

# **Annual IADI Africa Regional Committee Conference**

## **The Role of Deposit Insurance in Maintaining Financial Stability The Taiwan Experience**



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# Where is Taiwan?





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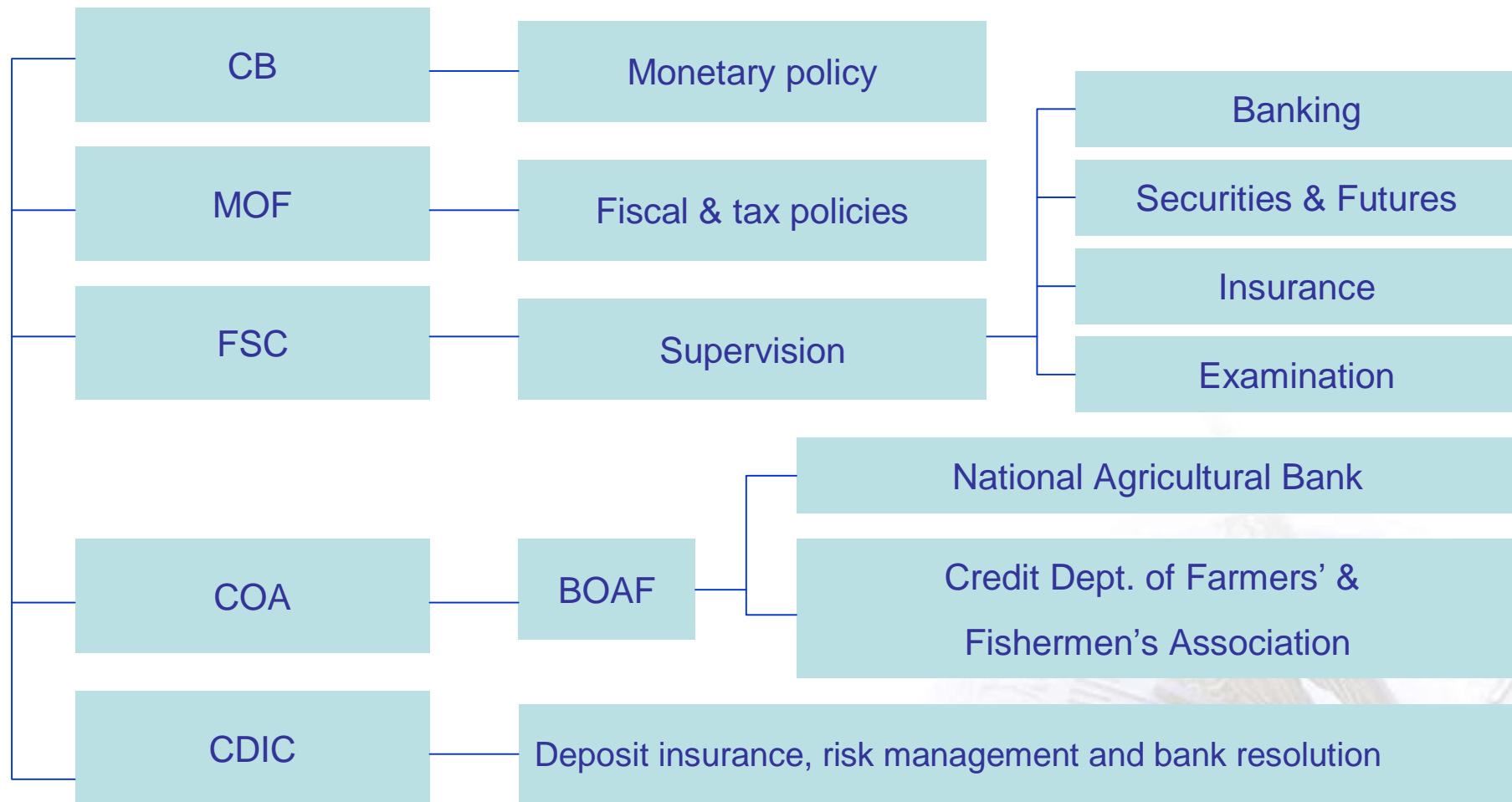
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- I. Financial Safety Net in Taiwan
- II. Major Features of The Deposit Insurance System (DIS)
- III. Taiwan's Current and Unwinding Situation of Implementation of Temporary Blanket Guarantee and Unwinding Measures with Response to the Financial Crisis
- IV. Conclusion



