



Early Intervention and Bank Resolution -The Taiwan Experience

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experience
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Early Intervention and Resolution Mechanism in Taiwan (Flowchart)

Early Intervention

Regular on-site Inspection by CDIC



Self-assistance by FIs



Off-site guidance by CDIC



On-site guidance by CDIC



Early resolution—Conservatorship

Resolution methods

- Payout
- Deposit transfer
- P&A
- Bridge bank (systemic crisis)
- OBA (systemic crisis)

Systemic crisis

If there is a concern of a systemic crisis, CDIC obtains consent of the FSC in consultation with MOF and CB, and with final approval of the Premier

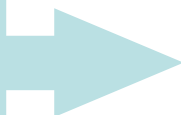


Introduction of DIS in Taiwan



Establishment of CDIC

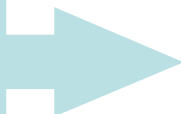
Organization



Govt-owned institution

**Jointly funded by
Ministry of Finance &
Central Bank in 1985**

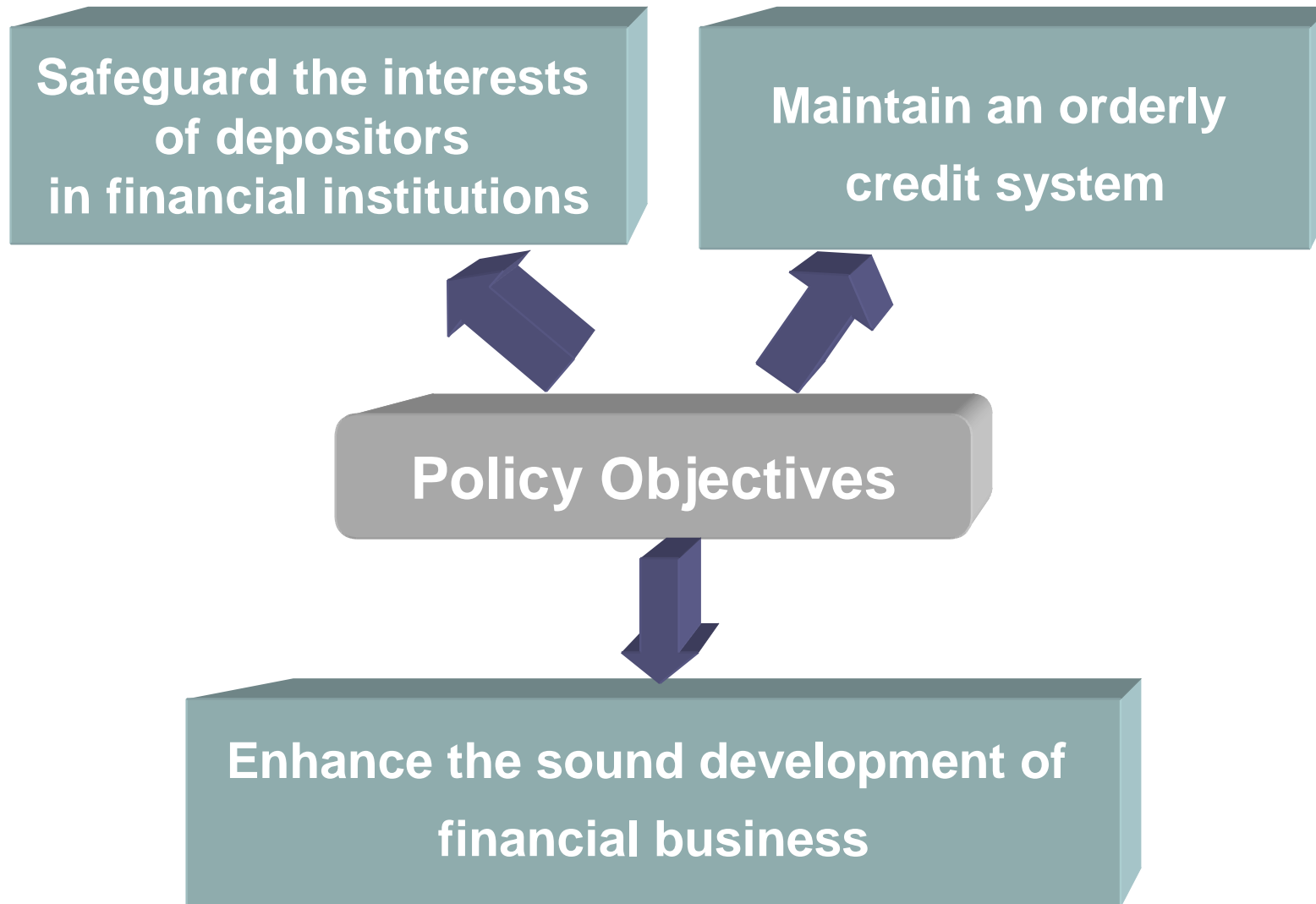
Paid-in capital



US\$ 300 million



Public Policy Objectives





Financial Safety Net Liaison System





Membership

§ Mandatory application, but subject to CDIC's on-site inspection and review

- If applying institution doesn't conform to the Approval Standard, CDIC urges it to make improvements within certain timeframe

§ Number of insured institutions

As of June 2010

Competent Authority	Types of insured institutions	No.	No. of branches
Financial Supervisory Commission	Domestic banks	37	3,285
	Local branches of foreign banks	28	132
	Credit cooperatives	26	259
	Post Co.	1	1,321
Council of Agriculture	Credit dept. of farmers' associations	274	814
	Credit dept. of fishermen's associations	25	42
Total		391	5,853



Coverage & Premium

§ Coverage

- Blanket guarantee from Oct. 2008 – Dec. 2010
- New coverage: After Jan. 2011, **NT\$ 3 million**
(about US\$94,000)

NT\$ 1.5 million (about US\$47,000)

§ Premium

- Risk-based system



Insured & Uninsured Deposits

Insured Deposits	Uninsured Deposits
<ol style="list-style-type: none">1. Checking deposits2. Demand deposits3. Time deposits4. Deposits required by law to be deposited in certain financial institutions5. Other deposits approved as insurable by the FSC (excluding interest)	<ol style="list-style-type: none">1. Foreign currency deposits2. Negotiable certificates of deposit3. Deposits from government agencies4. Deposits from the Central Bank5. Deposits from banks, trust and investment companies, credit cooperatives, and farmers' and fishermen's associations with credit departments6. Other deposits that the competent authority has approved as uninsurable such as structured deposits



Interest of deposits and foreign currency deposits to be covered from 2011 (proposal)



Legislative History of DI Act (I)

Enactment and Promulgation (Jan. 9, 1985)
Establishment of Deposit Insurance System (Sept. 1985)

First Revision (Jan. 20, 1999)
Membership from Voluntary to Mandatory

Second Revision (July 9, 2001)
CDIC (Taiwan) Commissioned by FRF
to Execute Related Missions

Third Revision (May 17, 2006)
Priority of Deposit Liabilities

Fourth Revision (Jan. , 2007)



