



International Association  
of Deposit Insurers

November 2012

# **Enhanced Guidance for Effective Deposit Insurance Systems:**

## **Reimbursement Systems and Processes**

### **Guidance Paper**

**Prepared by the Research and Guidance Committee**

**International Association of Deposit Insurers**

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## Executive Summary

The mission of the International Association of Deposit Insurers (IADI) is to contribute to the enhancement of deposit insurance effectiveness by promoting guidance and international cooperation. Its vision is to share its deposit insurance expertise with the world. As part of its work, the IADI undertakes research projects to provide guidance on deposit insurance matters.

A key function of a deposit insurance system is to give depositors prompt access to their insured deposits when a bank is closed. A deposit insurer's effectiveness in providing prompt reimbursements to depositors is critical for maintaining confidence in the banking system and financial stability. In this regard, IADI has set forth guidance through the adoption of the *BCBS-IADI Core Principles for Effective Deposit Insurance Systems*<sup>1</sup> and its accompanying assessment methodology.<sup>2</sup> The *Core Principles* include guidance for reimbursing depositors under Principle 17 which focuses on consumer protection elements aimed at protecting the rights of depositors to reimbursement, as well as the requisite enabling conditions necessary for deposit insurers to achieve this objective along with prompt reimbursements. Principle 17 on the reimbursement process states:

*"The deposit insurance system should give depositors prompt access to their insured funds. Therefore, the deposit insurer should be notified or informed sufficiently in advance of the conditions under which a reimbursement may be required and be provided with access to depositor information in advance. Depositors should have a legal right to reimbursement up to the coverage limit and should know when and under what conditions the deposit insurer will start the payment process, the time frame over which payments will take place, whether any advance or interim payments will be made as well as the applicable coverage limits".*

Additional guidance is provided through a number of essential and additional criteria contained in the *BCBS-IADI Methodology for Assessing Compliance with the Core Principles*.

Nevertheless, since the adoption of the *Core Principles* in 2009, efforts to benchmark country practices in depositor reimbursements has revealed the existence of significant gaps between current practices in many jurisdictions and the *Core Principles*. Furthermore, experience gained and lessons learned during the international financial crisis has led to the evolution of good practices in payout approaches. During 2008-11, the IADI Research and Guidance Committee undertook a survey of its membership and the development of a number of case studies to better understand the challenges faced in ensuring effective reimbursement processes.<sup>3</sup> The Committee found some of the biggest constraints hindering prompt and accurate reimbursements included: (1) the lack of early

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<sup>1</sup> See BCBS-IADI (2009).

<sup>2</sup> See IADI (January, 2011).

<sup>3</sup> See IADI (2012).

access to accurate depositor information (e.g. access to depositor records in advance of a failure, poor quality of depositor records, the lack of bank client unique identifiers to aggregate deposits); (2) difficulty in determining depositor claims and related loans/liabilities for complying with netting requirements; and (3) the lack of appropriate IT systems and reimbursement plans to deal with different sized banks.

During 2011-12, the FSB undertook a *Thematic Review on Deposit Insurance Systems*.<sup>4</sup> The *FSB Review* made a number of observations regarding payout practices in the wake of the financial crisis. It observed that the payout systems in the 24 FSB jurisdictions studied varied significantly – for example, in terms of the institution that triggers a claim for payment or the speed of depositor reimbursement. The starting date used to set the payout timeframes also differed, thus making it difficult to compare jurisdictions on the actual time it takes for depositors to regain access to their deposits after the institution fails.

The *FSB Review* confirmed IADI’s research findings on the need for early access to information; the reform of certain design features – e.g. shifting from a net to a gross payout basis – to improve the timeliness and efficiency of payouts; provide assured access to secondary funding sources (e.g. standby liquidity facility from the government or the central bank); and, that all DIS (and particularly those that had not conducted a payout in some time) undertake frequent simulation exercises to ensure the readiness and effectiveness of the payout process. In closing, the FSB recommended that IADI should, in consultation with the BCBS and other relevant bodies where appropriate, update its guidance that pre-dates the financial crisis.

As a result, this IADI Guidance Paper sets out additional enhanced guidance to address those areas where payout effectiveness could be enhanced and where the *Core Principles* could benefit from more precision to achieve effective compliance or to better reflect leading practices.

## **Enhanced Guidance**

Utilizing the experiences of IADI deposit insurers, surveys and case studies of practitioners and academic literature, IADI has identified the following 16 supplemental guidance points aimed at updating and enhancing its guidance related to depositor reimbursement for the effective implementation of the *Core Principles*.

1. A deposit insurer should have access to depositor records at all times and undertake preparatory reviews of bank deposit liability records to ensure prompt and accurate reimbursement of insured deposits.
2. Authorities should issue guidelines or regulations to ensure that banks can provide accurate deposit liability records, within a specific timeframe, for aggregation of depositors’ funds and when required by law or regulation (i.e. a “single customer view”).

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<sup>4</sup> See FSB (2012).

3. Authorities should eliminate impediments to prompt reimbursement. These could include eliminating the application of set-off and disaggregation of multiple ownership accounts, removing the need for claims to be made by depositors, and to review and possibly eliminate any inefficient or counterproductive regulations applicable to the deposit insurance reimbursement process.
4. Transit items of banks should be subject to agreements with all clearing and settlement system agencies to ensure that the items after a bank failure are dealt with in an appropriate and consistent manner, and as quickly as possible.
5. To expedite the reimbursement process, a deposit insurer should rely on technology-based systems to process depositor information in a systematic and accurate manner.
6. The limits and scope of coverage and product insurability must be set out in law, clearly defined and communicated to depositors to mitigate confusion.
7. Funding arrangements for the deposit insurance system should ensure the prompt reimbursement of depositors' claims and include a pre-arranged and assured source(s) of back-up funding for liquidity purposes.
8. A deposit insurer should consider a range of payment methods that would expedite the reimbursement process.
9. Depositors should be provided access to their insured funds as quickly as possible and no longer than one month from the event triggering reimbursement (e.g. closure of the bank).
10. A deposit insurer must communicate clearly the payment methods and timing for payments to depositors as part of a comprehensive communications strategy to manage public expectations.
11. A deposit insurer may, on its own decision, provide interim payments in circumstances where the deposit insurer is of the view that insured depositors require urgent access to their funds before the start of actual reimbursement is made (e.g. where there may be extended delays in reimbursements), provided it has the technical capacity to do so without impeding the overall payout process.<sup>5</sup>

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<sup>5</sup> In order to undertake an interim payment the deposit insurer requires timely access to the necessary information and should be able to provide the interim payments without harming its own position vis-à-vis these depositors and without impeding the smoothness and speed of the overall payout process.

12. For deposit insurers that do not have the authority to act as a receiver or liquidator (or choose not to exercise such powers) it is an effective practice to have in place arrangements (e.g. pre-arranged contracts) for the receiver/liquidator to assist the deposit insurer, if requested, in the execution of the deposit insurer's duties.
13. An audit of the reimbursement process should be conducted by an independent party to confirm that appropriate internal controls have been applied during the reimbursement process and that reimbursements are accurate.
14. Adequate resources and trained personnel dedicated to the reimbursement function should be made available to ensure readiness in undertaking reimbursements. Where internal resources are insufficient, a contingency plan should be in place to augment resources in times of need.
15. Where reimbursement-related cross-border issues exist, such as who would perform a reimbursement in an affected jurisdiction, these should be addressed well in advance to ensure that effective and timely reimbursements can be implemented. This would involve developing coordination protocols to define the responsibilities for performing reimbursement-related activities, developing consistent communication messages and strategies, and addressing other reimbursement-related issues.
16. Effective practices should be in place to conduct regular contingency planning and simulation exercises to test the operational readiness of the deposit insurer in carrying out reimbursements.