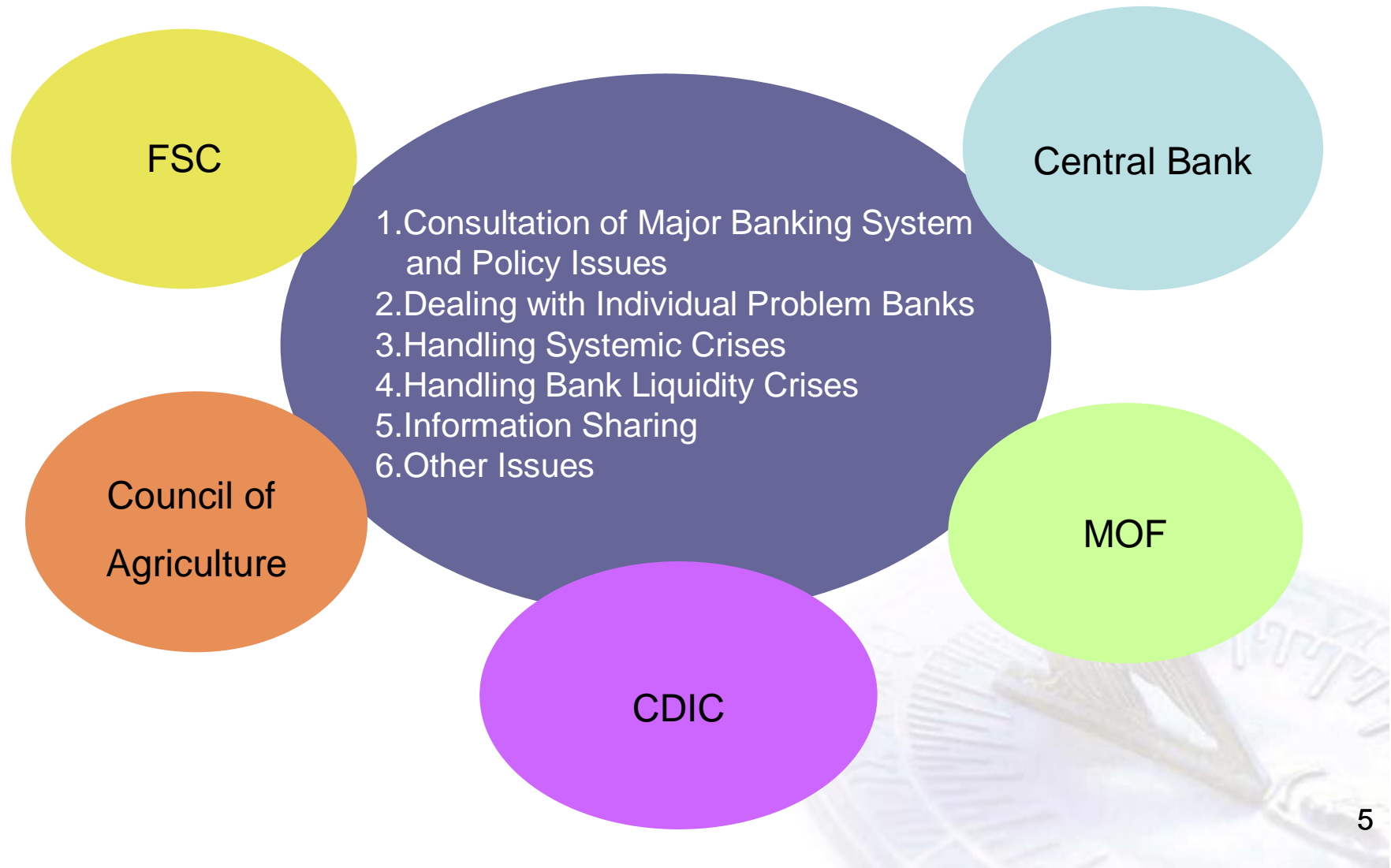


# I. Financial Safety Net in Taiwan





# Financial Safety Net Liaison System





## II. Major Features of The DIS

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- 1. Background
- 2. Vision and Objectives
- 3. Membership
- 4. The limit and scope of Coverage
- 5. Funding Sources





