

# **Bank Deposit Guarantee Systems**

*A Comparative Study within the G-20*

By

**Felix I. Lessambo**

# **Bank Deposit Guarantee Systems: A Comparative Study within the G-20**

**By Felix I. Lessambo**

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# List of Acronyms

ASBA:	Association of Supervisors of Banks of the Americas
BCBS:	Basel Committee on Banking Supervision
BCRA:	Banco Central de la República de Argentina
BoP:	Balance of Payment
CAMELS:	Capital adequacy, asset quality, management, earnings, liquidity, and sensitivity
CBR:	Central Bank of Russia
CD:	Certificate of Deposit
CDIC:	Canada Deposit Insurance Corporation
CGF:	Credit Guarantee Fund
CRA:	Contingent Reserve Arrangement
CSR:	Corporate Social Responsibility
CU:	Credit Union
DDR:	Designated Reserve Ratio
DGS:	Deposit Guarantee Scheme
DICGC:	Deposit Insurance and Credit Guarantee Corporation
DICJ:	Deposit Insurance Corporation of Japan
DIF:	Deposit Insurance Fund
DIS:	deposit Insurance Scheme
DPF:	Deposit Protection Fund

ECB:	European Central Bank
EDIS:	European Deposit Insurance Scheme
EFF:	Extended Fund Facility
EFSM:	European Financial Stabilization Mechanism
ESM:	European Stability Mechanism
ESRRF:	European Single Resolution Fund
EU:	European Union
FCA (UK):	Financial Conduct Authority
FCL:	Flexible Credit Line
FDI Act:	Federal Deposit Insurance Act
FDIC:	Federal Deposit Insurance Corporation
FGC (Brazil):	Credit Guarantee Fund
FGCoop (Brazil):	Cooperative Guarantee Fund
FITD (Italy):	Interbank Deposit Protection Fund
FSAP:	Financial Sector Assessment Program
FSB:	Financial Stability Board
FSCS (UK):	Financial Services Compensation Scheme
FSLIC:	Federal Savings and Loan Insurance Corporation
FSOC:	Financial Stability Oversight Council
GFSN:	Global Financial Safety Network
GICs:	Guaranteed Investment Certificates
IADI:	International Association of Deposit Insurers
IBRA:	Indonesian Bank Restructuring Agency



ILC:	Industrial Loan Companies
IMF:	International Monetary Fund
IRA:	Individual Retirement Account
NAFA:	North American Framework Agreement
NCUA:	National Credit Union Administration.
NRA:	National Resolution Authority
OCC:	Office of the Comptroller of the Currency
PBOC (China):	People Bank of China
RBI:	Reserve Bank of India
RFA:	Regional Financing Arrangement
SAIF:	Savings Association Insurance Fund
SARB:	South African Reserve Bank
SBA:	Stand-By-Arrangement
SEC:	Securities and Exchange Commission
SEDESA (Argentina):	Deposit Insurance Corporation
SRB:	Single Resolution Board
SRF:	Single Resolution Fund
SRM:	Single Resolution Mechanism
WOCCU:	World Council of Credit Union

# Glossary of Terms

**Account Balance:** The dollar amount including principal and interest for a specific account.

**Assessment Base:** The base on which the deposit insurer charges the premium or calculates the levy needed to compensate the insured depositors.

**Bailout:** Any transfer of funds from public sources to a failing or failed Bank, or a commitment by a public authority to provide funds with a - Bank: Any entity, which accepts Deposits or repayable funds from the public and is classified under the jurisdiction's legal framework as a Deposit-taking Institution.

**Balance of Payments (BOP):** A statement summarizing the economic transactions between the residents of a country and nonresidents during a specific period, usually a year. The BOP includes transactions in goods, services, income, transfers and financial assets and liabilities.

**Bank run:** A rapid and significant withdrawal of Deposits from a bank by depositors following a loss of confidence precipitated by the fear that the Bank may fail, and that depositor may therefore suffer losses or lose access to funds.

**Blanket Guarantee:** A declaration by authorities that, in addition to the protection provided by limited coverage deposit insurance or other arrangements, certain Deposits and perhaps other financial instruments will be protected.

**Beneficiary:** A person or entity named or identified either in the bank account records or in a written trust that will have an interest in the trust upon the account owner's death.

**Bridge bank:** refers to an entity that is established to temporarily take over and maintain certain assets, liabilities and operations of a failed bank as part of the resolution process.