## **I. Introduction and objectives**

The mission of the International Association of Deposit Insurers (IADI) is to contribute to the enhancement of deposit insurance effectiveness by promoting guidance and international cooperation. Its vision is to share its deposit insurance expertise with the world. As part of its work, the IADI undertakes research projects to provide guidance on deposit insurance matters.

A key function of a deposit insurance system is to give depositors prompt access to their insured deposits when a bank is closed. A deposit insurer's effectiveness in providing prompt reimbursements to depositors is critical for maintaining confidence in the banking system and financial stability.

Given the importance of ensuring prompt and effective reimbursements, IADI has set forth guidance through adoption of the *BCBS-IADI Core Principles for Effective Deposit Insurance Systems*<sup>6</sup> and its accompanying assessment methodology. The

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<sup>6</sup> See BCBS-IADI (2009).

*Core Principles* include guidance for reimbursing depositors under Principle 17. The key elements of Principle 17 are comprised of consumer protection elements aimed at protecting the rights of depositors to reimbursement, as well as the requisite enabling conditions necessary for deposit insurers to achieve this objective along with prompt reimbursements.

*Principle 17 – Reimbursing depositors: The deposit insurance system should give depositors prompt access to their insured funds. Therefore, the deposit insurer should be notified or informed sufficiently in advance of the conditions under which a reimbursement may be required and be provided with access to depositor information in advance. Depositors should have a legal right to reimbursement up to the coverage limit and should know when and under what conditions the deposit insurer will start the payment process, the time frame over which payments will take place, whether any advance or interim payments will be made as well as the applicable coverage limits.*

*Essential Criteria:*<sup>7</sup>

1. *The deposit insurer is able to reimburse depositors promptly after the deposit insurance system is triggered by law, contract or the relevant authority.*
2. *The time frame for accomplishing the reimbursement process is prompt and clearly stated to meet the public policy objectives of protecting depositors and promoting public confidence and financial stability of the deposit insurance system . The time frame is made public.*
  - (a) *Depositors are provided information after the failure on when and under what conditions the deposit insurer will start the reimbursement process and when the process is expected to be completed;*
  - (b) *Information on coverage limits, scope of coverage and whether advance or interim payments will be made is provided; and*

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<sup>7</sup> The key assessment criterion for promptness is whether depositors receive their funds (in whole or in part) in a timeframe that maintains confidence and stability. What is considered prompt may vary from jurisdiction to jurisdiction, and will depend on the insolvency regime in place (whether a special resolution regime exists or the insolvency is addressed through the corporate bankruptcy process). Nevertheless, international practice is moving towards shorter and shorter payout periods. Payout delays might be mitigated by permitting the DIS to make advanced interim payments.

- (c) *If there is an interest-bearing account, the deposit insurer shall reimburse depositors for interest as provided by contract, law or regulation up until at least the date the deposit insurance obligation is triggered.*
3. *In order to promptly reimburse depositors, the deposit insurer has:*
    - (a) *Access to necessary data, including deposit account records, to prepare for reimbursing depositors as soon as the supervisor is aware of a likelihood of failure.*
    - (b) *The power to review in advance by itself (or by request from the supervisory authority) the way depositor records are kept by banks to ensure the reliability of records, to reduce the time needed for calculation and verification of depositors' claims;*
    - (c) *A range of payment methods for reimbursing depositors; and*
    - (d) *Access to adequate and credible sources of funding (e.g., reserve fund, Ministry of Finance, central bank) to meet its obligations under the established time frames.*
  4. *The deposit insurer has the capacity to carry out the reimbursement process in a timely manner, including:*
    - (a) *Adequate information technology; and*
    - (b) *Adequate personnel (in-house or contractor).*
  5. *In situations where there may be extended delays in reimbursements, the deposit insurer can make advance, interim or emergency partial payments.*

*Additional Criteria:*

1. *The deposit insurer has contingency plans as well as regularly scheduled tests of its systems.*
2. *The reimbursement process is audited by an independent auditor or authority.*

Since the adoption of the *Core Principles* in 2009, efforts to benchmark country practices in depositor reimbursements has revealed the existence of significant gaps between current practices in many jurisdictions and the *Core Principles*. Further, payout processes have evolved following the experience and lessons learnt in the crisis.

During 2008-11, the IADI Research and Guidance Committee undertook a survey of its membership and the development of a number of case studies to better understand the challenges faced in ensuring effective reimbursement processes.<sup>8</sup>

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<sup>8</sup> See IADI (2011).

The Committee found some of the biggest constraints hindering prompt and accurate reimbursements included: (1) the lack of early access to accurate depositor information (e.g. access to depositor records in advance of a failure, poor quality of depositor records, the lack of bank client unique identifiers to aggregate deposits); (2) difficulty in determining depositor claims and in particular related loans/liabilities for complying with netting requirements; and (3) the lack of appropriate IT systems and reimbursement plans to deal with different sized banks.

During 2011-12, the FSB undertook a *Thematic Review on Deposit Insurance Systems*.<sup>9</sup> The *FSB Review* made a number of observations regarding payout practices in the wake of the financial crisis. The *Review* observed that the payout systems in the 24 FSB jurisdictions studied varied significantly – for example, in terms of the institution that triggers a claim for payment or the speed of depositor reimbursement.<sup>10</sup> The starting date used to set the payout timeframes also differed, thus making it difficult to compare jurisdictions on the actual time it takes for depositors to regain access to their deposits after the institution fails.<sup>11</sup> And, the *Review* noted the important linkage between funding sufficiency and the promptness of reimbursements.

The *FSB Review* confirmed IADI's research findings on the need for: (1) more effective payout arrangements – such as early information access need to be put in practice more widely; (2) the reform of certain DIS design features – e.g. shifting from a net to a gross payout basis, or simplification of claimant eligibility requirements – can also be helpful to improve the timeliness and efficiency of payouts; (3) ensure secondary funding sources (e.g. standby liquidity facility from the government or the central bank) helped ensure the deposit insurer to meet its funding needs; and <sup>12</sup> (4) that all DIS (and particularly those that had not conducted a payout in some time) could benefit from undertaking more frequent simulation exercises to ensure the readiness and effectiveness of the payout process.

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<sup>9</sup> See FSB (2012).

<sup>10</sup> In the case of Germany, the institutional protection schemes do not have any arrangements to reimburse depositors because they protect their member institutions against insolvency and liquidation. In the case of Switzerland, depositor reimbursement is the responsibility of the failed bank's liquidator (or authorized agent in charge of the bank's recovery) as opposed to the deposit insurance agency.

<sup>11</sup> The *FSB Key Attributes of Effective Resolution Regimes* advocates that in the case of insured transaction accounts, depositors be provided with access to their funds promptly (e.g. within seven days).

<sup>12</sup> According to the *Review*: "In contrast, unclear or informal standby funding arrangements that may require additional approval before draw-down is effected could jeopardize the speed of handling a depositor payout or bank resolution, impede the effectiveness of the DIS in maintaining financial stability and would not be consistent with the *Core Principles*."