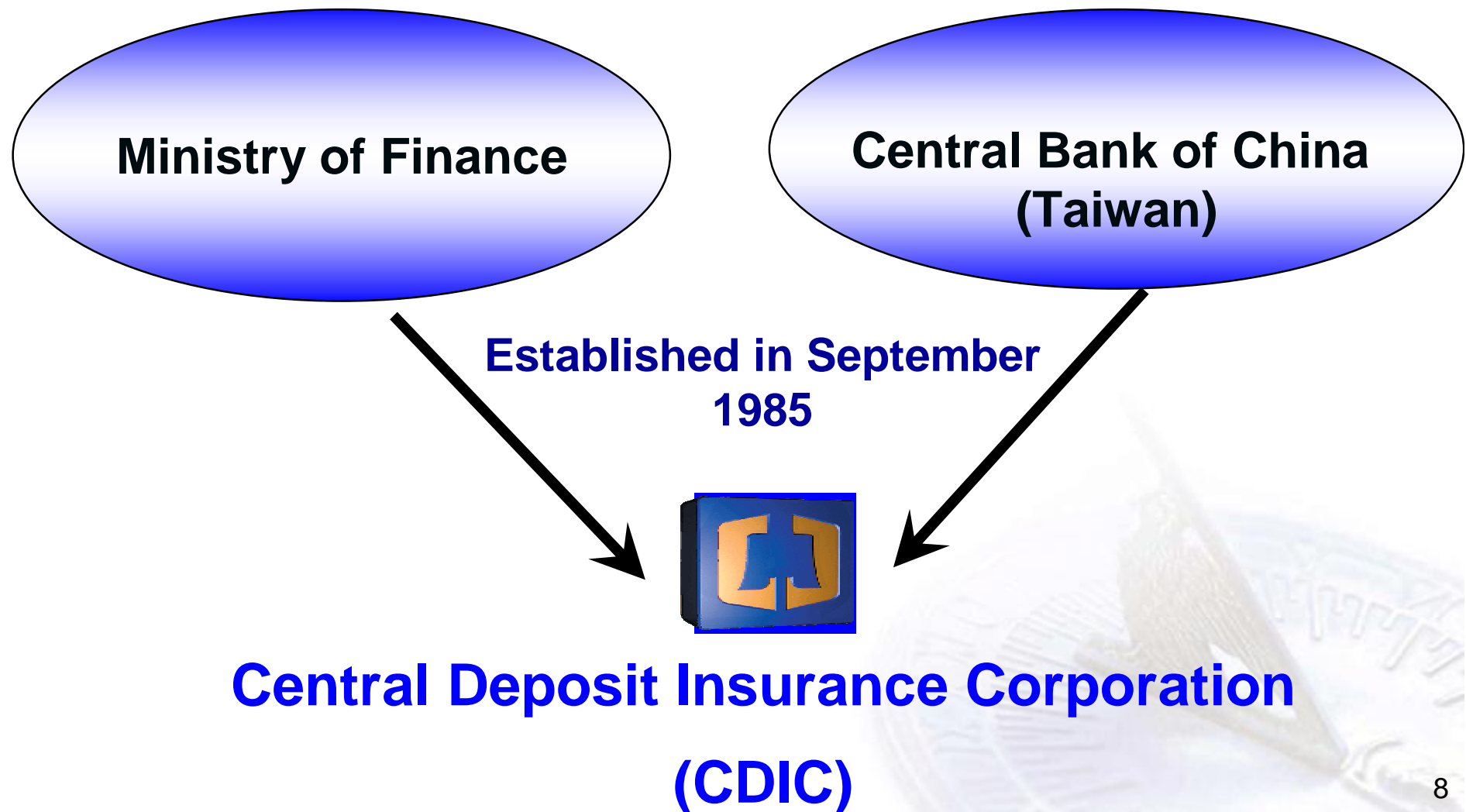
## II. Major Features of The DIS

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- 6. Risk Management Mechanisms
- 7. Premium
- 8. Authorities of Conducting Special Inspection and Investigation
- 9. Early Intervention and Bank Resolution
- 10. Mechanism for Handling Systemic Financial Crisis



# 1. Background

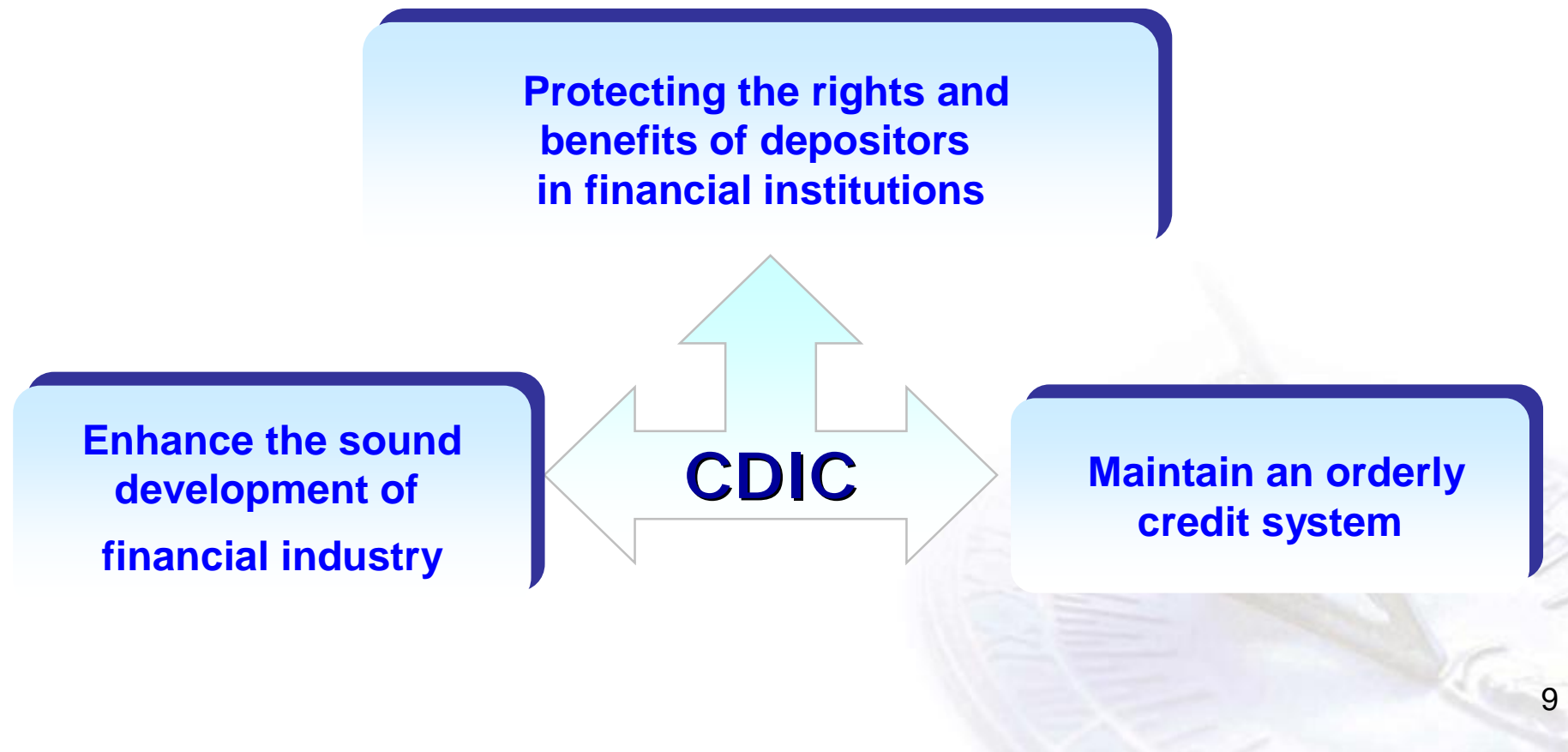






## 2.Vision and Objectives

**Exerting functions of deposit insurance system to ensure financial stability**





### 3. Membership

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**Voluntary participation (Sept. 1985 – Jan. 1999)**

