



Gibraltar Investor Compensation Scheme

Explanatory Information



The Investor Compensation Scheme Act 2002 ("the Act") implements the EU Directive on Investor Compensation Schemes (97/9/EC). Investment firms⁽¹⁾ are required, on request, to provide all investors and intending investors with details of the Investor Compensation Scheme to which they belong and the conditions and procedures for making a claim. The following describes the basic terms of the Investor Compensation Scheme (the "Scheme").

Which Firms Are Covered By The Scheme?

The following firms are covered by the scheme:

- Firms authorised under the Financial Services Financial Services (Markets in Financial Instruments) Act incorporated in Gibraltar including their branches in the European Economic Area (EEA)
- Firms with a head office in a non-EEA state where equivalent protection to investors in Gibraltar is not offered by any investor compensation scheme.

How Do I Know If A Particular Firm Is A Member Of The Scheme?

The firm's own literature in relation to the Scheme will state to which scheme(s) the firm belongs. The Gibraltar Investor Compensation Board ("the Board") can also advise you if the firm participates in the Scheme.

What Limits Apply To The Scheme?

The Scheme covers 90% of a firm's total liability to an investor in respect of eligible investments held subject to a maximum payment to any one individual of Euro 20,000.

A firm's total liability to an investor is the aggregate of all investments in the name of that investor, including the investor's share in an investment held jointly.

Investments held jointly are divided equally between investors where there is no indication of the share of each holder in the investment.

Partnerships or similar associations will be treated as one claimant.

Investments held by trustees will be treated as one claimant unless each of the beneficiaries can be separately identified, and has a separate right under the trust before the date of the declaration by the Chief Executive Officer of the FSC.

The following will be deducted from the amounts payable under the Scheme:

- payments received from investor compensation schemes elsewhere;
- payments from any insurance policy taken out by the claimant in respect of the investment;
- payments from the liquidator or receiver; and
- any amounts which had a right of set-off at the date of declaration.

The limits shown above are those which will apply in the majority of cases. However, if an investment is made with the branch of a Gibraltar firm in a Member State or a Gibraltar branch of a European Authorised Institution, the limits may be higher than those shown above.

¹ The terms 'firm' and 'investment firm' are used as meaning those banks and firms carrying on investment business as set out in Schedule 1 to the Financial Services Financial Services (Markets in Financial Instruments) Act .

Eligible investments



The Scheme only covers eligible investments. Eligible investments are defined as follows:

- Transferable securities
- Units in collective investment undertakings
- Money market instruments
- Financial-futures contracts (including equivalent cash-settled instruments)
- Forward interest-rate agreements (FRAs)
- Interest-rate swaps
- Currency swaps
- Equity swaps
- Options to acquire or dispose of any of the above instruments (including equivalent cash-settled instruments) e.g. currency options and interest-rate options. Options, futures, swaps, forward rate agreements and any other derivative contracts relating to securities, currencies, interest rates or yields, or other derivatives instruments, financial indices or financial measures which may be settled physically or in cash
- Options, futures, swaps, forward rate agreements and any other derivative contracts relating to commodities that must be settled in cash or may be settled in cash at the option of one of the parties (otherwise than by reason of a default or other termination event)
- Options, futures, swaps, and any other derivative contract relating to commodities that can be physically settled provided that they are traded on a regulated market and/or a multilateral trading facility (MTF)
- Options, futures, swaps, forwards and any other derivative contract relating to commodities, that can be physically settled not otherwise mentioned in the previous paragraph and not being for commercial purposes, which have the characteristics of other derivative financial instruments, having regard to whether, inter alia, they are cleared and settled through recognised clearing houses or are subject to regular margin calls
- Derivative instruments for the transfer of credit risk
- Financial contract for differences
- Options, futures, swaps, forward rate agreements and any other derivative contract relating to climatic variables, freight rates, emission allowances or inflation rates or other official economic statistics that must be settled in cash or may be settled in cash at the option of one of the parties (otherwise than by reason of a default or other termination event), as well as any other derivative contract relating to assets, rights, obligations, indices and measures not otherwise mentioned in this Section, which have the characteristics of other derivative financial instruments, having regard to whether, inter alia, they are traded on a regulated market or an MTF, are cleared and settled through recognised clearing houses or are subject to regular margin calls.

The following investments therefore are amongst those not covered by the scheme:

- Investment instruments falling outside the definition in the Market in Financial Instruments Directive (MiFID);
- Life assurance products;
- Pension products;
- Investments arising out of transactions in connection with which there has been a conviction under the anti money-laundering legislation;
- Investments eligible for compensation under the Deposit Guarantee Scheme Act 1997;



Eligible investors

The scheme is only available for certain types of investor. Such investors are often referred to as "private" investors, "ordinary" or "retail" investors.