In closing, the *FSB Review* recommended that IADI should, in consultation with the BCBS and other relevant bodies where appropriate, update its guidance that predates the financial crisis. As a result, this report sets out to develop additional guidance to address those areas where payout effectiveness could be enhanced and where the *Core Principles* could benefit from more precision to achieve effective compliance or to better reflect leading practices.

## II. Methodology

The paper is based on a survey of the experiences of IADI deposit insurers, observations and survey results from the *FSB Thematic Review on Deposit Insurance* and recent academic literature. The paper also draws on the results of a number of deposit insurers in conducting self-assessments against the *Core Principles* to identify impediments to developing effective reimbursement systems and processes<sup>13</sup>. The research covers key processes that are fundamental building blocks of an effective reimbursement system.

The IADI survey questionnaire was divided into five sections.<sup>14</sup> The respondents were asked to identify the impediments and challenges of undertaking a reimbursement and how they addressed these problems. They were asked to rank those impediments in order of criticality with 1 being the most critical, 2 (critical), 3 (somewhat critical), and 4 (not critical).

In addition, five country case studies were undertaken by IADI to analyse in greater detail several aspects that were considered to be important elements of the fundamental building blocks.<sup>15</sup> These country studies provide a rich variety of experiences and valuable lessons that were incorporated into this paper.

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<sup>13</sup> Twenty-seven organisations (close to 80% of participants that have indicated interest to participate in survey) responded to the survey. However, two responses were not complete. The 25 deposit insurers which completed the questionnaires are from Albania, Bahamas, Bulgaria, Canada, Canada (Quebec), Hong Kong, Hungary, India, Kazakhstan, Korea, Malaysia, Mexico, Netherlands, Romania, Russia, Singapore, Slovakia, Sweden, Taiwan, Tanzania, Trinidad & Tobago, Turkey, UK, US and Vietnam.

<sup>14</sup> The five sections are: access to prompt and accurate information, resources, coverage rules and product insurability, IT System and mandate and powers.

<sup>15</sup> The case studies were - CDIC (Canada): Contingency Planning and Simulations at Canada Deposit Insurance Corporation, FDIC : Information Technology for Effective Reimbursement of Insured Deposits, FSCS : Faster Reimbursement, IPAB : Technical aspects of the inspection visits carried out by the IPAB, in order to evaluate the banks' compliance to the Rules for classifying transactions relating to insured deposits, and MDIC : MDIC's Experience in Designing and Developing an Effective Reimbursement System.

### **III. Essential elements of effective reimbursement systems**

#### **A. Timing of reimbursements and pre-closure preparatory work**

Core Principle 17 states that “the deposit insurance system should give depositors prompt access to their insured funds.” In practice, the timing of reimbursements to depositors varies considerably across jurisdictions and is usually measured from a starting point or triggering event ranging from when an institution reaches a point of non-viability to a court declared bankruptcy.

The IADI Survey on Effective Reimbursement Systems showed that 17 respondents have a mandated reimbursement period while the other eight do not. The mandated period for reimbursement ranged from “as soon as possible” for the Canada Deposit Insurance Corporation (CDIC - Canada) to “not later than six months” for the Deposit Insurance Corporation (Bahamas), which relies on its central bank to conduct a reimbursement.<sup>16</sup> According to the FSB Review, EU member states are legally obliged to reimburse depositors within 20 working days of bank closure (extendable to 30 days by the regulator or the DIA). In the case of Switzerland, the depositor protection system has to pay the liquidator (or authorised agent in charge of the bank’s recovery) who is responsible for reimbursing the depositors (with no specific delay) within 20 working days after the issuance of a decree by the supervisory/resolution authority FINMA (as opposed to the bank’s actual failure).<sup>17</sup>

Notwithstanding that, almost all respondents have a targeted period to reimburse depositors, which is generally shorter than the mandated reimbursement period. The Federal Deposit Insurance Corporation (FDIC) has the shortest targeted period, with the ability to advance full payments within the next business day, typically two days. The Central Deposit Insurance Corporation (CDIC -Taiwan) is not far behind, with plans to reimburse depositors three days after a failed bank is closed. The CDIC (Canada)’s system allows for partial reimbursement within five days after a bank failure and full reimbursement of most accounts within 14 days. In the UK, the FSCS has a target to repay the majority of depositors within 7 days; in fact in the case of a bank liquidation in 2011 (Southsea), the vast majority of depositors were paid the day after the liquidation. In Mexico, the Instituto para la Protección al Ahorro Bancario (IPAB) has a mandate to reimburse depositors who have met requirements, within 90 days of the announcement of the payout procedure in the Official Gazette. However, past experiences demonstrated that the IPAB was able to reimburse depositors within seven days after a claim has been filed.

It should be noted that the targeted reimbursement periods begin from the date of the closure of the bank. The time periods do not include the time that may be taken by the deposit insurer, prior to a closure, to prepare for reimbursement. Clearly, deposit insurers cannot reimburse eligible depositors promptly if they do not have

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<sup>16</sup> Source: Information Paper: IADI Survey on Effective Reimbursement Systems.

<sup>17</sup> See FSB (2012).

adequate time to conduct reimbursement preparatory work before a bank is closed.<sup>18</sup> To assess the level of constraint or performance required from a deposit insurer, notwithstanding other factors, such as the complexity of the regulations, the time period starting from the day the deposit insurer is able or authorized to gain access to depositors data should be considered.

Although it is difficult to arrive at a precise reimbursement period to recommend, at a minimum depositors should be provided access to their insured funds within one month from the event triggering reimbursement (e.g. closure of the bank).

Reimbursing depositors is a complex undertaking and requires establishing the infrastructure building blocks in anticipation of a potential bank closing. This includes establishing the legal authorities for the deposit insurer to direct banks to submit accurate depositor records, strategies and approaches for handling depositor records, coordination protocols with other safety net players and service suppliers, as well as policies, controls and authorities within the governance structure of the deposit insurer that will guide the management of the reimbursement process.

Even with the relevant infrastructure in place, there are a large number of activities to be undertaken prior to a bank closure if a prompt reimbursement to depositors is to be met. The preparatory activities to be performed include:

- Coordinating with other safety net agencies to obtain relevant information to assist in planning for the reimbursement;
- Reviewing the relevant regulations in order to eliminate inefficient or counter-productive impediments;
- Developing work plans and budgets, including an estimate of the timeframe required to make reimbursements;
- Assessing the funding requirements and effecting the necessary arrangements for obtaining funds;
- Arranging and organising human resources, internal and external;
- Reviewing the bank's systems and procedures for obtaining depositors' information;
- Transforming the depositor records into a format that is usable by the deposit insurer;
- Reconciling the bank's depositor information with the bank's accounting and financial reports;
- Confirming the eligibility of products, depositors, and accounts with differing legal statuses for insurance coverage and assessing the level of work required for valuation issues, such as interest calculations;

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<sup>18</sup> For example, the FDIC regulations include early intervention activities that under the best case scenario provide at least 90 days' notice before the closure of a bank.

- Confirming the treatment of transit items in the clearing and settlement process;<sup>19</sup>
- Establishing the payment method or methods to be used in making reimbursements, identifying the service providers to be used, and assessing whether to utilise interim payments as part of the reimbursement strategy; and
- Developing the communications strategy for dealing with the failure of the bank.