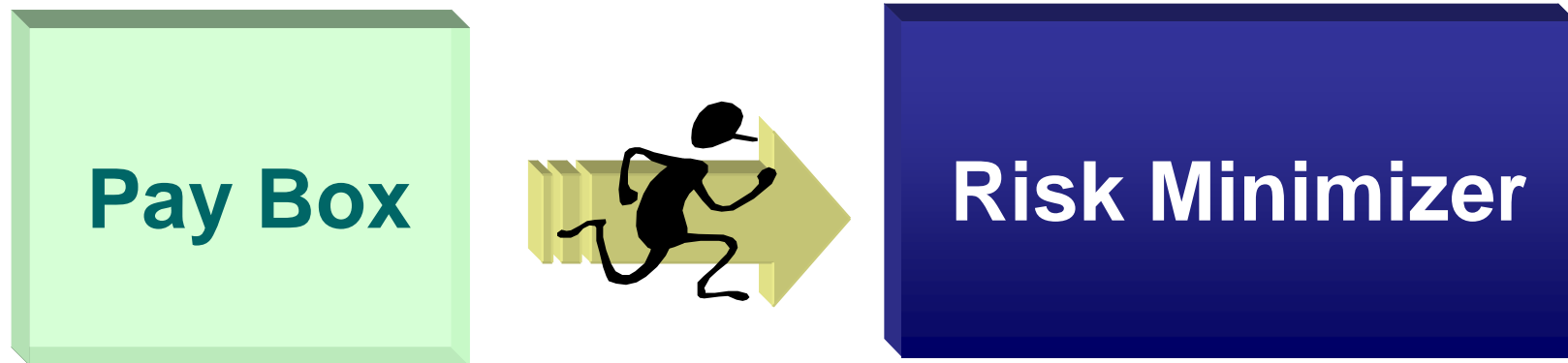
Legislative History of DI Act (II)

Fourth Revision (Jan. 2007)

- Reinforce the replenishment of DIF
- Strengthen risk control
- Enhance ways to fulfill insurance responsibilities
- Establish mechanism for handling systemic crises