**Compulsory system (Since Jan. 1999)**



**Mandatory application (since Jan. 2007)  
but subject to CDIC's approval**



# Number of insured institutions

As at 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



## 4. The limit and scope of Coverage



**NT\$0.7 million (US\$17,500, September 1985)**

**NT\$1 million (US\$30,000, August 1987)**

**Temporary blanket guarantee on the deposits in unsound Financial institutions (July 2001- July 2005)-Era of Financial Restructuring Fund**

**Resume to NT\$1 million (July 2005)**

**NT\$1.5 million (US\$49,000, July 2007)**

**In response to financial tsunami by providing temporary full coverage (October 7, 2008 ~ December 31, 2010)**



# Insured & Uninsured Deposits

Insured Deposits	Uninsured Deposits
<ol style="list-style-type: none"><li>1. Checking deposits</li><li>2. Passbook deposits</li><li>3. Time deposits</li><li>4. Deposits required by law to be deposited in certain financial institutions</li><li>5. Other deposits approved as insurable by the FSC</li></ol> <p>(excluding interest)</p>	<ol style="list-style-type: none"><li>1. Foreign currency deposits</li><li>2. Negotiable certificates of deposit</li><li>3. Deposits from government agencies</li><li>4. Deposits from the Central Bank</li><li>5. Deposits from banks, trust and investment firms, credit cooperatives, and farmers' and fishermen's associations with credit departments</li><li>6. Deposits exceeding the per-institution maximum insurance coverage established for each depositor</li><li>7. Structured deposits</li></ol>