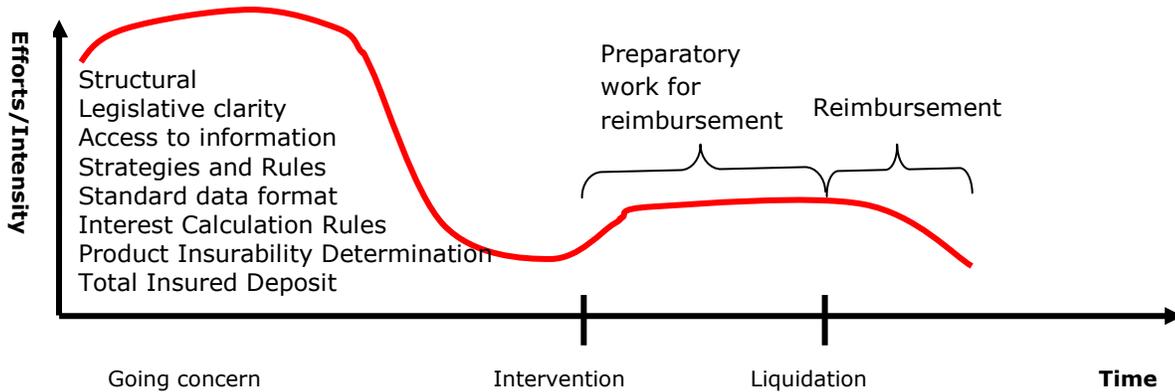
These preparatory activities are essential for a successful reimbursement process.

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<sup>19</sup> To avoid any changes to the balance, IPAB rejects all transit operations which are underway after the bank's closing date, sending them back to their originating point.

Chart 1 depicts the level of pre and post closure reimbursement preparation activities under an effective reimbursement model. Under this model, preparatory activities are carried out ahead of a bank closure.

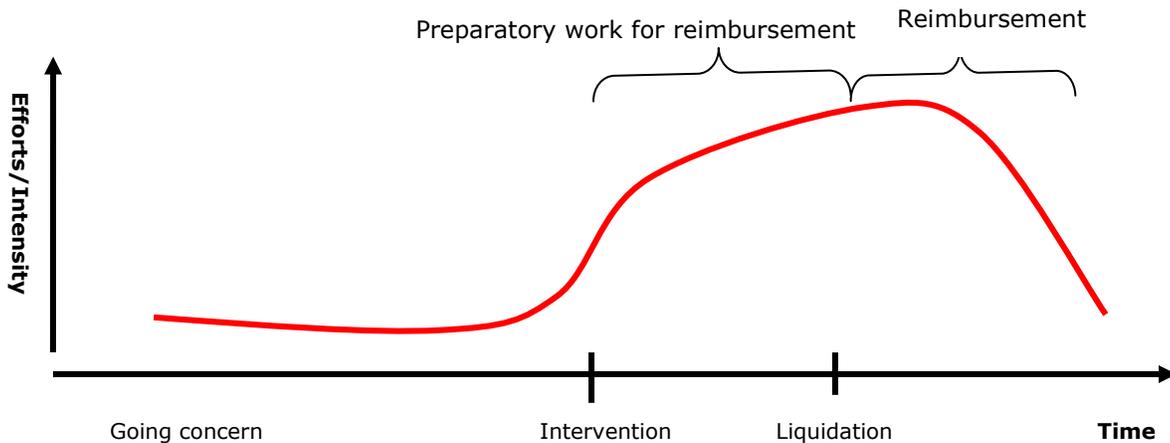
**Chart 1: Effective reimbursement model – Pre and post closure preparation activities**



Source: IADI Case Study: MDIC's Experience in Designing and Developing an Effective Reimbursement System .

Chart 2, on the other hand, shows the level of pre and post closure reimbursement preparation activities under a traditional reimbursement model, which only start once the decision to liquidate a bank has been made.

**Chart 2: Traditional reimbursement model – Pre and post closure preparation activities**



Source: IADI Case Study: MDIC's Experience in Designing and Developing an Effective Reimbursement System

With limited preparation and time, a deposit insurer could possibly face numerous data quality problems amidst the pressure to complete reimbursements. Working under extremely stressful timelines, errors in computation of reimbursement

amounts could occur, leading to delays, reputational risks to the deposit insurer, and costlier resolutions.

There are many impediments to prompt and accurate deposit reimbursements. Table 1 from the IADI Survey on Effective Reimbursement Systems summarises the top six most critical and critical impediments to an effective reimbursement.

**Table 1: Key impediments to effective reimbursement system:**

Top six most critical and critical problems (% of total)

<b>Impediments</b>	<b>Most Critical</b>	<b>Critical</b>	<b>Total</b>
Lack of access to deposit records in advance of a failure	28.0%	28.0%	56.0%
Poor quality of depositor records at banks	40.0%	12.0%	52.0%
Inability of banks to provide depositor record within desired timeframes	24.0%	24.0%	48.0%
Determining depositor claims and related loans/liabilities for complying with netting requirements	12.0%	28.0%	40.0%
Lack of unique identifier	8.0%	20.0%	28.0%
Lack of appropriate IT system reimbursement plans to deal with different size banks	16.0%	8.0%	24.0%

Source: Information Paper: IADI Survey on Effective Reimbursement Systems

## **B. Access to and accuracy of depositor data**

Among the deposit insurers surveyed, problems associated with access to accurate information was considered the biggest constraint confronting deposit insurers in carrying out prompt and accurate deposit reimbursements. The IADI survey results revealed that the biggest impediment to an effective reimbursement is the lack of access to depositor records in advance of a failure. In some jurisdictions, deposit insurers do not have access to deposit records until a bank is closed. This finding was confirmed by the FSB Review in 2012. As noted, it is crucial for the deposit insurer to be able to access and test the bank's data.

Poor quality of depositor records and the inability of banks to provide depositor records within desired timeframes was the second major impediment. Supervisory regulations or the deposit insurer's capacity to enforce high quality standards in record keeping amongst banks is critical for prompt and accurate reimbursement. Towards this end, one important reform that is being implemented in several jurisdictions is to develop a Single Customer View (SCV). A consolidated view of all

deposit accounts eligible for deposit insurance coverage for a single depositor would enable faster determination for reimbursement.

For example, in the UK, the Financial Services Compensation Scheme (FSCS) undertook a program to require its member banks to produce an aggregated balance of a customer's accounts across the bank within 72 hours of a request from the FSCS. Included in the SCV program are requirements for dealing with clearing and settlement transit items, dormant accounts, and tagging of certain accounts (e.g., client and trust accounts with beneficiaries) for later special treatment. Along with the SCV requirements, legislative changes were made to increase the FSCS's rights to access information of its member banks. This was supported by simplifying the depositor eligibility requirements. The objective of the SCV solution is to enable the FSCS to make payment to a significant number of depositors within seven days of a failure and within 20 days of a failure for the other depositors with less straightforward banking relationships (e.g. trust accounts).<sup>20</sup>

The FSCS's experience points to the need for not only having access to depositor records in advance, but also for undertaking verification work to ensure that the records available at the time of a reimbursement are accurate and usable by the deposit insurer. To this end, the FSCS required its member banks to submit sample SCV files to allow the FSCS, through an outsourced solution, to perform verification procedures to ensure the SCV files are suitable for use in a reimbursement. These tests need to be repeated as part of any contingency planning.

In Mexico, to obtain information on insured deposits, the IPAB has the powers to:

- acquire information on insured deposits directly from the banks, when deemed necessary;
- compel banks to classify information on insured deposits in their own IT systems (or any other means) according to a general regulatory framework issued by the IPAB;
- conduct inspection visits to banks along with the banking Supervisor in order to verify and evaluate the bank's compliance to the said framework; and
- issue rules on joint account coverage.