Role of Deposit Insurance

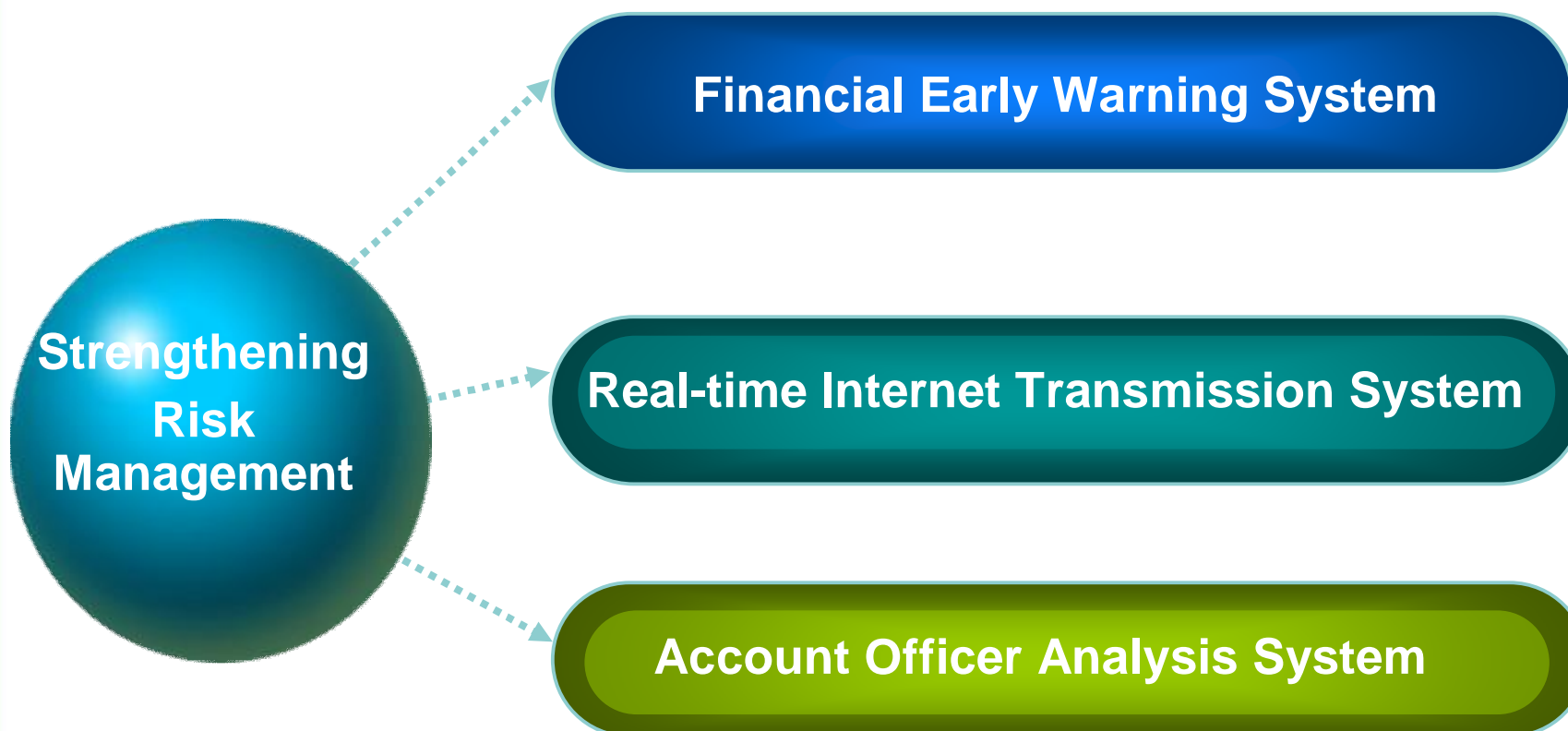




Early Intervention and Risk Management



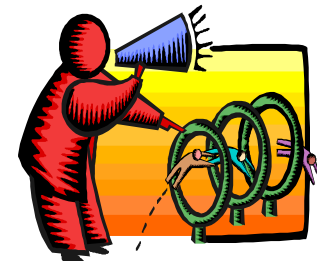
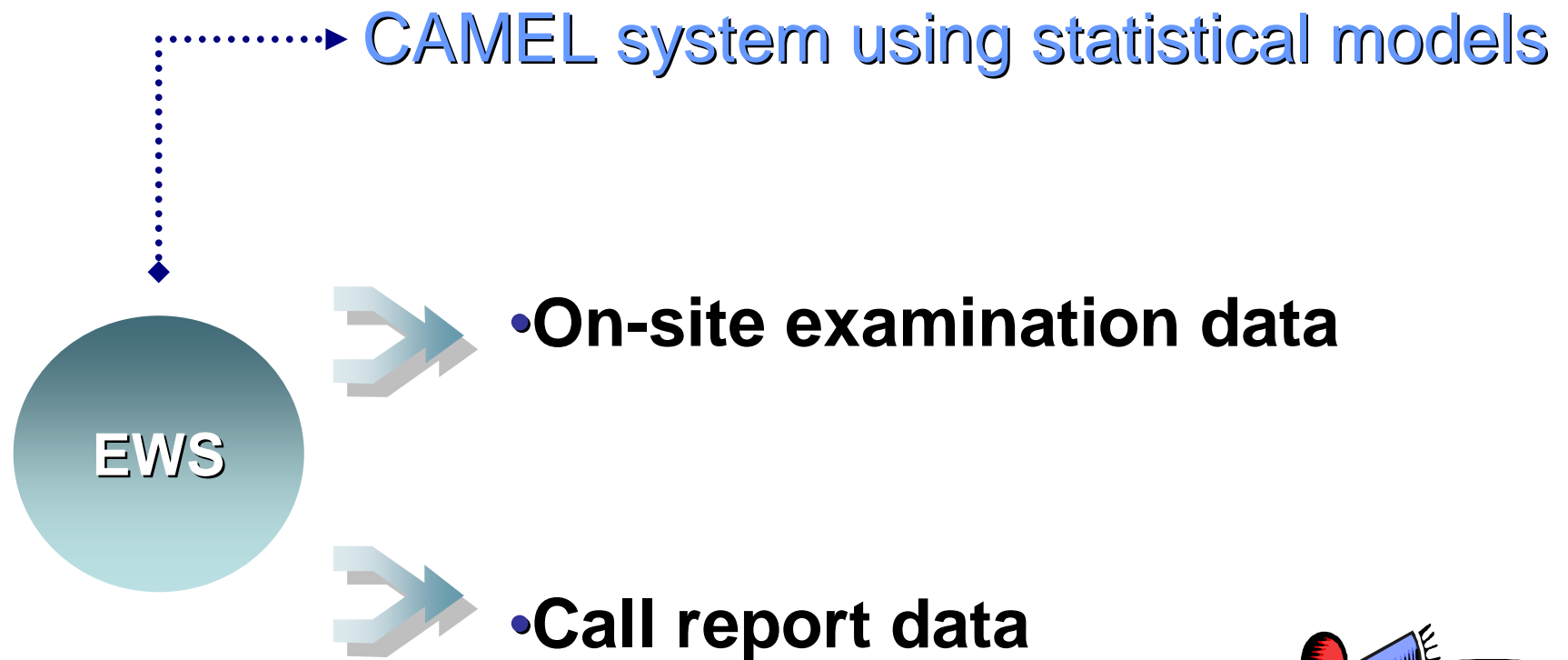
Risk Management Mechanisms



*** Warning of Deposit Insurance Contract Termination**



Financial Early-warning System (EWS)





Data collection and sharing (I)

**Information
Sharing**

Mechanism established by
financial safety net participants

**If data
insufficiency**

CDIC may require
Insured institutions
to provide additional information



Data Collection and Sharing (II)

§Additional information required by CDIC

- **Example:**

In normal times

When

- FI's investment positions generate losses
- FI highly concentrates on construction or mortgage loans, or loans to interested parties

For making transition smooth

FI is required to submit contingency plan for liquidity risk to CDIC when:

- Inappropriate deposit structure
- Maturity mismatch between assets & liabilities
- Poor funding capacity



Real-time Internet Transmission System

- § Financial institutions transmit major financial information to CDIC on a daily basis
- § CDIC can promptly discover and respond to warning signals
- § Case:
 - In 2008, detection of operational abnormalities in deposits at some private commercial banks





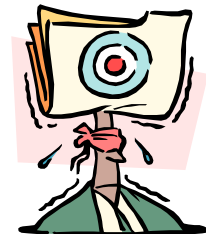
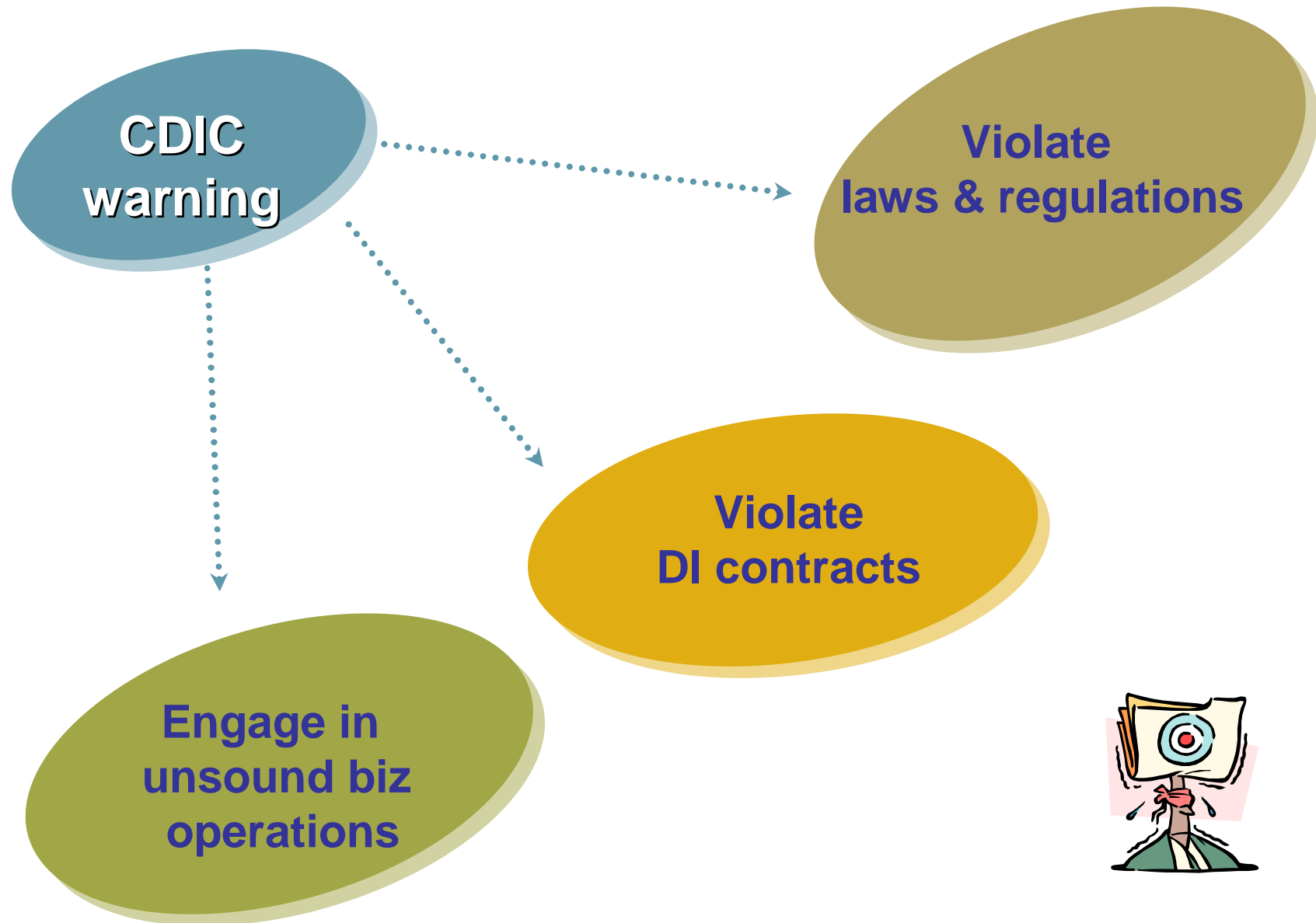
Account Officer System

- § CDIC dispatches personnel to further monitor the operational condition of financial institutions
- § Close coordination with competent authority