- Employee Pension Accounts insured separately



## 5.Funding Sources

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**Capital**

**Assessment Income**  
- Semiannual Assessment  
- Special Assessment

**Business tax revenues  
from FIs after 2011**

**Investment Income**

**Emergency liquidity needs: CB & other FIs**



# Deposit Insurance Funds

**DI Fund target ratio: 2%**

**Two Separate Deposit Insurance Funds**

**BDIF**

**for Banking Financial Sector**

**Current ratio: 0**

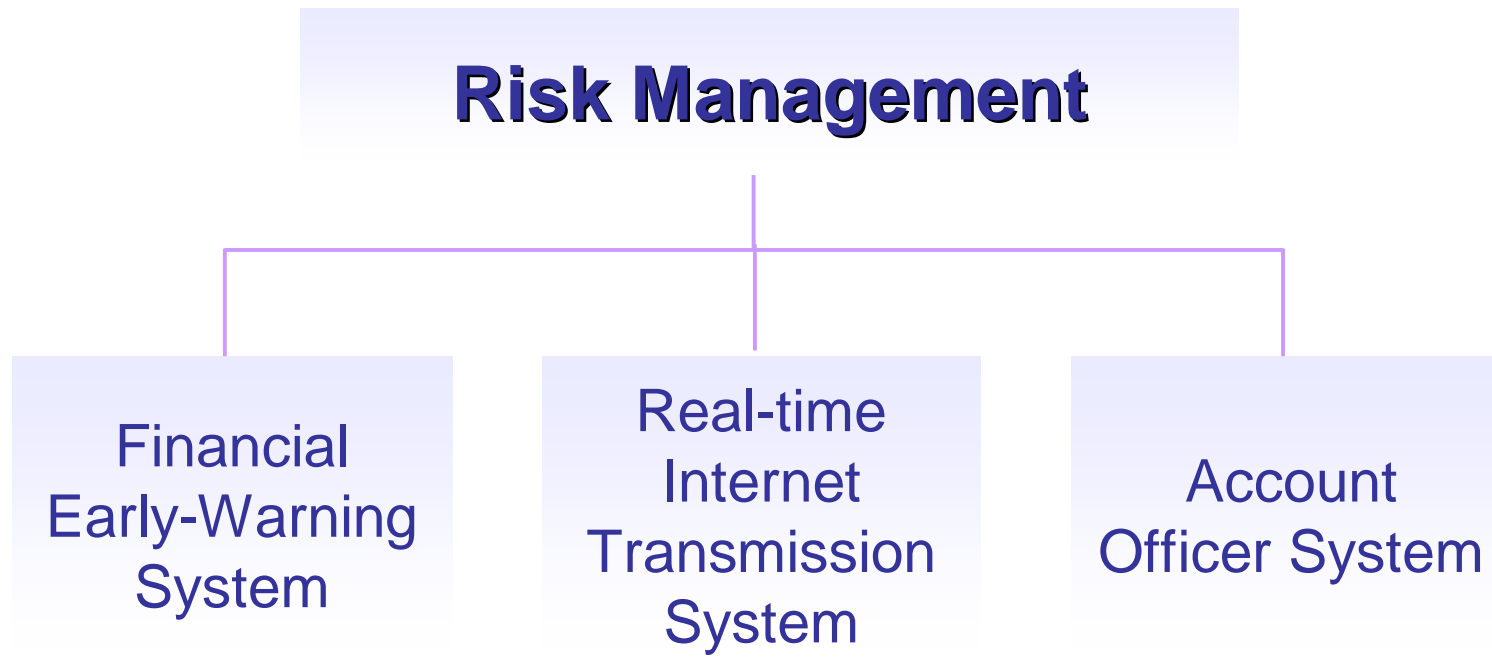
**ADIF**

**for Agricultural Financial Sector**

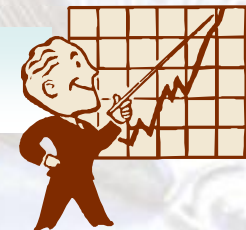
**Current ratio: 0.25%**



## 6. Risk Management Mechanisms



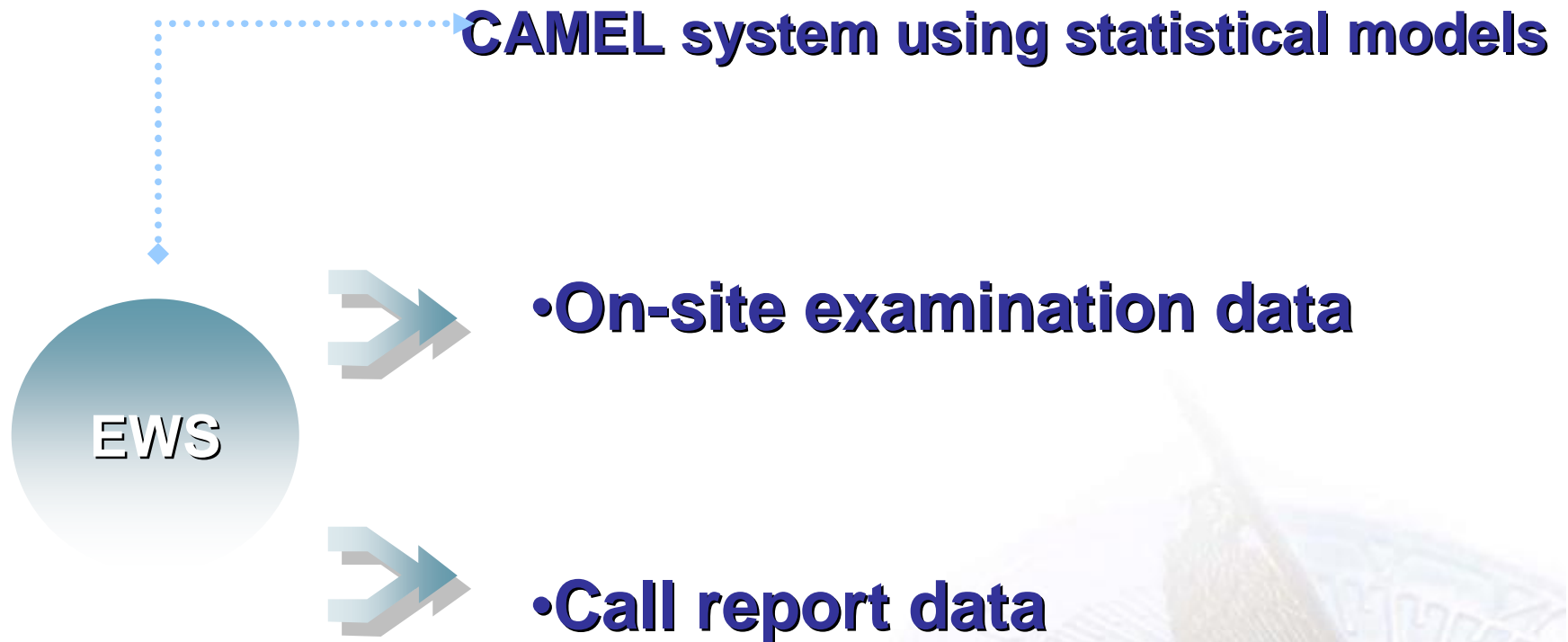
\* Warning of Deposit Insurance Contract Termination







# Early-Warning System (EWS)





# 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





# Account Officer System

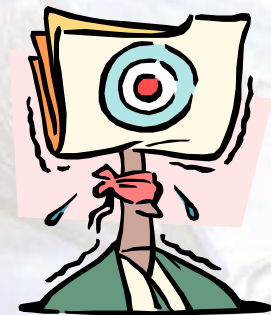
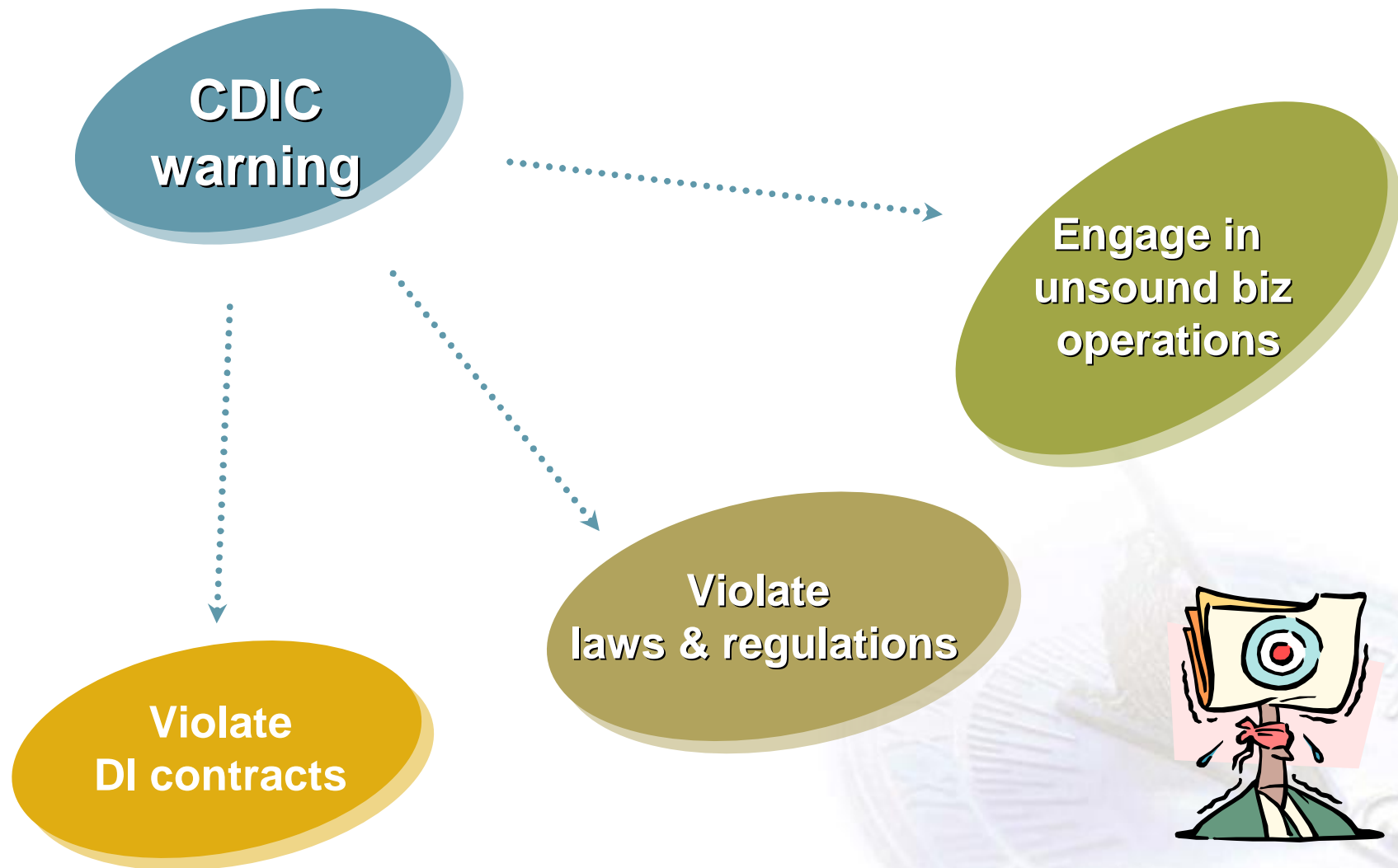
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- CDIC dispatches personnel to further monitor the operational condition of financial institutions
- Close coordination with competent authority