Once such information is received, it is processed using an automated system developed by the IPAB to validate data layouts and content. An important element of this system is the Depositor ID number (Unique Depositor Key Code -UDKC): a personal identification string of characters to match all accounts belonging to an individual depositor.<sup>21</sup>

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<sup>20</sup> Source: IADI Case Study: Financial Services Compensation Scheme (FSCS) – Faster Reimbursement.

<sup>21</sup> Source: IADI Case Study: Technical aspects of the inspection visits carried out by the IPAB, in order to evaluate the banks' compliance to the Rules for classifying transactions relating to insured deposits

The CDIC (Canada) issued a Data and System Requirements By-law and technical specifications that require its member banks to provide or make available depositor information to the CDIC (Canada) in specified formats. A verification process is underway subsequent to implementation of the requirements by its member banks, scheduled for June 30, 2013.<sup>22</sup>

Such experiences highlight the importance for deposit insurers to have access to depositor records in advance of a reimbursement, either as part of a preparatory review just prior to a reimbursement or as part of an on-going review and verification process. This enables insurers to be aware of the potential data issues that may arise during a reimbursement.

The lack of a bank client-unique identifier ranked fifth among the top six key impediments to effective reimbursement. This complicates the task of aggregating the relevant accounts held by a depositor where the deposit insurer makes reimbursements based on depositor rather than individual accounts.

Several deposit insurers, such as the Hong Kong Deposit Protection Board (HKDPB) and the MDIC, are able to rely on national identity documents and numbers for individuals and companies.

### **C. Netting requirements in determining depositor entitlements**

The difficulty in setting off a depositor's claim against his/her related loans and liabilities in determining compensation entitlement was the fourth most challenging impediment (40% of survey respondents identified this either as a most critical or a critical issue). The complexities of set-off or netting relate not only to matching depositors' deposit accounts with any related loans and liabilities of the depositors to the failed bank, but also to determining the appropriate amounts to set off against the deposit balances. This latter issue arises in situations involving guarantors of debt and contingent liabilities, and is typically the responsibility of parties other than the deposit insurer, such as the liquidator of the failed bank.

These complexities can have a significant impact on the ability to make prompt and accurate payments since set-off introduces the risk of overpayment when netting relationships cannot be quickly identified and determinations of the amounts to be set off cannot be made within short timeframes. This could delay reimbursement to the depositor group from the main reimbursement process and require special handling to deal with the depositor to work out the appropriate netting determinations. When the deposit insurer is not able to quickly identify those depositors that have loans and other liabilities with the failed bank and segregate them for special treatment, the deposit insurer should enlist the assistance of the liquidator to identify these depositors. In determining the amounts to set off against depositors' balances, the deposit insurer may consider making conservative

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<sup>22</sup> Source: CDIC Data and System Requirements By-Law (December 8, 2010) and Data and System Requirements - Version 1.0

estimates of the amounts to set off to allow for some form of payment to be made to these depositors while mitigating the potential for overpayment.

Besides the complexities, some deposit insurers also noted that set-offs are not equitable to depositors with non-collateralised loans, as their claims on the uninsured portion of deposits would be made against the estate of the failed bank and, in many instances, they would receive less than their full amount. However, collateralised uninsured deposits are reimbursed 100 per cent when set-offs take place. This gives collateralised depositors preference over non-collateralised depositors. Reforms have been undertaken in several jurisdictions, notably the UK and Singapore, to streamline the reimbursement determination process by moving to calculations based on gross deposit balances. To change from a net basis to a gross basis for reimbursement would require a change in the insolvency regime to be able to file a claim for the full reimbursement amount to the liquidator of the failed bank.

#### **D. IT systems for reimbursement**

Managing depositor reimbursement requires potentially processing thousands of accounts accurately and within tight timeframes. To keep within the reimbursement time frame, deposit insurers will have to rely on an information technology (IT) system for reimbursement. Not having an IT-based reimbursement system to deal with different size banks is ranked as the sixth key impediment to prompt and effective reimbursement. In the event of a reimbursement, if the eligibility of a depositor and of each deposit product for deposit insurance protection needs to be assessed manually, the deposit insurer may not be able to execute reimbursements promptly and effectively. Even in situations where banks make significant use of paper-based systems, the deposit insurer will still need to make use of a technology-based solution to process data, apply its insurance rules, track payments and minimise the likelihood of errors occurring in the process. A technology-based solution allows the deposit insurer to perform the reimbursement process within the desired timeframes.

The options available to deposit insurers for technology-based solutions for reimbursement systems depend on whether the deposit insurer has the authority to access, utilise, and modify a bank's IT systems for use in a reimbursement. When a deposit insurer has such authority, it can develop modules to perform the required insurance determinations and integrate these with the bank's systems to process reimbursements while leveraging the scalability of the bank's systems. Some deposit insurers (e.g. the Bulgaria Deposit Insurance Fund) utilise the IT system of the failed banks to conduct reimbursements. However, in most cases, deposit insurers do not have this authority, making it more feasible to develop an IT reimbursement system that will run independently of, and preferably parallel to, a failed bank's systems.<sup>23</sup>

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<sup>23</sup> It should be noted that having an IT reimbursement system does not preclude the deposit insurer from making use of manual processes in certain

Annex I highlights actions taken by deposit insurers to address impediments and challenges to an effective reimbursement system.

## **IV. Other Important Elements of an Effective Reimbursement System and Processes**

An effective reimbursement system and processes has a number of other important elements.

### **A. Payment methods and timeframes for payment**

There are a number of payment methods available for reimbursing insured depositors. Different methods can be applied in different circumstances or several methods can be used simultaneously, however; each option will have an impact on the timeliness of payment.<sup>24</sup> The options available include:

1. Cheque payments. The advantage of cheque payments, such as security and familiarity, must be weighed against the logistical challenges of having to produce a large number of cheques in a secure environment and sending them to depositors, usually through the postal system. The deposit insurer needs to identify an appropriate service provider who could develop the information transfer protocols to process depositor information and, based on this information, produce the requisite number of cheques in the names of the depositors with the correct reimbursement amount within the desired timeframe.
2. Electronic transfers. The use of electronic transfers for reimbursements is a feasible and time-saving option. This option is very efficient, as it only requires depositors to have an account with another bank. A secure system, to ensure authentication of depositor account details is absolutely required.
3. Payment agents. Paying agents may include other financial institutions or organisations that regularly deal with payments to the public (e.g. postal banks, government support payments). However, in order for this method to be efficient, the deposit insurer would need to identify and select its paying

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circumstances. For example, the HKDPB relies mainly on an automated reimbursement system to process depositor records from banks to determine depositor reimbursement amounts. However, owing to the complexities of certain issues, such as the application of set-off, the valuation of contingent and future liabilities, and the calculation of interest on complex financial products, along with data from smaller banks not being required to be in a specific format and structure, some manual intervention is required.

<sup>24</sup> For example, in a situation where most deposits are fixed term with long maturities the deposit insurer may wish to favour the use of cheques over other methods. Similarly, in cases where most deposits are very short term other methods may be favoured over cheques.

agents before a reimbursement takes place and to address issues such as cost arrangements, depositor information transfer protocols, and procedures, as well as the timelines for making reimbursements. Test runs must also be conducted.