Investments by professional and institutional investors, as per the definition provided in MiFID, are not covered by the scheme. Professional investors are those who may be deemed to possess the experience, knowledge and expertise to make their own investment decisions and properly assess the risks they incur.

Under MiFID, there is a third category of client - 'eligible counterparties'. For the purposes of GICS these are deemed to be equivalent to professional clients and are therefore outside the scope of the scheme.

For the purposes of calculating the number of eligible clients under the scheme, if the investor can be deemed professional in respect of any service or instrument at any point in time, then they would be deemed as professional investors for the purposes of GICS and therefore not afforded any of the protections. Firms will therefore be obliged to inform clients of this.

Categories of investors who are considered to be professionals

(a) Firms which are required to be authorised or regulated to operate in the financial markets. The list below should be understood as including all authorised entities carrying out the characteristic activities of the entities mentioned: entities authorised by a Member State under a Directive, entities authorised or regulated by a Member State without reference to a Directive, and entities authorised or regulated by a non-Member State-

These are:

- Credit institutions
- Investment firms
- Other authorised or regulated financial institutions
- Insurance companies
- Collective investment schemes and management companies of such schemes
- Pension funds and management companies of such funds
- Commodity and commodity derivative dealers
- Locals - A firm dealing for its own account on markets in financial futures or options or other derivatives and on cash markets for the sole purpose of hedging positions on derivatives markets, or dealing for the accounts of other members of those markets and being guaranteed by clearing members of the same markets, where responsibility for ensuring the performance of contracts entered into by such a firm is assumed by clearing members of the same markets.
- Other institutional investors

(b) Large undertakings meeting 2 of the following size requirements on a company basis: balance sheet total: EUR 20.000.000, net turnover: EUR 40.000.000, own funds: EUR 2.000.000.

(c) National and regional governments, public bodies that manage public debt, the Gibraltar Savings Bank, Central Banks, international and supranational institutions such as the World Bank, the IMF, the ECB, the EIB and other similar international organisations.

(d) Other institutional investors whose main activity is to invest in financial instruments, including entities dedicated to the securitisation of assets or other financing transactions.

(e) Investors with similar status in other firms within the same group and close relatives and third parties acting on behalf of these investors.

(f) Other firms in the same group.

(g) Investors who have any responsibility for or have taken advantage of certain facts, such as information not generally available to the public, relating to an investment firm which gave rise to the firm's financial difficulties or contributed to the deterioration of its financial situation.



(h) Persons responsible for carrying out the statutory audits of investment firms' accounting documents.

Where the client of an investment firm is an undertaking referred to above, the investment firm must inform it prior to any provision of services that, on the basis of the information available to the firm, the client is deemed to be a professional client, and will be treated as such unless the firm and the client agree otherwise.

Clients assessed as professional

Where the investment firm makes a determination based on an adequate assessment of the expertise, experience and knowledge of the client, which gives reasonable assurance, in light of the nature of the transactions or services envisaged, that the client is capable of making his own investment decisions and understanding the risks involved, then the firm can consider such investor as a professional client.

Where an assessment has been conducted under MiFID to classify a client and the client is categorised as a professional for the purposes of MiFID, this assessment will suffice for GICS - the client can be considered professional and would not be considered an eligible investor.

As part of the above mentioned assessment a minimum of two of the following criteria should be satisfied:

(a) The investor has carried out transactions, in significant size, on the relevant market at an average frequency of 10 per quarter over the previous four quarters;

(b) The size of the investor's financial instrument portfolio, defined as including cash deposits and financial instruments exceeds 0,5 million Euro;

(c) The investor works or has worked in the financial sector for at least one year in a professional position, which requires knowledge of the transactions or services envisaged.

If investors have already been categorised as professionals under parameters and procedures similar to those above, it is not intended that their relationships with the investment firm should be affected by any new rules adopted by firm.

Retail clients opting-up to professional status

Where a client who has been classified as retail, advises the firm post the relevant assessment conducted by the firm, that he wants to be considered as professional, i.e. is an elective professional, the firm is still required, prior to considering the client as professional for the purposes of GICS. This is to ensure that an adequate assessment of the expertise, experience and knowledge of the client is undertaken by the investment firm, and gives reasonable assurance, in light of the nature of the transactions or services envisaged, that the client is capable of making his own investment decisions and understanding the risks involved. Hence at least two of the following is satisfied:

(a) The investor has carried out transactions, in significant size, on the relevant market at an average frequency of 10 per quarter over the previous four quarters;

(b) The size of the investor's financial instrument portfolio, defined as including cash deposits and financial instruments exceeds 0,5 million Euro;

(c) The investor works or has worked in the financial sector for at least one year in a professional position, which requires knowledge of the transactions or services envisaged.

