

ANNUAL REPORT 2020

DEPOSITOR COMPENSATION SCHEME

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Introduction

Pursuant to Regulation 5(9) of the Depositor Compensation Scheme Regulations (“the Regulations”), S.L. 371.09, the Management Committee of the Depositor Compensation Scheme (“the Scheme”) hereby presents its report on the discharge of functions and operation of the Scheme for the year 2020.

The Scheme’s audited financial statements as at 31 December 2020 are attached.

Management Committee

In accordance with regulation 5(1) of the Regulations, the Scheme is managed and administered by a Management Committee (“the Committee”), appointed by the Malta Financial Services Authority. The members of the Committee during 2020 were:

Chairperson

Mr Robert Caruana

Members

Mr George Farrugia

Mr Kenneth Farrugia

Mr Silvio Galea

Mr Karol Gabarretta

Dr Mauro Magro

Dr Edmond Zammit Laferla

Secretary

Mr Aldo Giordano

Meetings of the Committee

The Committee held twelve meetings during 2020.

Membership in the Scheme

In line with Regulation 7 of the Regulations, a credit institution which is licensed in Malta under the Banking Act shall participate in the Scheme, excluding branches established in Malta by a credit institution which has its head office outside the European Union.

List of participants in 2020:

Agri Bank plc

APS Bank Limited

BNF Bank plc

Bank of Valletta plc

Credorax Bank Limited

ECCM Bank plc

FCM Bank Limited

Ferratum Bank plc

Fimbank plc

HSBC Bank Malta plc

IIG Bank (Malta) Limited

Izola Bank plc

Lombard Bank Malta plc

Medirect Bank

MFC Merchant Bank Limited

NBG Bank Malta Limited

Novum Bank Limited

Satabank plc – Licensed revoked June 2020

Sparkasse Bank Malta plc

Financial Statements as at 31 December 2020

The Scheme registered a deficit of €145,459 in 2020, compared to a deficit of €374,303 registered in 2019. Income from available financial means amounted to €376,643 (2019: €83,149), while Management Expenses incurred during the year added up to €522,102 (2019: €457,452). As at the end of 2020, Accumulated Contribution Funds and Reserves amounted to €66,200,406 (2019: €51,156,625).

Objective and functions of the Scheme

As outlined in Directive 2014/49/EU on deposit guarantee schemes, the key task of a DGS is to protect depositors against the consequences of the insolvency of credit institutions. The primary aim is thus to repay depositors up to a harmonised coverage level of €100,000 per depositor.

Once the Competent Authority makes a determination that a financial institution has unavailable deposits, that is, the institution failed to repay deposits which are due and payable, and appears for the time being to be unable to repay deposits for reasons which are directly related to its financial circumstances, or otherwise, a judicial authority has made a ruling for reasons which are directly related to the member's financial circumstances and which has the effect of suspending the rights of depositors to make claims against it, the Scheme shall be informed of such determination by the Competent Authority, as soon as possible.

Upon being informed, the Committee shall publish a notice on its website and in at least two local newspapers, informing depositors of the financial institution concerned of such determination or ruling and of the manner in which the compensation to the depositors shall be processed.

The Scheme shall then proceed to pay compensation as specified in the Regulations, for eligible deposits, taking into consideration the provisos and exclusions set out in Regulation 9. Regulation 13 sets the time limit for payment of compensation at fifteen working days if the pay-out is effected from 1 January 2019 until 31 December 2020.

On a more specific level, the functions of the Scheme, as outlined in Regulation 3 of the Regulations are:

- a) to maintain 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 funds in accordance with these regulations;
- b) to establish and maintain, after consultation with the Competent Authority, arrangements for the making of payments to depositors;
- c) to process claims for compensation by depositors as expeditiously as possible and to ensure that compensation is paid out without undue delay;

- d) to finance the resolution of members, pursuant to Regulation 33(2);
- e) to use available financial means for alternative measures to prevent the failure of a member, pursuant to Regulation 33(3);
- f) to use available financial means for alternative measures to preserve the access of depositors to covered deposits, including transfer of assets and liabilities and deposit book transfer, in the context of insolvency proceedings, pursuant to regulation 33(6);
- g) to advise the Malta Financial Services Authority on matters relating to the functions of the Scheme.