4. Cash payments. This is generally not a preferred method. The security and logistical challenges relating to the management of large sums of cash and the establishment of a sufficient number of centres to address geographically dispersed depositors are significant.<sup>25</sup> Aside from the travel inconvenience to visitors if the centres are located far away, there are other challenges such as crowd management and communication management when the centres become focal points for depositors to express their frustrations. However, for jurisdictions where payment systems are not well developed, cash payments may be the most feasible. Alternatively, cash payments may be convenient for smaller balances, especially where the depositors may not have alternative accounts. Similarly, the use of ATMs introduces the same security issues for depositors withdrawing large sums of cash. However, ATMs may be a feasible method for interim or advance payments. The efficacy of this option will depend heavily on the ability of the deposit insurer to utilise the systems of the failed bank to track payments made throughout the reimbursement process.
5. Interim payments. Interim payments may relieve the pressure for making full payments too quickly, especially in circumstances where the deposit insurer may be faced with significant risks of overpayment (e.g., incomplete depositor information, incomplete aggregation).<sup>26</sup> Nevertheless, certain preconditions should be fulfilled, in particular: the deposit insurer should be in the position to make the decision to undertake interim payments; be able to gain access to the necessary data in advance; be able to provide interim payments without harming its own position vis-à-vis these depositors; and, provide interim payments without impeding the smoothness and speed of the overall payout process.
6. Transfer of insured deposits through a purchase and assumption agreement. Another alternative method is a deposit transfer through a purchase and assumption agreement.

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<sup>25</sup> The IPAB's Governing Board may decide to establish a limited amount to be paid in cash (e.g. \$100) to those insured depositors who hold a total balance that is less or equal to that amount. This way, the inconvenience of cash payments is radically reduced.

<sup>26</sup> Some deposit insurers have incorporated optional interim payments into their reimbursement systems, with a number of them choosing an approach that provides for a broader-based interim payment, such as CDIC (Canada), HKDPB, FSCS, KDIC and MDIC.

7. Other methods. Payment methods used by depositors evolve over time (e.g. the introduction of e-money and mobile phone banking) and the deposit insurer should review its payment methods on a regular basis to consider whether changes need to be made.

Whatever the payment method, a deposit insurer needs to know when to start and when to complete the reimbursement process. Likewise, depositors need to know when and how they can expect to receive their funds. In many instances, insured depositors do not have to take any action to receive their reimbursement – once the bank’s records are processed, the insurer distributes depositor funds. In other cases, however, insured depositors must file a claim and show proof of ownership or identification before being reimbursed, but this can slow down the overall payout process. When the depositors must file a claim, the reimbursement timeframe must be considered from the date the depositor presents such claim provided the deposit insurer enables the depositor to present its claim immediately after the bank’s closing date. In addition, an appeal process may need to be established, and the deposit insurer may need to process payments for uninsured and non-depositor claimants if it is also acting as the receiver. To prevent any the loss of public confidence in a deposit insurance scheme, depositors must be made aware of any actions that affect their insured deposits – such as the need to file a claim and how to do so – and when they can expect to be reimbursed.

## **B. Human resource capabilities and capacity**

Based upon the survey results, the effectiveness of the reimbursement process is dependent on the level of pre-closure preparatory work carried out by the deposit insurer. This requires skilled human resources with expertise in carrying out the reimbursement functions. The preference as to whether the deposit insurer employs reimbursement personnel or elects to use external service providers depends upon the frequency of reimbursements. In either case, a deposit insurer needs to develop a network (otherwise known as a “virtual organisation”), combining internal reimbursement personnel and external service providers, who can deliver the necessary services, when called upon. A deposit insurer should develop contractual relationships with the service providers well in advance of any reimbursements and develop the necessary protocols to ensure the services provided are properly integrated with and supportive of the deposit insurer’s reimbursement process.

In those cases where the deposit insurer employs bank personnel to carry out most of the payout procedures (i.e. receiving and processing a claim form), it is necessary for the deposit insurer to be able to provide adequate training considering the bank’s organizational structure and geographic issues.<sup>27</sup>

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<sup>27</sup> For deposit insurers that do not have the authority to act as a receiver or liquidator (or choose not to exercise such powers) it is an effective practice to have in place arrangements (e.g. pre-arranged contracts) for the receiver/liquidator to assist the deposit insurer, if requested, in the execution of the deposit insurer’s duties.

### **C. Coordination with other safety net participants**

A framework should be in place for the close coordination and information sharing, on a routine basis, as well as in relation to particular banks, among the deposit insurer and other financial system safety-net participants. Such information should be accurate and timely (subject to confidentiality when required). Information-sharing and coordination arrangements should be formalised.<sup>28</sup>

There are a number of coordination issues that have an impact on the deposit insurer's ability to prepare and act promptly. The first issue concerns the conditions under which a reimbursement would be triggered and the notification to be given to the deposit insurer when such conditions have taken place. It is critical for the deposit insurer to have a clear understanding, based on legislative provisions, of when it will be called upon to commence reimbursements and that it will be provided prior notification of this event by the appropriate authority to commence preparatory reimbursement arrangements.

Another issue is clear delineation of duties amongst the safety net participants. In many situations, the deposit insurer would not have control over the failed bank's systems and personnel, but would require a number of reimbursement processes to be either performed by or with the assistance of personnel of the failed bank and the liquidator.

One other area of critical concern that requires coordination is the treatment of transit items that are caught in the clearing and settlement process. Upon the closure of a bank, clearing system default rules would take effect. This may result in the reversal or unwinding of transit items. How these transit items are dealt with would depend on the rules of the clearing system. However, the status of these items and the processing time needed should be known to the deposit insurer.

In light of the above, deposit insurers advocate working early with the clearing and settlement participants, prior to any bank closure, to confirm the treatment of such transactions and to understand the processes in the clearing system and bank systems.

Netting requirements are an example of some of the complexities of the applicable regulations that should be reviewed. Other examples include: exclusions or specific treatment for categories of deposits or depositors which are vaguely defined or not referenced as such in the IT systems of banks.

### **D. Funding**

IADI survey respondents, the *FSB Review*, and experience conducting self-assessments of the Core Principles noted the important linkage between funding

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<sup>28</sup> Principle 6 of the Core Principles provides the essential criteria for establishing effective relationships.

sufficiency and ensuring the promptness of reimbursements. Core Principle 11 and essential criteria 2 of the assessment methodology stress that deposit insurance systems should have available all funding mechanisms necessary to ensure prompt reimbursements, including a pre-arranged and assured source(s) of back-up funding for liquidity purposes.<sup>29</sup>

## **E. Cross-jurisdictional coordination**

A coordination issue arises in circumstances where the deposit insurer provides coverage for its banks operating in another jurisdiction or where another deposit insurance scheme provides coverage to banks operating in the host deposit insurer's jurisdiction (host country schemes). The coverage may take one of the following forms:

- Home country scheme provides full coverage to depositors in the host country, as its banks may have opted-out of coverage under the host country scheme or the host country operations are performed through a branch;
- Host country provides coverage to depositors of a home country scheme usually while the home country scheme provides "top-up" coverage where its coverage levels are higher, although it could be full coverage; and
- Home country scheme provides protection up to its coverage limit while the host country scheme provides "top-up" coverage to the host country scheme's limit where the host country scheme levels are higher.

These situations were especially prevalent in Europe, but less so now that there is a harmonised limit in the 27 EU members states, although they also occur in other jurisdictions that allow branch operations of international banks (e.g., Hong Kong).