# Warning of DI Contract Termination





## 7. Premium

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**Flat-rate system**

**Risk premium**  
(since July 1, 1999)

**Risk indicators**

- **Capital adequacy ratio**
- **Composite score of Examination Data Rating System**



# **Reasons Implementing Risk Premium**

**1. Complement measures of mandatory DIS**

**2. Mitigate moral hazard and increase market discipline**

**3. Reasonably reflect risk level of insured institutions**

**4. Facilitate fairness of premium system**



# Adjustments of Premium Rate Levels

**Sep. 1985**      **Flat Rate System**  
0.05% of Covered Deposit



**July 1987**      **Flat Rate System**  
0.04% of Covered Deposit



**Jan. 1988**      **Flat Rate System**  
0.015% of Covered Deposit

★**Jan. 1999**      **Making Deposit Insurance System Compulsory**



**July 1999**      **Risk-Based Premium System**  
0.015%, 0.0175% and 0.02% of Covered Deposit



**Jan. 2000**      **Risk-Based Premium System**  
0.05%, 0.055% and 0.06% of Covered Deposit



**July 2007**      **Modification of the Risk-Based Premium System**  
Widen tier rates and spreads



# The Expansion of the Levels of Tier Rates

< 9 risk groups & **3** tier rates >

Capital Adequacy	Composite Score		
	A	B	C
Well Capitalized	First Tier Rate	First Tier Rate	Second Tier Rate
Adequately Capitalized	First Tier Rate	Second Tier Rate	Third Tier Rate
Undercapitalized	Second Tier Rate	Third Tier Rate	Third Tier Rate



< 9 risk groups & **5** tier rates >

Capital Adequacy	Composite Score		
	A	B	C
Well Capitalized	First Tier Rate	Second Tier Rate	Third Tier Rate
Adequately Capitalized	Second Tier Rate	Third Tier Rate	Fourth Tier Rate
Undercapitalized	Third Tier Rate	Fourth Tier Rate	Fifth Tier Rate





# Premium Rates



Type of Financial Institutions	Below Max. Coverage	Above Max. Coverage
Commercial Banks, Investment & Trust Companies, Local Branches of Foreign Banks and Credit Cooperatives	0.03%, 0.04%, 0.05%, 0.06% <b>and</b> 0.07% <b>of covered deposit</b>	0.0025% (0.005% after Jan. 2010 ) <b>of insurable deposit</b>
Credit Departments of Farmers' & Fishermen's Associations	0.02%, 0.03%, 0.04%, 0.05% <b>and</b> 0.06% <b>of covered deposit</b>	0.0025% <b>of insurable deposit</b>



## **8. Authorities of Conducting Special Inspection and Investigation**

**Accuracy of deposit assessment base and content of electronic data files**

**Any event causing the termination of DI agreement**

**Assets and liabilities of insured institutions prior to the fulfillment of insurance responsibilities**

**Property information and information needed to pursue civil liabilities for illegal acts or omissions by employees of failed insured institutions**



## 9. Early Intervention and Bank Resolution





## **9. Early Intervention and Bank Resolution**

- **(1) Early Intervention**
- **a. Self-assistance by problem financial institutions**
- **b. Off-site guidance mechanism**
- **c. On-site guidance for problem financial institutions**