Warning of DI Contract Termination



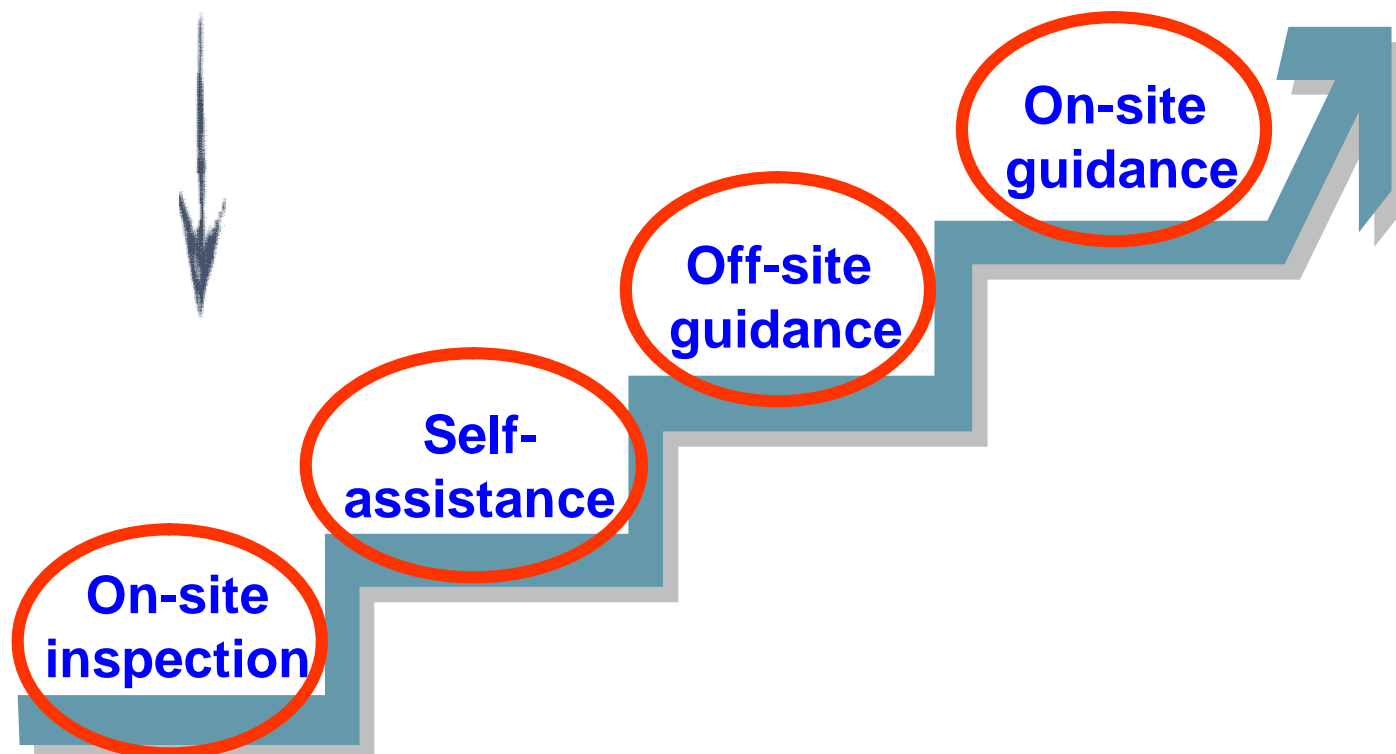


Steps of Early Intervention

Ongoing Risk Management



Conservatorship





On-site Inspection

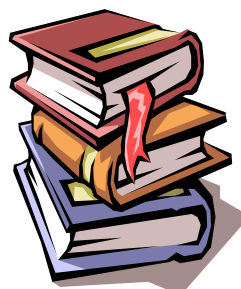
- § Any event causing termination of deposit insurance contract
- § Assets and liabilities of insured institutions before bank closure
- § Properties of employees of failed insured institutions, who violate the laws, to pursue civil liabilities
- § Accuracy of deposit assessment base and content of electronic data files





On-site Inspection of Electronic Data Files

Legal basis

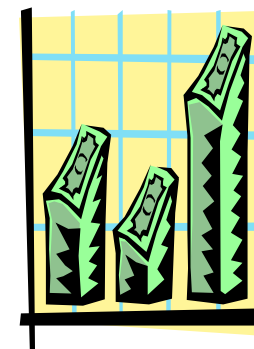


§ *Deposit Insurance Act*

- FIs are required to set up e-data files based on CDIC's format

Electronic Data Files
- 7 categories with 25 types of data

Inspection emphasis



- File format
- Data type
- Data content



Self-assistance & Off-site Guidance Mechanisms

§ Self-assistance by problem financial institutions

- Recapitalization or self-improvement plan

§ Off-site guidance by CDIC

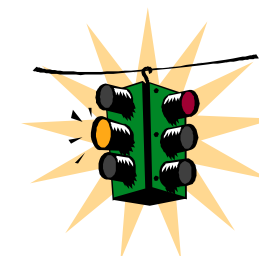
- Ask financial institution to provide related data
- Attend board of director meetings and other important meetings
- Review meeting resolutions and minutes
- Assist in speedy completion of capital reduction, recapitalization or consolidation plans





On-site Guidance

- **CDIC dispatches officers to provide on-site guidance to closely monitor:**
 - Business operations
 - Corporate governance
 - Internal controls
 - Problem institution's capital restructuring
- **Intervention as early as possible**





Quiz 1



Overview of Taiwan's Bank Resolution Experience



Taiwan's Bank Resolution Experience

§ Before deposit insurance system in place:

- Policy/administrative direction and persuasion by the government
- Government-owned bank as the 1st choice of the acquirer

§ In the period of voluntary DIS 1985-1999:

- Non-members of CDIC:
 - Assumed through government administrative persuasion; acquirers assumed the loss
- Members of CDIC: Handled according to the *Deposit Insurance Act*; no failure cases during this period

§ In the period of compulsory DIS in 1999 ~ 2001:

- CDIC provided financial assistance for purchase and assumption after 1999

§ No market mechanism before 2001





Establishment of Financial Restructuring Fund (FRF)