To avoid confusion on the part of depositors, both the home and host country schemes should develop necessary coordination protocols in advance, either on a bilateral or multilateral basis. These protocols should specify responsibilities for the reimbursement function in the affected jurisdiction, communication messages and strategies to be employed, depositor information that needs to be exchanged between the schemes, and cross-border claims process between the host and the home country scheme or vice versa.<sup>30</sup> In any event, where there may be a material

<sup>29</sup> See IADI (January 2011).

<sup>30</sup> As the failure of the Icelandic bank Landsbanki Islands hf illustrated, even having Memoranda of Understanding (MOU) and protocols in place between the deposit insurers does not guarantee certainty. In the case of Icesave (a branch of Landsbanki operating in the UK), the UK authorities, alongside the FSCS, fully compensated the Icesave depositors with their own resources, with the aim to recover from the Iceland authorities at a later stage. This was inconsistent with the MOU between the FSCS and the Iceland Depositors and Investors Guarantee Fund (DIGF), in which both agreed that the FSCS would provide top-up coverage after the DIGF provided initial coverage.<sup>30</sup> This highlights the need for deposit insurers to have contingency plans that include dealing with such unexpected situations. In addition, the enforceability of such MOUs and protocols in a court

number of depositors in one country with a bank whose payout will be handled by the deposit insurer in another country, it is recommended that the deposit insurers agree plans for the handling of such claims (e.g. whether the host state deposit insurer may assist the home state deposit insurer to distribute information, claims, or even payments).

#### **F. Verification of the reimbursement process and reimbursed amounts**

The reimbursement function is one of the primary tools which the deposit insurer uses to manage public confidence in the banking system. As in all dealings with members of the public, it is important to manage perceptions relating to integrity, internal controls, and governance issues within the reimbursement process. One critical function is the verification or audit of the reimbursement process to ensure accurate computation of reimbursement amounts. The audit should be performed by an independent party, such as a government audit agency or an accredited accounting firm that is not involved in the design or the execution of any part of the reimbursement process. The audit itself should also be conducted in accordance with approved auditing standards to provide an opinion on the state of the internal controls and the accuracy of the reimbursement amounts.

The timing for performing the audit is an important consideration, as it may impact the timeframe for making reimbursements. The audit should ideally begin at the same time as the reimbursement process and run concurrently. An audit of the reimbursement process and reimbursement amounts will assist the deposit insurer in having its claim in the liquidation proceedings approved expeditiously. The liquidator may place significant reliance on the audit report, thus minimising the amount of verification work necessary to the deposit insurer's claim, allowing such advances to be made sooner.

#### **G. Operational readiness through simulations**

Although infrastructure is important, it is equally important for a deposit insurer to be confident that all the reimbursement processes will perform as expected in a "live" scenario. To achieve this, IADI advocates periodic testing of operational readiness through simulation exercises of all or some aspects of the reimbursement function, including readiness of banks to provide accurate depositor information within targeted timeframes.

The objectives for simulation exercises, generally, are to ensure that the personnel involved in the reimbursement function are sufficiently trained, knowledgeable, and able to identify improvements to reimbursement procedures and processes, and

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of law, as well as the capacity and capability of the signatories to honour their financial commitments or carry out a reimbursement, should also be given consideration and reviewed regularly.

that the IT reimbursement system has adequate capacity and functionality to deal with the possible situations that may arise in a reimbursement.

With regard to human resource capabilities, simulation exercises provide the opportunity to determine the appropriate level of resources required for a reimbursement and to assess the ability of the deposit insurer's internal and external resources to work in a coordinated and effective manner. It also provides an opportunity to assess whether the required reimbursement activities can be performed within a constrained timeframe and under a stressed environment.

A simulation also tests the deposit insurer's IT reimbursement system by internal and external reimbursement personnel. When the deposit insurer can utilise actual depositor records from a bank (appropriately masked for purposes of protection of personal information and compliance with banking secrecy legislation), it would be able to verify the functionality of the IT reimbursement system when faced with data that may not fully comply with the deposit insurer's requirements. Also, the deposit insurer can assess the time required for processing data throughout the entire reimbursement process to confirm if the reimbursement amounts can be paid accurately and within the appropriate time frames.

Finally, simulation exercises and their results may also be published as part of a deposit insurer's communication program to contribute to financial system stability. This is important as such disclosure builds brand confidence in the deposit insurer and affirms its commitment to protecting financial consumers' rights to prompt access to insured funds.<sup>31</sup> Overall, the common objectives for conducting reimbursement simulations include the following:

- Involve all personnel, including personnel from external suppliers, to ensure reimbursement policies, procedures, processes, internal controls, and governance practices are well understood by all;
- Test the deposit insurer's organisational reimbursement procedures and processes, including the IT reimbursement system, on a comprehensive basis to ensure they all work well together to meet the deposit insurer's targeted timeframes. For simulations that target specific critical procedures, processes and IT reimbursement system functions are also important, especially when stress testing them against standard and unusual scenarios in order for management to assess foreseeable and unforeseeable risks; and
- Apply the lessons learnt from the simulation exercise to fine tune or enhance the overall reimbursement function, particularly to ensure that reimbursements are accurate and made within the targeted timelines. In this regard, regular simulations will enable deposit insurers to be aware of their

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<sup>31</sup> The CDIC (Canada) has conducted extensive simulation exercises and has documented its processes and lessons learned. IPAB (Mexico) has experience conducting an inter-agency simulation exercise, in close coordination with the World Bank.

own level of operational readiness and to identify the problematic areas requiring improvements.

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## Annex I

### Actions taken to address impediments and challenges to an effective reimbursement system

Impediments and challenges	Actions to address impediments	Organisation
Complexity and size of depositor records	Develop an IT-based reimbursement system that is scalable and expandable	FDIC, FSCS, HKDPB and MDIC
Different file formats submitted by banks	Issue Guidelines to banks requiring the submission of depositor records in a standard file format to MDIC on annual basis and upon request.	MDIC
	Insured banks are obliged to provide the DIA with a SCV for each depositor in accordance with the format requested by the DIA.	DIA (Albania)
	The FSA has introduced rules requiring all banks to introduce a SCV.	FSCS
	Banks are required to submit to the DIA depositor information in a standard file format within a 7 day time frame.	DIA (Russia)
	Issued a final rule (Large-Bank Deposit Insurance Determination Modernisation Rule) requiring Covered institutions <sup>32</sup> to adopt mechanisms that would, among others, provide the FDIC with deposit account data in a standard format.	FDIC
	Banks are compelled to submit information on insured deposits in a standard file format provided by IPAB or a self-designed format which complies with the Rules for Classifying Information regarding insured deposits.	IPAB
Lack of access to	The MDIC Act provides MDIC with unfettered	MDIC

<sup>32</sup> Covered institutions - defined as any insured depository institution with at least \$2 billion in domestic deposits and either (1) more than 250,000 deposit accounts or (2) total assets over \$20 billion, regardless of the number of deposit accounts