Recovery and Resolution Regime

During 2020 the Scheme was not required to exercise any of its functions referred to in paragraphs (d), (e) and (f) above, under the Recovery and Resolution regime established by the Bank Recovery and Resolution Directive.

Maintenance of the Fund

In line with regulation 23 of the Regulations, the available financial means of the Scheme shall amount to 1.3% of the covered deposits of its members and the target level must be maintained. Where the financing capacity falls short of such target level, the payment of contributions shall resume at least until the target level is reached again. As at the end of 2020, the Scheme's available financial means amounted to €134,736,675 whereas the target level required as at the end of 2020 was €169,221,427. The difference may be accounted for in the compensation paid out to depositors of a credit institution in 2017 and the Committee is taking all the necessary action to reach the target level of the available financial means.

The Scheme may at any time require members to pay a Compensation Contribution and a Management Expenses Contribution.

- Compensation Contribution

The Compensation Contribution is based on the amount of covered deposits, excluding temporary high balances, of each member and the degree of risk incurred by the respective member.

The annual compensation contributions are determined by the Scheme for each member in accordance with the Compensation Contribution method.

The annual Compensation Contributions are determined having regard to:

- a) 1.3% of the covered deposits of the members;

- b) the covered deposits of each member at the end of the year immediately preceding the relevant financial year;
- c) the degree of risk incurred by each member by reference to an aggregate risk weight for the year immediately preceding the relevant financial year, in accordance with the risk-based method;
- d) an adjustment coefficient, determined by the Competent Authority at least once in every financial year for all members.

The risk-based method, for determining the degree of risk incurred by members and the Compensation Contribution method, for determining the amount of Compensation Contribution due by each member in each financial year are established by banking rules set by the Competent Authority and which adhere with guidelines issued by the European Banking Association.

The Compensation Contribution may be paid partly in cash contribution and partly by means of a payment commitment, as outlined in Regulation 25(8) of the Regulations. For the year 2020, the total portion of payment commitment could not exceed 52.5%. Payment Commitments may be paid directly into the Scheme's account, in the form of deposits pledged in favour of the Scheme or as securities pledged in favour of the Scheme.

The Compensation Contribution representing 47.5% paid in cash from members collected as at 31 December 2020 amounted to €80,380,178.

The payment commitments in the form of deposits made directly with the Scheme as at 31 December 2020 amounted to €7,852,517, whereas the value of deposits pledged in favour of the Scheme as at 31 December 2020 was €8,350,943 and the value of securities pledged in favour of the Scheme as at 31 December 2020 was €72,637,789.

As at reporting year end, all banks were in compliance with the requirements of the Regulations regarding Compensation Contribution.

- Management Expenses Contribution

The scheme may also require members to pay a Management Expenses Contribution if it has reasonable grounds to believe that the funds available to it meet management expenses in that financial year are, or will be, insufficient. No collection was made for Management Expenses in 2020.

- Contingency Contribution

The Competent Authority has imposed a licence condition on a number of local banks, requesting an additional contingency contribution by means of a pledge in favour of the Scheme. The assets making up the Contingency Contribution Reserve may only be used by the Scheme for the payment of claims of depositors in the event of the pledgor's bank's default. The percentage of covered deposits requested as pledge varies from one institution to the other. The amount required to be pledged in favour of the scheme as at 31 December 2020 amounted to EUR 124,195,325 (2019: EUR 100,037,583). The effective amount pledged in 2020 was EUR 64,681,965 (2019: EUR 93,800,681). The Committee has been tackling this aspect with the relevant participants and the Competent Authority. The Committee is aware of the actions being taken by the Competent Authority to resolve this matter shortly.

Protection of Funds

The Scheme may place its available financial means in a low-risk and sufficiently diversified manner. Funds managed and administered by it may either be held on deposit or invested, having regard to the need for prudence.