§ Background of FRF

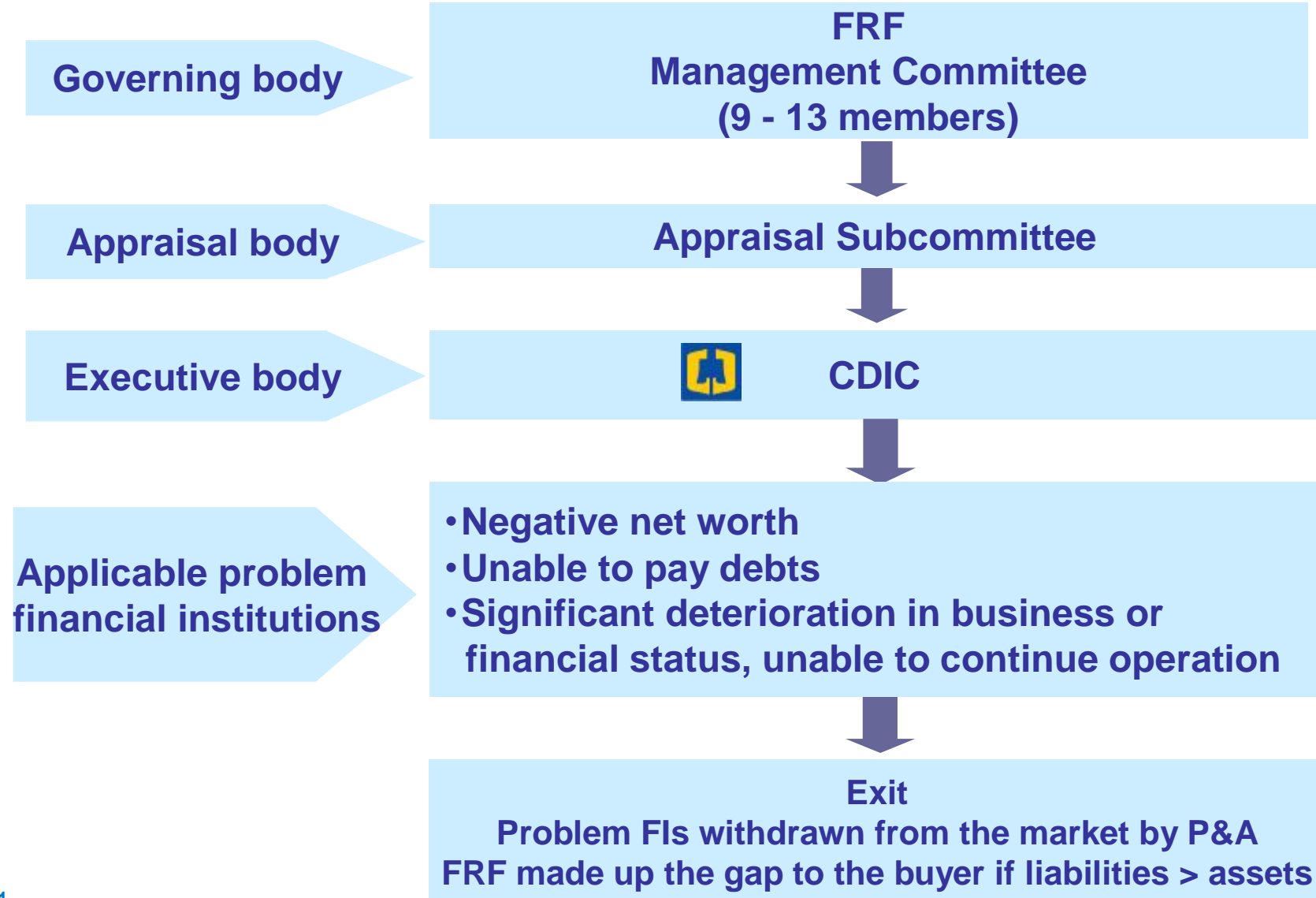
- Recession of real estate market in the 1990's
- Economy recession worsened by the 1997 Asian Financial Crisis
- Shocks of earthquake in 1999
- Growing NPLs
- Rampant rumors of a systemic financial crisis

**July
2001**

**Government appropriated US\$ 7.6 billion
to provide blanket guarantee for bank resolution**

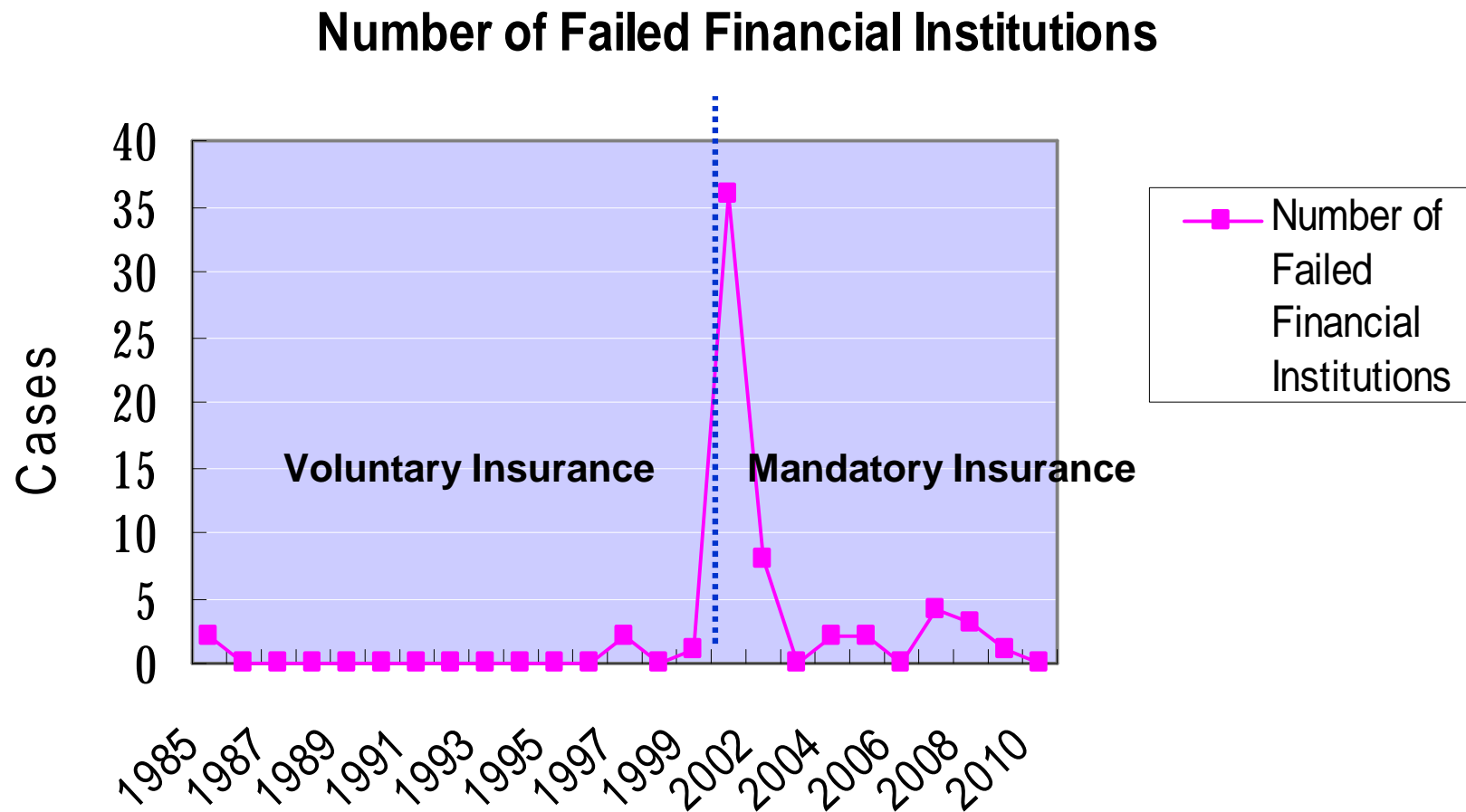


Resolution Methods under FRF





Number of Failed Financial Institutions





Early Banking Resolution

Ongoing Risk Management



On-site inspection

Self-assistance

Off-site guidance

On-site guidance

Conservatorship





Early Banking Resolution - Conservatorship

Banking Act

amended in Dec. 2008:

PCA mechanism

Standard for market withdrawal:
Capital adequacy (BIS) ratio

If BIS ratio < 2%,
the bank to be put under
conservatorship within 90 days

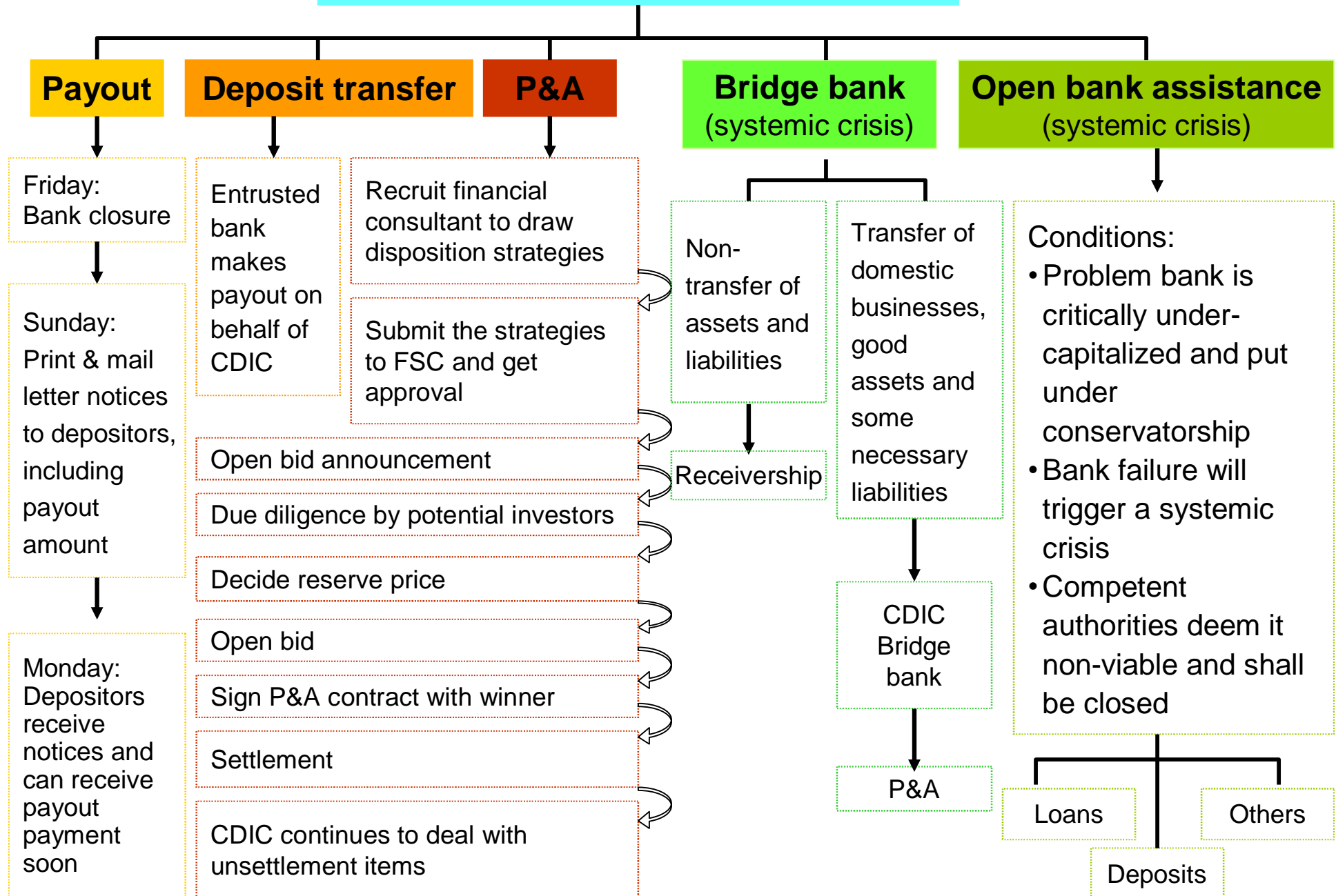
Banking Act

Bank should also be
taken over

In case a bank:

- Is unable to pay its liabilities and could harm depositors' interests; or
- Has losses exceeding 1/3 of capital and bank cannot make improvement within the stipulated timeframe

Resolution methods

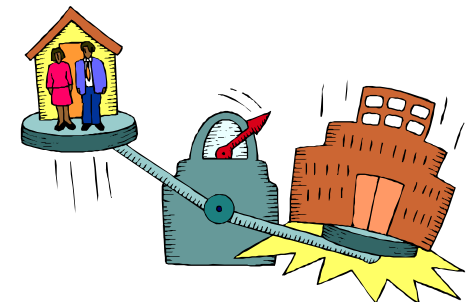




Purchase and Assumption (I)

Purchase & Assumption

P & A is a resolution transaction in which a healthy institution or group of investors purchases some or all of assets and assume some or all of the obligations of a failed or failing financial institution.





Purchase and Assumption (II)

Year	Banks	Credit Coop.	Credit departments of farmers' & fishermen's associations	Methods
1999		1		Whole bank P&A
2001		7	29	Whole bank P&A
2002		1	7	Whole bank P&A
2004	1	1		Whole bank P&A and Partial P&A
2005	1		1	Whole bank P&A and Partial P&A
2007	3		1	Whole bank P&A and Partial P&A
2008	3			Partial P&A and P&A with put back option
2010	1			Partial P&A
Subtotal	9	10	38	
Total	57			



Benefits of Purchase & Assumption

§ Benefits

- For a failed bank and its depositors
 - Financial services of a failed bank are less interrupted compared to a payout
- For a deposit insurer
 - Meeting least cost principle in most cases
 - Preserving confidence in financial system
- For an acquiring financial institution
 - A great opportunity for expanding its business and market share



Considerations of Purchase & Assumption

§ Considerations

- No suitable buyers
- Dilemma:

Fast disposition without optimizing asset values

VS.

