

## **DEPOSITORS COMPENSATION SCHEME**

This section is intended to provide a general explanation of the workings of deposit compensation arrangements in the Isle of Man. These arrangements apply to deposits with institutions licensed under the Isle of Man banking legislation. This explanation inevitably simplifies many of the relevant procedures and criteria and is not intended to be a substitute for reference to the [Banking Business \(Compensation of Depositors\) Regulations 1991](#), as amended ("the Regulations") (see [Appendix C1](#)) under which the Isle of Man Depositors Compensation Scheme ("the Scheme") was established and by which it is now governed.

The following explanation is based on the Regulations as is in force and as operated by the Scheme Manager as at 1 June 1999 and the references in square brackets are to the provisions of those Regulations in force at that date.

### **General**

The purpose of the Scheme is to give a measure of protection to depositors in respect of sterling and foreign currency deposits made with Isle of Man offices of institutions which are licensed under the [Banking Act 1998](#) ("the Act") ("banking institutions") but with the exception of a few such institutions as listed in the Regulations. Compensation for depositors arises when a banking institution is deemed to be in default under the Scheme which, in essence, occurs when that banking institution becomes insolvent.

Unlike the equivalent scheme in the United Kingdom, there is no standing fund under the Scheme. A fund for the payment of compensation to depositors is created when the need arises - by virtue of the default of a banking institution. Each such fund is financed by way of contributions which all banking institutions are liable to make.

The Scheme is managed by the Financial Supervision Commission in its capacity as Scheme Manager. The financial year of the Scheme runs from 1 April to 31 March and the Scheme Manager is obliged, in respect of each financial year of the Scheme, to make and publish a report to the Isle of Man Treasury on the operation of the Scheme. That report must include a balance sheet and income and expenditure account. The Scheme Manager is also required to keep proper financial and other records. [[Regulation 5](#)].

## Compensation

Where a banking institution is deemed to be in default under the Scheme, the Scheme Manager is required to pay compensation to depositors out of the fund created in respect of that default. The amount of the compensation payable to each depositor to whom the banking institution in default has an "eligible protected deposit liability" is an amount equal to 75% of the eligible protected deposit liability, subject to a maximum compensation payment to any one depositor of £15,000. [[Regulation 11\(1\)](#)]. It should be noted that the amount of compensation may be reduced as outlined in paragraph [7.1.2.4](#) below.

The Scheme Manager's calculation of the amount of an eligible protected deposit liability and the extent of the compensation available to a depositor is based on the following:

- i. An eligible protected deposit liability means the total liability of the banking institution to the depositor. It includes principal and accrued interest on sterling and foreign currency deposits - in the name of the depositor - made with an Isle of Man office of the banking institution - at the time of the default [[Regulation 9\(1\)](#)];
- ii. i) Separate deposits in the Isle of Man in the same name are aggregated [[Regulation 9\(3\)](#)];
- iii. Joint accounts (other than partnership accounts) are divided equally between the accountholders [[Regulation 9\(3\)](#)];
- iv. (iv) No distinction is made between protection for corporate or personal accounts and a deposit may be considered for protection regardless of the depositor's residential status;
- v. No protection is given to deposits made by banking institutions or investment businesses licensed in the Isle of Man or to banks which are authorised, licensed or recognised in a country or territory outside the Isle of Man [[Regulation 10\(4\)](#)];
- vi. No protection is given to deposits made by any person who, in the opinion of the Scheme Manager, has any responsibility for, or may have profited directly or indirectly from the circumstances giving rise to the banking institution's default
- vii. No protection is given to deposits made by any person who was at the time of the banking institution's default a shareholder, director, controller or manager of the banking institution or any associate of such persons (for definitions see the relevant Regulations) [[Regulation 10\(4\)](#)];
- viii. Secured deposits are excluded from protection [[Regulation 10\(3\)](#)]

- ix. Special provisions apply to the treatment of certain trust accounts; in general, these are determined by the terms of the trust and it will usually be necessary for the Scheme Manager to have sight of the relevant trust documentation [Regulation 9\(3\)](#)];
- x. Special provisions also apply to designated client accounts [Regulation 9\(3\)](#)];

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In addition to the criteria for the calculation of an eligible protected deposit liability, there are a number of pre-conditions to be satisfied before compensation can be paid:

- i. (i) No compensation can be paid unless the depositor has first lodged with the liquidator of the banking institution a proof of debt in respect of the eligible protected deposit liability [\[Regulation 9\(2\)\]](#);
- ii. No compensation can be paid unless the depositor has agreed that his existing rights in respect of his eligible protected deposit liability shall vest in the Scheme Manager [\[Regulation 15\(2\)\]](#);
- iii. A depositor's application for compensation will be rejected if submitted more than six months after the depositor became aware, or ought reasonably to have become aware, of the default of the banking institution, unless the Scheme Manager determines that, by reason of exceptional circumstances, it ought to be accepted for consideration [\[Regulation 10\(1\)\]](#);
- iv. a depositor's application for compensation will be rejected if submitted more than eighteen months after the date of the default of the banking institution [\[Regulation 10\(1\)\]](#).

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The Scheme Manager is required to deduct from the amount of any compensation which would otherwise be payable to a depositor:

- a. the amount of any liability of the depositor to the banking institution in respect of which a right of set-off existed at the time of the default [\[Regulation 10\(5\)\]](#);
- b. the amount of any payment made to a depositor under any scheme for protecting or assisting depositors or investors in

respect of the relevant eligible protected deposit liability [[Regulations 10\(5\) & 10\(7\)](#)].

The length of time between making a claim and the payment of compensation by the Scheme Manager depends on the particular circumstances. Under the Regulations, the Scheme Manager is required to decide to pay compensation to a depositor as soon as he is satisfied that the banking institution in question has an eligible protected liability to the depositor and is unable or is likely to be unable to meet that liability [[Regulation 8\(1\)](#)]. However, once the Scheme Manager has decided to make a compensation payment, it will not necessarily be possible for the Scheme Manager actually to pay compensation in full or in part immediately. The method of funding of the Scheme imposes certain constraints on the actual payment of compensation, in that the Scheme Manager is not permitted to pay out compensation in any one financial year of the Scheme which would exceed the amount of contributions to the Scheme from banking institutions in that year [[Regulation 11\(2\)](#)] and any partial payment of compensation must be apportioned pro rata between claimants [[Regulation 11\(3\)](#)].

## **Contributions**

When a banking institution is deemed to be in default, a fund is created for the payment of compensation to the depositors with that banking institution. The fund created is financed by the payment of contributions from the other banking institutions participating in the Scheme.

The amount of the contributions which may be levied on a banking institution in any one financial year of the Scheme is subject to upper and lower limits. The lower limit is £25,000 and the upper limit is the lesser of £250,000 and 0.125 per cent of the relevant banking institution's average sterling and foreign currency deposit base as calculated in accordance with the Regulations [[Regulations 12\(1\) & 12\(2\)](#)]. For the purpose of calculating a banking institution's sterling and foreign currency deposit base, there are to be excluded such deposits as the Scheme Manager reasonably thinks represent funds deposited with the banking institution by other banking institutions but only to the extent that those funds originate from deposits which are available to be taken into account in the calculation of the contribution to be levied from those other banking institutions [[Regulation 12\(4\)](#)].

Special levy provisions may apply where a participating banking institution is in the process of transferring its business and assets to another member of the same group of companies which is also a participating banking institution [[Regulation 12A](#)].

## **Subrogation**

Before compensation can be paid to a depositor in respect of an eligible protected deposit liability, that depositor must have agreed that his existing rights in respect of that liability shall vest in the Scheme Manager [[Regulation 15\(2\)](#)]. Where the depositor so agrees, the liability - to the depositor - of the banking institution in question is extinguished. There is conferred on the Scheme Manager a right of recovery against that banking institution, being a right otherwise identical to the depositor's right in respect of the liability in question [[Regulation 15\(3\)](#)].

**Out of any sums recovered by the Scheme Manager, by virtue of the rights vested in it by a depositor, the Scheme Manager is entitled to retain an amount equal to the aggregate of: the amount of the compensation paid to the depositor; plus interest on that compensation at a rate equal to two per cent over the base rate of NatWest Offshore Limited; plus the costs of recovery [[Regulation 12\(4\)](#)].**

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Any amounts recovered which exceed the amount which the Scheme Manager is entitled to retain shall be paid to the depositor [[Regulation 12\(4\)](#)].

## **Co-operation with the Scheme Manager**

The Regulations require banking institutions to co-operate with the Scheme Manager in making available all information, books and documents and otherwise render all such assistance as is necessary to assist the Scheme Manager in performing his functions in relation to the Scheme [[Regulation 14](#)].