Impediments and challenges	Actions to address impediments	Organisation
deposit records in advance of a failure	access to depositor information at all times.	
	New powers to request more information in a timely manner and not just before an impending failure.	CDIC (Canada)
	The Banking Act 2009 introduced powers for the FSA and FSCS in respect of requesting information from authorised firms to enable the FSCS to undertake its functions effectively.	FSCS
	Put in place rules for compensation payout readiness to ensure that it is able to obtain all the necessary data from member institutions within 24 hours of notification.	SDIC
	Issued to its member institutions a guideline which specifies the format, structure and content of data that banks must provide to the HKDPB, including the timeframes within which various components of the information are to be delivered to the HKDPB.	HKDPB
Unable to undertake early or preparatory examinations of deposit liabilities in the event of an imminent reimbursement	The MDIC Act gives MDIC authority to undertake early or preparatory examinations of depositor information.	MDIC
Requirement for depositors to submit claims to MDIC delays reimbursement process	Subrogated to the rights of the depositor to the amount reimbursed. This eliminates the need for claim forms.	HKDPB and MDIC
	Abolish submission of claim forms and provide for automatic subrogation rights.	FSCS
Poor quality or incomplete depositor information records at banks.	Conduct validation of banks' premium computation annually and require banks to improve the quality of their depositor information and systems over time.	MDIC
Poor quality	Granted the right to inspect member institutions'	KDIF

Impediments and challenges	Actions to address impediments	Organisation
includes non-updated or inaccurate information	software, files and accounting maintenance in relation to their compliance with the legislation and the KDIF's requirements on insured depositors' records and file keeping.	
	Conducts regular on-site examinations to test bank data quality and accounting techniques.	DIA (Russia)
	Verifies that member institutions are ready, at all times, to submit complete and accurate data by reconciling account balances submitted during annual simulation exercises to members' accounting records and verifying randomly selected customers' deposit position produced by the SDIC's Payout System against member institutions' records.	SDIC
	Undertakes reviews of banks' compliance with the guideline on information required for determining and paying compensation, on a sample basis, using risk-based criteria.	HKDPB
	Developed an audit deposit information software to help the IPAB verify banks' compliance with the classification of information on insured deposits and conducts regular on-site examinations to test bank data quality.  Allow access to banks to verify the single customer view file.	IPAB  FSCS
Implement a "live" system that continuously functions	Issue Guidelines to banks requiring the submission of depositors' records in a standard file format to MDIC on annual basis as part of the submission for the assessment of premiums.	MDIC
Human errors in handling depositor data	The IT reimbursement system provides a seamless and automated process, for verifications and checks, with minimum manual intervention.	MDIC, FSCS
Lacks unique identifier to aggregate	Use the national identity card number as the primary identifier. Supplements with information on date of birth and addresses.	MDIC

Impediments and challenges	Actions to address impediments	Organisation
depositor accounts	Relies mainly on the Hong Kong identification card, passport and business registration numbers as the primary sources for unique identifiers.	HKDPB
	Stipulate detailed SCV requirements for the bank to be able to identify and aggregate accounts.	FSCS
Bank secrecy laws which restrict access to depositors' names	Require banks to mask or use encryption on specific information on depositor records when submitting depositor information annually to MDIC.	MDIC
Lack of appropriate communication strategies to deal with depositors	Implement an interactive call centre with access to a Single Customer View of all depositors to provide information, such as the list of deposit accounts and deposit products for each depositor, the insurability status of each deposit product, the insured and uninsured balances, reimbursement status and reimbursement method used depositors' mailing address, etc. The call centre employees would be trained to adequately address depositor queries and concerns.  Depositors could also have direct access to the above information via the internet (password protected).	MDIC
	Enhancing access to timely information through its "self serve" website.	CDIC (Canada)
	Measures include an MoU with the regulator to coordinate communication strategies during a payout; Q&As provided to call centre operators, and Payout website with template messages prepared in advance.	HKDPB
	Detailed contingency communications plans.	FSCS

Impediments and challenges	Actions to address impediments	Organisation
Inability to aggregate the insured and uninsured balances held by an eligible depositor	The MDIC IT reimbursement system is able to generate a Single Customer View of insured and uninsured balances.	MDIC
Lack of resources within the organisation to conduct a reimbursement	Adopt a Virtual Organisation (VO) resource structure where the core internal employees will be supported by specialised services providers, such as accounting firms, IT contractors, legal firms, payment agents and customer service agents providing reimbursement-related activities.	HKDPB, FSCS, MDIC and SDIC
Difficulty in the reconciliation of in-transit transactions	Establish working arrangements with Payment Systems operators to address issues relating to reconciliation of in-transit items.	MDIC
Readiness to undertake and complete a reimbursement	Develop comprehensive strategies, policies, processes and procedures and build core competent skill sets to perform reimbursements.  Periodical simulation and deposit validation exercise, training and development for designated personnel, as well as review of policies and procedures.	MDIC
	Carry out annual simulation exercises.	IPAB and SDIC
	Developed comprehensive strategies, policies and procedures and built core competent skill sets to perform payouts. As part of its continuous improvement process to ensure readiness, annual simulation and insured deposit validation exercises, training and development as well as reviewing of policies and procedures are key aspects of resource management.	CDIC (Canada)
	Developed detailed contingency plans, carry out planning and simulation exercises with the authorities.	FSCS

Impediments and challenges	Actions to address impediments	Organisation
<p>Complexity of coverage rules which include the following:</p> <ul style="list-style-type: none"> <li>• Netting of deposits against loans;</li> <li>• Computing accrued interest payable;</li> <li>• Splitting and disaggregating of joint deposit accounts; and</li> <li>• Determination of beneficiaries and their share of ownership of trust accounts</li> </ul>	<p>Coverage rules are kept simple to ensure that the computation of depositor entitlement can be made easily and quickly, as follows:</p> <ul style="list-style-type: none"> <li>• No netting requirement;</li> <li>• Require banks to compute interest on a daily basis;</li> <li>• No disaggregation of joint accounts. The MDIC Act provides that joint accounts are separate and distinct deposits. Reimbursement is made in the joint names of depositors as stated in the joint account; and</li> <li>• Require banks to ensure that they have a data management system to record trust account information, including beneficiaries and their entailments, and that this information be updated frequently.</li> </ul> <p>• Set-off requirements have been abolished (and insolvency rules amended).</p> <ul style="list-style-type: none"> <li>• Eligibility rules simplified.</li> <li>• Removal of claim form.</li> <li>• Banks are required to supply figures for interest calculated up to the date of default as part of the SCV.</li> <li>• For beneficiary and trust accounts, the banks must flag such accounts on their systems.</li> </ul> <p>• The Payout System includes built-in interest calculations for simple products while legislative change has been proposed to allow approximate interest calculations for complex products.</p> <ul style="list-style-type: none"> <li>• Member institutions are required to indicate trust/client accounts. The HKDPB will request beneficial/client interests from account holders for ownership determination.</li> </ul>	<p>MDIC</p> <p>FSCS</p> <p>HKDPB</p>
<p>Unable to determine insurability of deposit products during a reimbursement</p>	<p>Banks are required to undergo a product insurability certification process whereby MDIC will verify and certify the insurability status of each and every deposit product prior to its launch.</p> <p>Depositors are to be informed of the insurability</p>	<p>MDIC</p>

Impediments and challenges	Actions to address impediments	Organisation
	status of deposit products at the point of sale.	

Source: IADI Case Study: MDIC's Experience in Designing and Developing an Effective Reimbursement System. Information Paper: IADI Survey on Effective Reimbursement Systems

## **Annex II**

### **Developing Effective Reimbursement Systems and Processes: IADI Discussion Paper**

[http://www.iadi.org/docs/Discussion\\_paper\\_-\\_Developing\\_Effective\\_Reimbursement\\_Systems\\_a.pdf](http://www.iadi.org/docs/Discussion_paper_-_Developing_Effective_Reimbursement_Systems_a.pdf)