Maximize asset recovery





General Procedures of Conducting P&As

§ Outsourcing services of professional financial and legal consultants

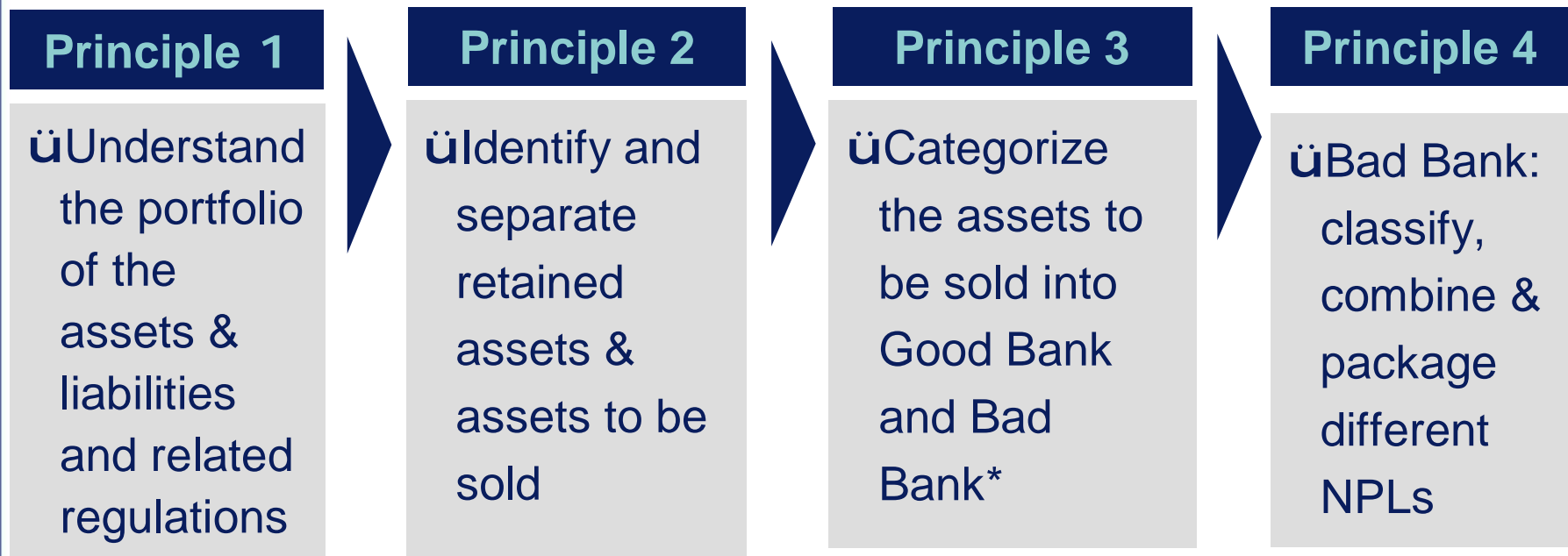
- Disposition plans
- Assets & liabilities valuation
- Open bidding processes
- Due diligence
- Real estate appraisals
- Legal issues, tax planning and employee settlement plans





Proposed Disposition Plan for Failed Banks (I)

Objective: To maximize the successful rates of open bid through the well-designed package of the assets, liabilities and operations



* “Good Bank” includes assets and liabilities, excluding NPLs and retained items

“Bad Bank” consists of NPLs and certain real estate



Proposed Disposition Plan for Failed Banks (II)

Failed Banks	Good Banks	Bad Banks		other
Biz Bank	1 Batch	Corporate Accounts		-
		Consumer Accounts		
CS Bank	1 Batch	Batch 1	Corporate Accounts	-
			Consumer Accounts	-
		Batch 2	Tranche 1	-
			Tranche 2	-
			Tranche3	-
T Enterprise Bank	1 Batch	Tranche A		-
		Tranche B (Credit card & cash card)		-
		Tranche C (Credit card & cash card)		
CH Bank	1 Batch	Tranche A		-
		Tranche B (Credit card & cash card)		
		Tranche C (Credit card & cash card)		



Proposed Disposition Plan for Failed Banks (III)

Failed Banks	Good Banks	Bad Banks	Other
C Trust & Investment Corp.	1 Batch	Specific NPLs	ÿ To dispose real estate through individual auctions
BW bank	1 Batch	Tranche A	-
		Tranche B (Credit card & cash card)	
A Trust & Investment Corp.	Tranches A	Tranches A	-
	Tranches B	Tranches B	-
CF Bank	Tranche 1 (Local branch)	Tranche A	ÿ To dispose antiques through individual auctions
	Tranche2 (Local branch)	Tranche B	
	Tranche 3 (Overseas branch)	Tranche C (Credit card & cash card)	
	Tranche 4 (Credit card business)	Tranche D (Credit card & cash card)	



Proposed Disposition Plan for Failed Banks (IV)

§ Provide incentives to entice potential buyers

- Branches relocation without any restrictions
- Upgrade branches offering only deposit and withdraw services to full function branches
- If BIS < 8% after merge, acquiring bank is allowed to meet the min. 8% BIS ratio with a grace period



Buyers Qualification: Good Bank

§ Types of buyers

- Domestic & foreign Banks
- Domestic & foreign financial holding companies without banks
- Other legal entities under *Company Law* w/certain financial strength and with capacity of running a bank

§ Financial strength

- **Total asset value** should reach NT\$150billion (US\$4.9 billion)

ÿ Net book value

- Banks should exceed NT\$10billion (US\$ 327 million)
- Financial holding companies should exceed NT\$ 20 billion (US\$654 million)

ÿ **BIS ratio** should maintain at 8% or above



Buyers Qualification: Bad Bank

§ Types of buyers

• Domestic or foreign asset management companies

(Article 15 of *the Financial Institutions Merger Act*)