## d. 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

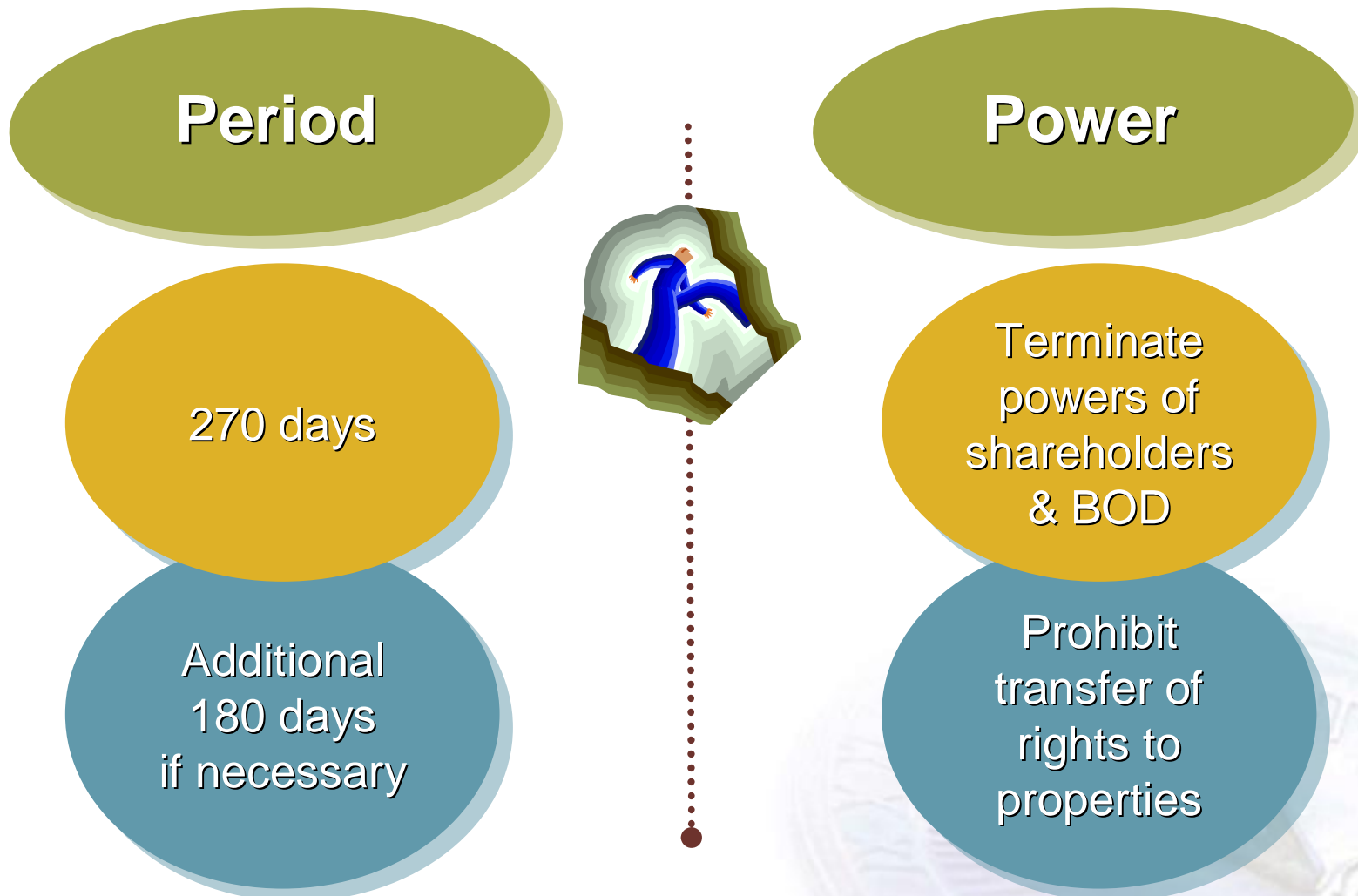
***Banking Act***  
Bank should also be  
taken over

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 does not make improvement within the stipulated timeframe



## d. Conservatorship





## d. Conservatorship

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### Authorities & Duties of CDIC Conservatorship Team

- **Operations and Property Management of the Problem Financial Institution**
- **Executing the Rights in Litigious and Non-Litigious Proceedings.**





## (2)The Resolution Methods

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**Straight pay-out**

**Deposits transfer**

**Purchase and Assumption( P&A)**

**Bridge bank (in response to the systemic crisis)**

**Open bank assistance (in response to the systemic crisis)**





# Market Withdrawal Procedures

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1

Professional financial consultancy to assist with appraisal and provide advice

2

Appraisal subcommittee to review appraisal result

3

Final auction amount through an open bid





## **10. Mechanism for Handling Systemic Financial Crisis**

- CDIC can reimburse the depositors above the coverage limit, if CDIC obtains consent of the FSC in consultation with ,CBC and with approval of the Executive Yuan
- CDIC's handling a systemic financial crisis causes the DI fund insufficient, CDIC can collect a special premium from the insured institutions.



### **III. Taiwan's Current and Unwinding Situation of Implementation of Temporary Blanket Guarantee in response to the Global Financial Crisis**

- **1. The Periods within the Establishment of Financial Restructuring Fund**
- **2. The Global Financial Crisis in 2008**
- **3. Implementation Results**
- **4. The CDIC Enforces Risk Control in Conjunction with Supporting Measures for Financial Supervision**





# 1. Establishment of Financial Restructuring Fund (FRF)

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- **FRF in 2001 NT\$ 250 billion (US\$ 8 billion)**
  - **Four-year blanket guarantee provided**
  - **56 problem financial institutions withdrawn from the market through P&A method**
  - **average non-performing loan ratio came in at 1.5%, BIS ratio at 11.4%, the liquidity reserve ratio at 21%, and coverage ratio at 68% at the end of 2008**





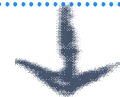
## 2.The Global Financial Crisis in 2008

### § Temporary blanket guarantee adopted to maintain public confidence (Oct. 2008 – Dec. 2010)

**Due to instability in international financial markets  
& over reporting by the local media**



**Lack of depositor confidence**



**Flight to quality + Liquidity pressure**



**Temporary blanket guarantee**



## 3. Implementation Results

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- **Liquidity Pressure Relieved**
- **Huge Outflow of Deposits from Private Banks Decreased**
- **Inter-Bank Call-Loan Market Returned to Normal**





## **4. Enforces Risk Control in Conjunction with Supporting Measures for Financial Supervision**

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- Improving the information transparency, corporate governance, internal control, internal auditing and BIS ratio
- Controlling its insurance risk to avoid any negative reaction caused by the blanket guarantee
- Coordinates with the competent authority's supervisory policies. Implementing Financial Warning System and off-site monitoring mechanism
- Collects a special premium and charges the punitive premium to inter-bank call loans to reduce the moral hazard.