**Certificate of Deposit (CD):** A CD is a deposit type, not an account ownership category. The amount of coverage available to the owner of a CD depends on the ownership category (single, joint, trust, IRA) in which the CD is held and what other deposit accounts the owner holds in that same category at the same bank.

**Co-insurance:** A “loss-sharing” arrangement whereby depositors are covered for a pre-specified portion of Deposits that is less than 100% of their Insured Deposits.

**Commercial Bank:** refers to a financial institution that accepts deposits, offers checking account services, makes various loans, and offers basic financial products like certificates of deposit (CDs) and savings accounts to individuals and small businesses.

**Corporate Governance:** A set of relationships between a company's management, its board, its shareholders and other stakeholders which provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance. It helps define the way authority, responsibility is allocated, and how corporate decisions are made

**Coverage limit:** The maximum amount, which a depositor can Claim from or be reimbursed by a Deposit Insurer in the event of a Bank failure.

Credit Union is a type of financial cooperative that provides traditional banking services. Ranging in size from small, volunteer-only operations to large entities with thousands of participants spanning the country, credit unions can be formed by large corporations, organizations, and other entities for their employees and members.

Default: is the term used when a party is unwilling or unable to pay their debt obligations.

Deposit: Any credit balance which derives from normal banking transactions and which a Bank must repay at par under the legal and contractual conditions applicable; any debt evidenced by a certificate issued by a Bank; and any other funds or obligations defined or recognized as Deposits by the law establishing the Deposit Insurance System.

Deposit guarantee schemes (DGSs): Are schemes that refer to a) statutory deposit schemes, b) contractual deposit schemes that are officially recognized as deposit schemes, c) institutional protection schemes that are officially recognized as deposit schemes, and d) credit institutions affiliated to these schemes.

Deposit insurance: A system established to protect depositors against the loss of their insured deposits in the event that a bank is unable to meet its obligations to the depositors.

Deposit Insurance Fund (DIF): The fund maintained by the DIC to insure deposits at failed member institutions.

Deposit Insurer: A specific legal entity responsible for providing Deposit Insurance, Deposit guarantees or similar Deposit protection arrangements.

**Deposit reimbursement:** A Resolution method that involves the reimbursement of Deposits to Insured Depositors.

**Eligible deposit:** Deposits that fall within the Scope of Coverage of a Deposit Insurance System (i.e. they meet the requirements for coverage under a Deposit Insurance System, and are based typically on the type(s) of depositor and/or Deposit).

**European Banking Authority:** An independent EU Authority, which works to ensure effective and consistent prudential regulation and supervision across the European banking sector.

**European Banking Union (EBU):** was established at the Euro Area Summit of 29 June 2012, as a reaction to the financial crisis in 2008. The Banking Union consists of the Single Resolution Mechanism (SRM), the Single Supervisory Mechanism (SSM) and the Single Deposit Guarantee Scheme.

**Ex ante Funding:** The regular collection of Premiums, with the aim of accumulating a fund to meet future obligations (e.g. reimbursing depositors) and cover the operational and related costs of the Deposit Insurer.

**Ex post Funding:** A system in which funds to cover deposit insurance obligations are only collected from surviving Banks after a Bank failure.

**Federal Deposit Insurance Corp (FDIC):** An independent agency of the U.S. government that insures bank and thrift institution deposits of up to \$250,000 per depositor.

**Financial Safety Net:** A framework that includes the functions of prudential regulation, supervision, Resolution, lender of last resort

and Deposit Insurance. In many jurisdictions, a department of government (generally a Ministry of Finance or Treasury responsible for financial sector policy) is included in the financial safety net.

Financial safety net: A framework that includes the functions of prudential regulation, supervision, resolution, lender of last resort and deposit insurance.

The FSB: An international body that oversees and provides recommendations about the global financial system. It promotes international financial stability by coordinating national financial authorities and international standard-setting bodies as they work toward developing strong regulatory, supervisory and other financial sector policies.

G-20: Formed in 1999, the G-20 brings together finance ministers and central bank governors from 19 countries and the European Union (represented by the President of the European Council and the European Central Bank).

Individual Retirement account: An individual retirement account (IRA) is a savings account with tax advantages that individuals can use to save and invest long-term.

International Association of Deposit Insurers (IADI): A forum for deposit insurers from around the world to gather to share knowledge and expertise to enhance the effectiveness of deposit insurance systems

Joint account: A joint account is a bank account that has been opened by two or more individuals or entities.