And;

(1) The investor must state in writing to the investment firm that they wish to be treated as a professional investor;

(2) The investment firm must give the investor a clear written warning of the protections and investor compensation rights they will lose;

(3) The investor must state in writing, in a separate document from the contract, that they are aware of the consequences of losing such protections.



Before deciding to accept any request, investment firms must be required to take all reasonable steps to ensure that the client requesting to be treated as a professional client meets the relevant requirements stated above.

"Elective" professional clients under MiFID are non-eligible clients for the purposes of GICS.

Professional clients opting-down to retail status

Professional clients may wish to opt-down and be treated as retail clients under MiFID, such clients would not be eligible for cover under GICS.

Under MiFID, a firm may agree to a request from a professional investor to be categorised as a retail investor, or such a re-categorisation occurs as a result of the firm's assessment of that client's suitability or appropriateness i.e. where a professional client 'opts down' to the retail category, such a client would not be eligible for compensation under the scheme, by virtue of having been considered a professional investor at some other point. These clients would need to be advised by the firm that their re-categorisation as a retail client would not change their treatment under the scheme i.e. this type of client would continue to be excluded from the scope of the scheme.

Treatment of all clients as retail

Firms opting to categorise all their investors as retail investors for the purposes of MiFID, should continue to classify investors as eligible or professional for the purposes of GICS, and these classifications should not change irrespective of the client's 'new' and 'temporary' treatment under MiFID. For example, when a participant of the scheme has historically reported 20 eligible clients and 25 professional clients but now under MiFID will be categorising all investors as retail investors for those purposes, the number of eligible clients reported in the GICS quarterly return would still be 20 clients and not 45.

Firms should advise clients accordingly of whether protection is in fact afforded to them under the Scheme.

Firms must have appropriate written internal policies and procedures to categorise investors.



How Is the Scheme activated?

The Scheme is activated upon the occurrence of one of the criteria prescribed in section 9 of the Act. The most likely of these events is a Court's decision to put the firm into liquidation.

The Scheme will also be activated if the Chief Executive Officer of the FSC determines that a firm has been unable to meet its obligations to investors for reasons which are directly related to its financial circumstances, and has no current prospect of being able to do so.

How Are Claims Made Under The Scheme And How Are Payments Made?

If the Scheme is activated, the Board will obtain from the firm in default the name and address of each investor with eligible investments. The Board will then write to each investor enclosing a claim form. Full details of how to complete the form will be given at the time. In the normal course, investors need take no action until they have heard from the Board.

Each claim will need to be verified before payment can be made. This will usually involve the Board asking the liquidator or administrator to confirm the total amount of eligible investments, and to confirm that the investment is due and payable under the terms on which it was made and is not a type of investment which is excluded from protection.

If the firm has been placed in liquidation by the Gibraltar Courts, investors will need to lodge a proof of debt or a claim for repayment in the liquidation with the liquidator. This procedure will normally be notified to investors by the relevant liquidator. If a liquidator has not been appointed, investors will be asked to complete an appropriate form by the Board which the Board will be able to lodge on their behalf with a liquidator or administrator, if one is appointed at a later date.

All payments to investors will be made as soon as practical after an investment becomes due and payable. In a liquidation, all investments become due and payable immediately and therefore payments can be made as soon as a claim is verified. However, in other cases, investments normally continue to their original maturity date. Investors will therefore have to wait for a compensation payment until that maturity date is reached. Payments will be made by cheque in favour of the individual investor.

Before paying any compensation, the Board must receive confirmation from the claimant that:

- rights in respect of his investment will vest in the Board;
- he will assist the Board in exercising those rights;
- he will pay the Board any amounts he receives in respect of those rights, after deduction of any amount the Board may be required to repay him; and
- any prospect of recovering an amount in excess of the compensation payable will vest in the Board.

Any costs incurred by the Board directly in relation to that investment will be deducted from the amount of compensation paid, or payable to, the claimant.

A claimant who is dissatisfied with a decision of the Board relating to compensation may appeal to the Supreme Court who may direct the Board to take any action which the Board may take under the Act.

Further Information

The above is a summary of the terms of the Scheme and claims procedures and conditions that must be fulfilled before payments under the Scheme can be made. Reference should also be made to the original legislation for its full terms and effect.



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