• No any illegal records

• CDIC reserves the rights to reject any buyers to participate in open bid



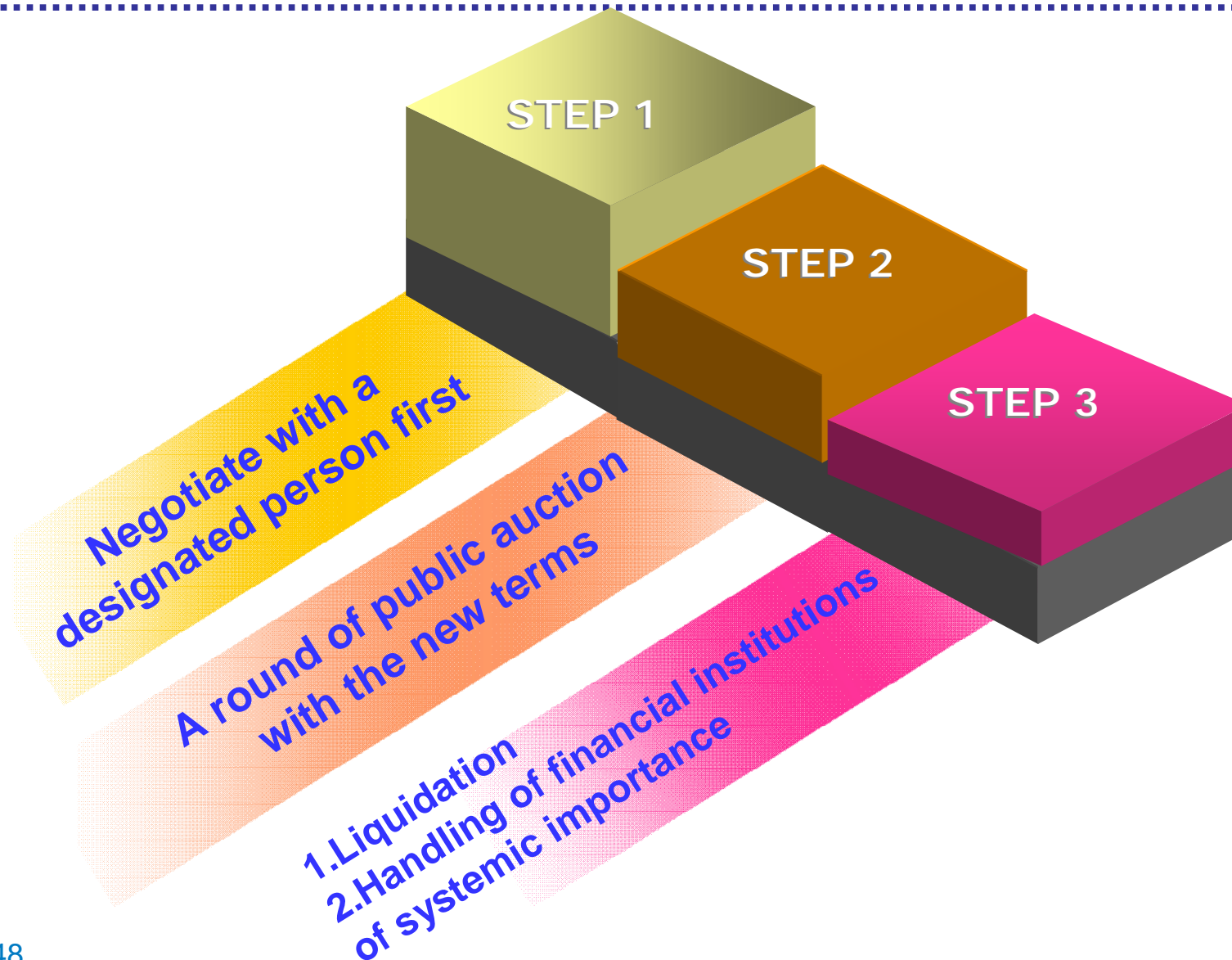


Timelines for Purchase & Assumption





Procedures after a Failed Open Bid





Key to Facilitate P&A – External Factors

- § Overall economic and financial market conditions need to be considered**
- § Benign economic and financial conditions would greatly increase the success rate of P&A transactions**



Key to Facilitate P&A – Internal Factors (I)

- § Well-designed disposition plan
- § Reserve price determination in the “Good Bank” and the “Bad Bank” transactions
- § Flexibility and adaptability to market needs
- § Case 1:

A failed bid due to lack of buyer participation



Adjusting the bidding strategy and incorporating a “loss-sharing put back option” in a bid



Key to Facilitate P&A – Internal Factors (II)

§ Case 2:

To max.
recovery
and
reduce
resolution
cost

segmenting a
good real
estate building
from the Good
Bank

Building
sold at a
high price

Resulting
in no loss
to CDIC

§ Case 3:

Maximizing
asset
recovery is
not always
the case

Chinese
antiques
are
different
from other
assets

National
museums
are the
priority
buyers
among
others

These antiques
sold to national
museums
directly with
relatively lower
prices



Key to Facilitate P&A – Internal Factors (III)

§ Flexibility





Key to Facilitate P&A – Internal Factors (IV)

§ Employees' rights and interests

- To give a pension and severance pay to the employees according to the *Labor Standards Law*
- To request the investor to rehire more than 50% of the employees for at least one year
- To convince the investor to compensate for employees' losses caused by the severance of their working years



Key to Facilitate P&A – Internal Factors (V)

Financial consultants appraise the value of the problem banks as reference



CDIC reviews the appraisal provided by financial consultants

FRF Appraisal Subcommittee reviews the appraisal

FRF Management Committee decides the benchmark price
Final price decided by an open bid



Key Challenges - Cross Border Issues

§ Lesson learned



Y Close coordination with financial safety net players in other countries

- CDIC took over one problem bank with overseas branches in 2008
- 1st resolution case in Taiwan involving cross border issues

**During
handling
process**

CDIC with FSC kept communicating with financial supervisors of the other country

Finally

Overseas branches were sold successfully by an open bid



Key Challenges – Retained Assets

Hillside land



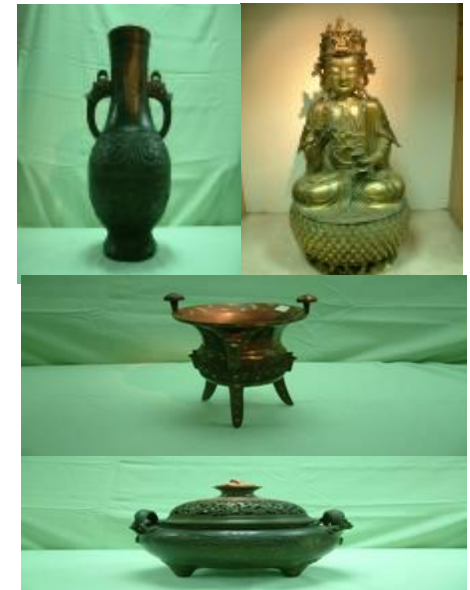
Hotel



Taipei 101



Chinese antiques





Quiz 2



Mechanism for Handling Systemic Crises

§ Deposit insurance mechanism is not to deal with a systemic financial crisis

- But deposit insurance plays an important role in maintaining financial stability

§ Two resolution methods for handling systemic crises

- Open bank assistance
- Bridge bank



§ If fund insufficient, collections of special premiums



Open Bank Assistance (I)

§ OBA

- A distressed bank resolution method
- A failing insured institution receives financial assistance before closure in the form of a cash or non-cash financial assistance to prevent its failure or enable it to smoothly exit from the market





Open Bank Assistance (II)

§ Conditions

- Problem bank is critically under-capitalized
- Problem bank must be put under conservatorship
- Failure of the problem bank will trigger a systemic financial crisis
- Competent authorities deem it non-viable and shall be closed
- Full collateral to CDIC provided by financial holding company that the problem bank belongs to



Open Bank Assistance (III)

§ Ways of OBA

- Loans
- Deposits
- Other types of financial assistance such as providing guarantee





Open Bank Assistance (IV)

§ Documents submitted by problem institution

- Liquidity demand analysis and evaluation of assets and liabilities of the institution
- Full collateral agreement in the minutes of the Board of the Directors' meetings of the problem bank's parent financial holding company
- Other related information requested by CDIC

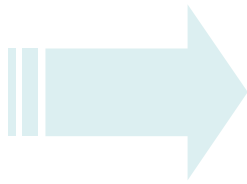




Open Bank Assistance (V)

§ Reasons for change

- Before Deposit Insurance Act amended in 2007, CDIC could also provide OBA in a normal bank failure case
- However,
 - OBA may allow shareholders of problem bank to benefit disproportionately
 - Use of OBA may turn out higher resolution cost due to the delay of closure
 - Collateral provided by problem bank had low disposition value-time and manpower consuming & cost ineffective



**After Deposit Insurance Act amended in 2007,
OBA is only provided under a systemic crisis**



Conclusion and Future Perspectives



Conclusion and Future Perspectives (I)

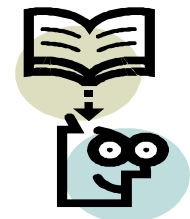
§ Amending the *Deposit Insurance Act*

1st stage

- Increasing coverage limit and expanding the scope of coverage

2nd stage

- Reinforcing risk management
- Strengthening resolution mechanism for dealing with failing financial institutions





Conclusion and Future Perspectives (II)

§ Reinforce risk management

- Formal authority to evaluate the assets and liabilities of the problem financial institutions





Conclusion and Future Perspectives (III)

§ Strengthening resolution mechanism for dealing with failing financial institutions

- To receive the authority by laws to enter a failing bank in a confidential manner and prepare for bank resolution before it is closed





Conclusion and Future Perspectives (IV)

§ Replenishing deposit insurance fund

- Deposit insurance fund is in deficit now
- Solutions
 - Bank business tax revenue to be injected into the Fund starting from 2011
 - CDIC has drafted a proposal to raise the premium rates starting from 2011 to achieve the 2% target ratio







Thank You!

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Q & A