**Liquidation:** The winding-down of the business affairs and operations of a failed bank through the orderly disposition of its assets after its license has been revoked and it has been placed in receivership.

**Maximum Coverage:** The amount a depositor can claim from the deposit insurer in the event of bank failures.

**Money market account:** A high-yield savings account that's FDIC-insured up to \$250,000. In contrast to a CD, with a money market account, one can still have regular access to his funds

**Moral hazard:** Risk, which arises when parties have incentives to accept more risk because the costs that arise from the risk are borne, in whole or in part, by others.

**Nonbank financial institution (NBFI):** is a financial institution that does not have a full banking license and cannot accept deposits from the public. However, NBFIs do facilitate alternative financial services, such as investment (both collective and individual), risk pooling, financial consulting, brokering, money transmission, and check cashing. NBFIs are a source of consumer credit (along with licensed banks).

**Pari passu:** The situation where two or more assets, securities, creditors or obligations are treated equally and managed without preference.

**Resolution:** The disposition plan and process for a non-viable bank. It includes liquidation and depositor reimbursement, transfer and/or sale of assets and liabilities, the establishment of a temporary bridge institution and the write- down of debt or conversion to equity.

**Single Resolution Fund:** An emergency fund that can be called upon in times of crisis. It can be used to ensure the efficient application of resolution tools for resolving the failing banks, after other options, such as the bail-in tool, have been exhausted.

**Term Deposit:** A deposit that is due at the end of a fixed term. A term deposit may pay interest at a fixed rate, at a floating (variable) rate or at an index-linked rate.

**Transparency:** is frequently used to mean openness in the working of institutions. It is linked to a variety of demands for broader public access to information.

**Trust account:** A trust account is a legal arrangement through which funds or assets are held by a third party (the trustee) for the benefit of another party (the beneficiary).



# Introduction

Deposit protection for banks has been around for a while. According to the IADI report (2024), more than 146 countries/ jurisdictions have adopted deposit insurance systems to protect their banking systems. Deposit insurance has different regulations across countries, ranging from full to partial coverage, from explicit to implicit appliance, from being compulsory to non-compulsory. Deposit insurance may also differ in terms of premium implementation. The most predominant argument in favor of deposit insurance systems arises from their ability to prevent bank runs, which usually lead to asset liquidation and potentially to bank failure. By preventing losses for individual depositors, their incentive to withdraw deposits before other depositors do so is limited if a DIS is in place.

To properly design a safety net, countries need to balance two competing goals: ensuring stability in the financial system when liquidity and solvency problems arise while minimizing moral hazard. Deposit insurance is one element of the financial safety net that exists in many countries, particularly developed countries. The safety net aims to maintain the stability of the financial system by protecting the critical financial intermediation function of banks and their role in the national payments system. Deposit insurance helps ensure depositors' confidence in the financial system.

# Chapter 1

## Global Financial Safety Net

**Abstract:** GFSN refers to the global network of crisis financing instruments. The GFSN aims to maintain the stability of the financial system by protecting the critical financial intermediation function of banks and their role in the national payments system. The GFSN has a triple objective vis-à-vis sovereign governments: to provide precautionary insurance against a crisis; to supply liquidity when crises hit; and to incentivize sound macroeconomic policies. It consists of four layers: countries can self-insure against external shocks using foreign reserves or fiscal space at national level.

### 1.1 General

Financial safety-net is defined to include the functions of prudential regulation, supervision, resolution, lender of last resort and deposit insurance.<sup>1</sup> In many jurisdictions, a department of government (generally a Ministry of Finance or Treasury responsible for financial sector policy) is included in the financial safety net. The safety net aims to maintain the stability of the financial system by protecting the critical financial intermediation function of banks and their role in the national payments system.<sup>2</sup> The term GFSN refers to the global network of crisis financing instruments. This network encompasses self-insurance (reserves); bilateral arrangements (e.g., swap lines

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<sup>1</sup> Oana Croitoru, Marc Dobler, and Johan Molin (2018): Resolution Funding: Who Pays When Financial Institutions Fail? IMF Monetary and Capital Markets Department, pp. 1-28.

<sup>2</sup> Ricki Tigert Helfer (2009): What Deposit Insurance Can and Cannot Do, Finance & Development, Volume 36, Number 1, <https://www.elibrary.imf.org/view/journals/022/0036/001/article-A006-en.xml>.