

# Message from the Chairman and the President



Financial institutions in Taiwan were mostly state-owned leaving very few to private ownership as a result of strict regulation of the financial industry. In addition, establishment of new financial institutions and new financial business items were strictly regulated. Profitability of the financial institutions, therefore, had been very stable as risks had been limited. The government would intervene for bailout in the event of rare financial frauds. Therefore, importance had never been attached to the financial safety net. It was only after the liquidation of the Continental Illinois Bank in the U.S. in 1984 that triggered impact on the international financial market, along with a series of financial incidents in 1985 in Taiwan when the government was prompted to set up the Central Deposit Insurance Corporation (CDIC) in September 1985 with a view to help stabilize the financial order through the safeguard of the majority of depositors.

The government started to promote international trade without reserving any effort after reign in Taiwan. Foreign exchange reserves accumulated massively and have ranked the first tier of the world. Accompanying the increases of the foreign exchange reserves was the abundant funds circulating in the local financial system. There was increasingly advocacy for the financial reform in deregulation and internationalization. The government responded by overhauling the *Banking Law* in 1989, which liberalized the scope of businesses of the banks and opened up the establishment of new banks. By end 1991, there had been a total number of 16 new banks in operation. A relatively regulated financial market had been carved up by a significant number of financial institutions. In 1995 financial crises broke out at the

level of the community financial institutions with more than forty cases of financial panic run. The Asian financial crisis followed immediately in 1997. These events exposed the systemic problems inherent in Taiwan financial institutions; the various problem financial institutions did not have an existing mechanism to withdraw from the market. As a result, the government amended the *Deposit Insurance Act* in 1999, aimed at providing the problem financial institutions with the deposit insurance as an exit mechanism of the financial market as smoothly as possible and prevented financial disruptions. However, CDIC was not capable of facilitating a smooth withdrawal of the problem financial institutions to maintain the financial order as it adopted a voluntary insurance at that time and hence the amount of pay-off funds was very limited. Consequently, the Financial Restructuring Fund was set up in 2001 to keep the financial order. The Financial Restructuring Fund used public funds to make up for the shortage of deposit insurance pay-off funds. The policy-making and supervision of the Fund is in charge by the Management Committee of the Financial Restructuring Fund, Executive Yuan. CDIC is responsible for carrying out the policy. By the end of August 2005, CDIC has smoothly disposed 48 failed insured institutions to withdraw from the market.

The interim measure of blank guarantee previously under the Financial Restructuring Fund ended in July 2005. The government is in the process of amending the regulations including the *Deposit Insurance Act* in order to restore the dealing of problem financial institutions to the mechanism of limited coverage deposit insurance. Other relevant measures to strengthen the deposit insurance mechanism include strengthening deposit insurance pay-off funds, implementing prompt corrective action (mechanism that enables problem financial institutions to immediately correct themselves and smoothly withdraw from the market), and dealing with systemic risks in a more flexible fashion.

Moreover, in light of the contagion nature of global financial crises, CDIC has joined the International Association of Deposit Insurers (IADI) since 2002 and become its founding member. The IADI is an important mechanism that provides international cooperation on deposit insurance. CDIC is also actively involved in international activities related to deposit insurance for exchanges of information and experiences to make sure that Taiwan's deposit insurance system is in line with international development and innovation by learning the paradigm of the advanced countries and to improve the current deposit insurance system.

Chairman



President

