS, participants become beneficially entitled to the shares with immediate effect irrespective of any procedural delays which might occur in effecting the transfer of shares from the APSS to beneficiaries.

Therefore, the following bases should be used in determining the number of eligible clients a firm has in relation to an ESOP - unless the clients would otherwise be regarded as 'excluded investors' under Section 2(1) of the Investor Compensation Act, 1998.

a) The Trustee(s) of the ESOT should be counted as a single eligible client.
b) The APSS Trustee(s) should be treated as a single eligible client if the Trust holds shares which are not attributable to particular beneficiaries.
c) Each beneficiary, either to whom the APSS has transferred shares or on behalf of whom the Trustee(s) of the APSS holds shares, should be counted as individual eligible clients.

A key issue with regard to whether an ESOP, or in particular an ESOT / APSS, constitutes one eligible client or whether some, or all, of their individual members constitute eligible clients depends on whether each such ESOP / ESOT / APSS / individual member meets the definition of eligible investor. Any such determination should be undertaken on a case by case basis for any given ESOP situation.

17. How should 'Insurance Clients' be treated when determining eligible client numbers?

Fund A firms, authorised to carry out insurance business and which have insurance clients, must contribute to the Investor Compensation Scheme on the following bases in respect of those clients:

1) Insurance-only clients should be included in a firm's calculation of eligible client numbers - unless the clients would otherwise be regarded as 'excluded investors' under Section 2(1) of the Investor Compensation Act, 1998.
2) An eligible client whom a firm identifies as both an investment and insurance client should be counted only once.

[10] In effect, the ICCL's definition of "eligible client" is a person, not being an excluded investor, who has entrusted money or investment instruments to an investment firm in connection with the provision of an investment business service by the investment firm.

APPENDIX 5
SOME RELEVANT DEFINITIONS

Investor Compensation Act, 1998

"Authorised investment firm" means –

(a) an authorised investment business firm, or

(b) an authorised member firm, or

(c) a credit institution the authorisation of which by the Bank under Directive No. 77/780/EEC of 12 December 1977 and Directive No. 89/646/EEC of 15 December 1989 extends to one or more investment services listed in section A of the Annex to the Investment Services Directive, or

(d) an insurance intermediary.

"Client" means a person who has entrusted money or investment instruments to an investment firm in connection with the provision of investment business services by the investment firm.

"Eligible investor" means a person, not being an excluded investor, who is a client of an investment firm and has made an application for payment under section 34 of the Act.

"Excluded investor" means a client of an investment firm which has been the subject of a determination by the supervisory authority under section 31 or a ruling and, in relation to that investment firm, is-

a) a professional or institutional client, including:

i. an investment firm;

ii. an investment firm for the purposes of the Investment Services Directive;

iii. a credit institution as defined in Article 1 of Council Directive No. 77/780/EEC;

iv. a financial institution as defined in Article 1(6) of Council Directive No. 89/646/EEC of 15 December 1989;

v. an insurance undertaking;

vi. an undertaking for collective investment; or

vii. a pension or retirement fund, or

b) a local authority, or

c) a director, manager or personally liable member of the investment firm, a holder of at least 5 per cent of the capital of the investment firm, a person responsible for carrying out the statutory audit of the investment firm or a client with similar status in a group undertaking, or

d) a close relative or a third party acting on behalf of a client referred to in paragraph (c), or

e) another firm in a group undertaking, or

f) a client who has any responsibility for, or has taken advantage of, facts relating to the investment firm which gave rise to the firm's financial difficulties or contributed to the deterioration of its financial situation, or

g) a company which is of such a size that it is not permitted to draw up abridged balance sheets under Article 11 of the Fourth Council Directive No. 78/660/EEC of 25 July 1978 based on Article 54(3)(g) of the Treaty on the annual accounts of certain types of companies, or

h) a client specified by the supervisory authority as an excluded investor in accordance with section 35(8).

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"Investment firm" means –

(a) an authorised investment business firm or a person (being a person who was an authorised investment business firm) whose authorisation has been revoked,

(b) an authorised member firm or a person (being a person who was an authorised member firm) whose authorisation has been revoked,

(c) a credit institution licensed in the State or a credit institution whose authorisation by the Bank under Council Directive 77/780/EEC of 12 December 1977 as amended by Council Directive 89/646/EEC of 15 December 1989 as amended and extended from time to time extends to one or more of the investment services listed in the Annex to the Investment Services Directive or a credit institution whose authorisation by the Bank under Council Directive 77/780/EEC of 12 December 1977 as amended by Council Directive 89/646/EEC of 15 December 1989 as amended and extended from time to time has been revoked or a credit institution whose authorisation by the Bank under Council Directive 77/780/EEC of 12 December 1977 as amended by Council Directive 89/646/EEC of 15 December 1989 as amended and extended from time to time no longer extends to one or more of the investment services listed in the Annex to the Investment Services Directive, or

(d) an insurance intermediary or a person who was formerly an insurance intermediary.

"Receipted monies" means the value of client money or investment instruments forming part of the net loss of an eligible investor which were entrusted by the eligible investor to a restricted intermediary for transmission to an identifiable product producer from which the restricted intermediary held a valid written appointment at the time the money or investment instruments were so entrusted.

"Restricted intermediary" means an investment firm which is or was –

(a) a restricted activity investment product intermediary, or

(b) an insurance intermediary which is not an authorised investment business firm (unless the investment firm is a restricted activity investment product intermediary),

or both and is not a member of a compensation scheme approved of under section 25.

NOTES

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