### III. Measures in Response to Blanket Guarantee Expiration

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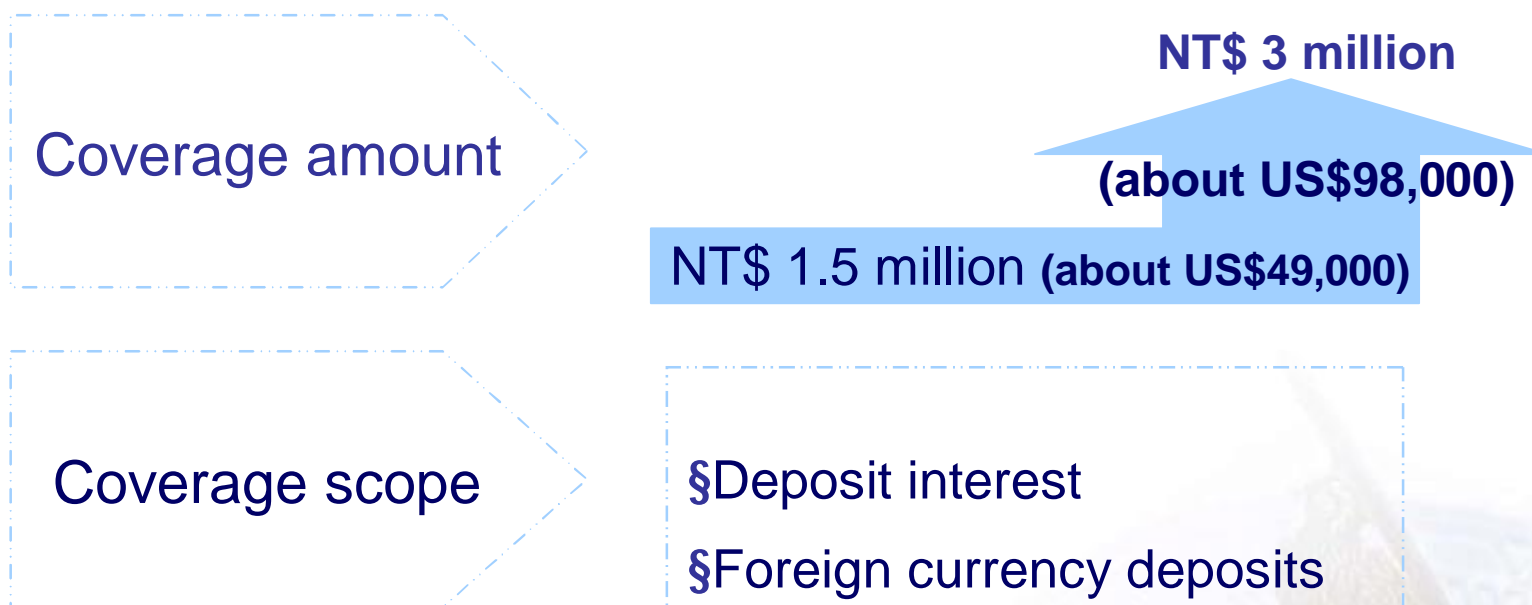
- 1. Amendment to the *Deposit Insurance Act*
  - (1) Increasing Coverage limit and expanding the scope
  - (2) Enhancing the Premium Adjustment Mechanism
  - (3) Reinforcing risk management
  - (4) Strengthening resolution mechanism for dealing with failing financial institutions
- 2. Extensive promotional campaign
- 3. Close coordination with other financial safety net participants





## § 1. Amendment to the Deposit Insurance Act

- (1) Increase coverage limit and expanding the scope





# 1. Amendment to the Deposit Insurance Act

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## ( 2)Enhancing the Premium Adjustment Mechanism

- 1.5% as the auto trigger point to raise the premium rates
- If the target ratio exceeds 2.5%, CDIC may temporarily terminate the collection of premium





# 1. Amendment to the Deposit Insurance Act

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## § (3) Reinforce risk management

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

## (4) Strengthen resolution mechanism

- Ø Authority by law to enter a failing bank confidentially and prepare for resolution before bank closure





## §2.Extensive promotional campaign

- Different media channels
- Publish transition related articles in CDIC's quarterly journals
- Host seminars for the general public and the insured institutions



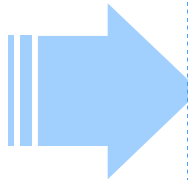


### 3. Close coordination with other financial safety net participants

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Transition  
plan



- Return to the limited coverage as schedule (January 1, 2011)
- Adopt fast approach with expansion of coverage limit and scope





## IV. Conclusions





## IV. Conclusions

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### Challenges

- § how to transit from blanket guarantee to a limited coverage system
- § how to overturn the policy that financial institutions are “too big to fail”
- § how to rebuild the deposit insurance fund
- § how to effectively ensure that the core principles of deposit insurance are effectively complied with



**Thank you !**  
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