In carrying out this function, the Committee has appointed the Central Bank of Malta for Investment Management Services since 2003. As the Investment Portfolio Manager, the Central Bank of Malta is tasked with financial, accounting and reporting services. Given the nature of the Scheme, the parameters for the investment of funds are primarily safety and liquidity.

Data Exchange and Payment Solution

The Scheme has a duty to process a pay-out expeditiously and to ensure that compensation is paid without undue delay. To this end, the Data Exchange and Payment Solution ("DEPS") system has been designed and commissioned. Its objective is to enable the Scheme to receive, load and verify the Single Customer View ("SCV") data file, the Deferred data file and associated metadata files for the purpose of implementing the Regulations. Both types of files should be received directly from the banks electronically via a secure transmission solution within the timeframes set by the Scheme. The system went live in January 2019. All banks were connected to DEPS and successfully submitted their test file. Simulations were conducted to test that the system is working correctly in case of a pay-out.

During 2020, simulations were conducted on the live data to test that DEPS is working as required.

In 2019, the Scheme also subscribed to EDDIES, a platform regarding the exchange of information between deposit guarantee schemes within the European Union and the European Economic Area. In line with the Deposit Guarantee Scheme Directive (“DGSD”), as Host DGS, the Scheme shall cover depositors on behalf of the Home DGS, should a determination be made. The EDDIES platform facilitates the exchange of information from the Home DGS to the Host DGS in order for the Scheme to effect the pay-out. In 2020, the scheme performed a functional test with the Dutch DGS to familiarize itself with the platform, which test resulted in a successful outcome.

Compensation

On 24 March 2017, the MFSA made a determination of unavailable deposits in respect of a credit institution. The Scheme subsequently compensated covered depositors and is actively seeking to replace the reduction in the available financial means resultant from compensation paid out.

COVID-19 Impact

The Scheme was not duly impacted during the months of the COVID-19 pandemic; however, contingency documents and impact assessments were still prepared by the Scheme for such eventuality.

Alternative Funding Arrangement

While private solutions had been sought by the Scheme, there was no availability to reliably source alternative funding arrangements from the private sector in Malta. As such, alternative funding arrangement was discussed in great depth with the Ministry for Finance and Employment, where it is being considered what would be the best option for a backstop measure. Discussions are ongoing with the Ministry.

Service Agreement with MFSA


A service agreement with MFSA was also discussed and drafted in order to improve the Scheme’s services provided for by the competent authority. The Scheme had also drafted a memorandum of understanding outlining the transactions between the DCS and MFSA IT. This was mainly to increase cyber security measures and enhance operational efficiency within the Schemes. Discussions on this are still ongoing.

Consultation

The Scheme works closely with the Competent Authority on matters relating to the compensation of depositors, contributions due by members and other issues that may arise. In 2021, discussions continued from the previous year concerning amendments to the Regulations, as promulgated in LN 43 of 2019. Most noteworthy, the amendments specify that electronic money and funds received in exchange for electronic money do not qualify as an eligible deposit. Furthermore, provisions have been added clarifying the payment of contributions when available financial means are reduced beyond specific levels.

Consultation is also ongoing with other stakeholders, particularly the Central Bank of Malta, the Ministry for Finance and Employment and the Malta Bankers' Association.

On an EU level, in 2020 the Scheme participated in a number of surveys and questionnaires by the European Forum of Deposit Insurers ("EFDI") and various other authorities. Furthermore, the Scheme was once again present for discussions held within the Expert Group on Banking, Payments and Insurance ("EGBPI"), the Task Force for Deposit Guarantee Schemes ("DGSs") set up by the European Banking Association ("EBA") as well as the Joint Workstream on Anti-Money Laundering and Available Financial Means and other meetings held by EFDI. Discussions on the European Deposit Insurance Scheme Regulation ("EDIS") are ongoing and the Scheme, together with the Ministry for Finance and Employment and other stakeholders provides feedback and support where necessary.



Robert Caruana

Chairman

On behalf of the Compensation Schemes Management Committee

26 May 2021

Attachment: Audited Financial Statements of the Depositor Compensation Scheme for 2020