

Deposit Insurance of Vietnam: Are there implications for Australia?

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Abstract

Recent inquiries into aspects of the Australian financial system have canvassed the possibility of deposit insurance not only for deposits at approved deposit-taking institutions but also funds held in life and general insurers. The number of countries introducing deposit insurance schemes is growing steadily, with the total world-wide now standing at 94 countries. With three of the most recent additions being in our region, Hong Kong, Singapore and Vietnam, it is timely to investigate the potential of adding deposit insurance to the range of deposit protection tools available to the bank regulator in Australia.

This paper first explains the principles of deposit insurance using examples from around the world. It then explains the advantages and disadvantages of deposit insurance, including techniques to address some of those disadvantages. The paper then draws on the personal experiences of the Director of one of the branches of Deposit Insurance Vietnam (DIV) in implementing their deposit insurance scheme over the last 5 years. The Director outlines the successes and areas for improvement in their Scheme.

The paper then concludes that the deposit insurance scheme as proposed by the Council of Financial Regulators in Australia should be implemented, with some suggested modifications.

Introduction

Globalization and improved communication systems are bringing economic opportunities to individuals, organizations as well as nations. Nearly a decade ago the Reserve Bank of Australia (RBA) had expressed concern that this would lead to consumer opportunities to deal unwittingly with institutions of lesser quality (RBA 1997). Because the banks and other financial institutions play an intermediary role between consumers and the financial markets, their depositors can no longer be isolated from the failure of these financial institutions in another country, simply by dint of domestic regulation.

The Asian financial crisis of 1997 illustrates how quickly contagion risk may spread and its devastating affect at national and international levels. Delhaise (1998) identifies five countries that bore the major impact of the Asian Financial Crisis: Thailand, Korea, Indonesia, Malaysia and the Philippines. Additionally he identifies effects flowing into the financial systems of China, Taiwan, Singapore, Hong Kong and Japan. The Asian financial crisis also had an impact on the banking activities of Vietnam and amongst other factors, led to the creation of the Deposit Insurance of Vietnam which commenced operations on 7th July 2000 (DIV 2005).

Depositor protection usually takes the form of one or more of the following:

- i. Insurance of small deposits through some form of deposit insurance scheme;
- ii. Lender of last resort facilities through a central bank;
- iii. Priority given to depositors where a bank wound up; and
- iv. Power for a regulatory body to take over and manage a bank in financial difficulties or one that is about to fail.

Australian depositors, first through the RBA and now the Australian Prudential Regulation Authority (APRA), have the protection of all but the first. The Federal Deposit Insurance Corporation (FDIC) in the USA has powers i. and iv. whilst the Federal Reserve exercises the lender of last resort facility (Koch & MacDonald 2006). It appears that uninsured depositors do not rank ahead of other creditors and therefore the FDIC does not have the power to repay depositors in priority to all other creditors.

Recent inquiries in Australia including The Financial System Inquiry (RBA 1997) and the Royal Commission into HIH collapse (APRA 2002), have canvassed deposit insurance for small depositors.

Kyei (1995) separates deposit insurance schemes into implicit and explicit. Implicit being those deposit insurance schemes “for which it is taken for granted, or assumed on the basis of past experience, that the government is bound to take steps to protect the banking system.” On the other hand he defines explicit schemes simply as those for whom formal arrangements have been established to protect deposits.

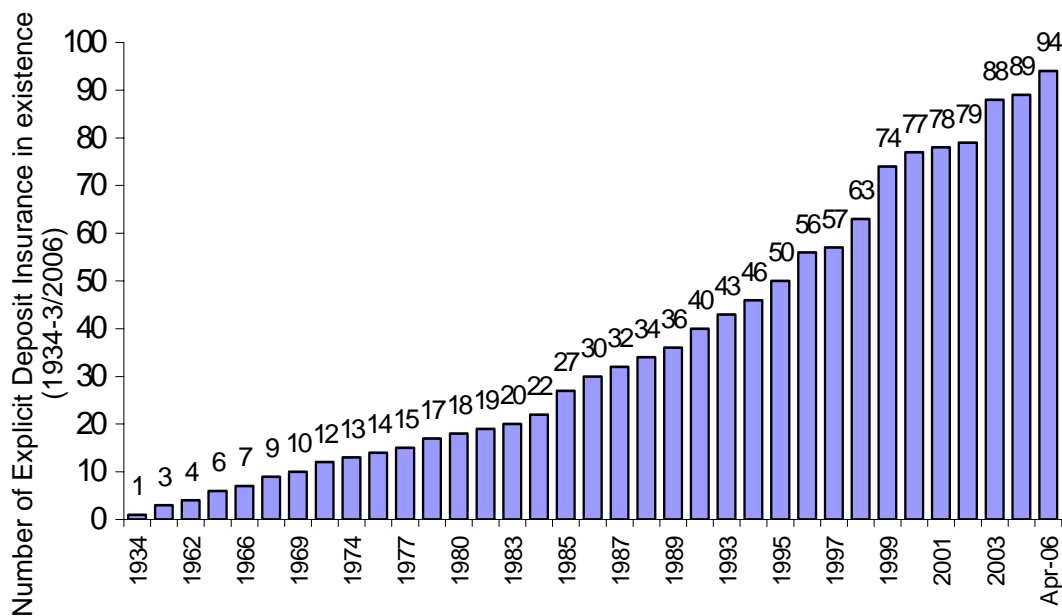
A survey this year for the Reserve Bank of Australia (RBA) found that 60% of Australians surveyed believed their main deposit account had a guarantee or that it would be protected by the Government in the event of their bank failing (RBA 2006). The Banking Act 1959 (as amended) under Division 2, Subdivision A Section 12 charges APRA with the duty to protect “the depositors of the several ADIs” subject to APRA’s jurisdiction, this is not a deposit guarantee. Previously when the RBA was the sole bank regulator in Australia, it expressed concern at the identically worded Section in the then Banking Act 1959 because it lacked transparency in: not guaranteeing full repayment of deposits; not defining what constituted deposits; not specifying if all holders of those deposits were protected regardless of their size or financial sophistication;

and in not guaranteeing prompt repayment of deposits (RBA 1997). In other words, Australia has at best an implicit deposit protection scheme.

On the other hand, an explicit deposit insurance policy is understood to be a transparent public commitment of the insurer to repay principal and interest to depositors in the event that the insured institution should fail and is insolvent. In fact, the public commitment is in the form of a tripartite insurance policy: the deposit insurer, the financial institution and their depositors.

Chart 1 shows the growth in explicit deposit insurance schemes world-wide. Recently at least three neighboring countries have introduced deposit insurance schemes: Vietnam in 2000 (DIV 2005), Hong Kong in 2003 (The Asian Banker 2003) and Singapore 2006 (MAS 2006).

Chart 1. Explicit deposit insurance schemes in existence



Source: IADI, 2006

This paper will concentrate on the features of deposit insurance schemes with particular emphasis on the recently introduced and largely unknown scheme of Vietnam. The paper will then recommend if a deposit insurance scheme should be adopted in Australia and if so, the form the authors believe it should take.

What is Deposit Insurance?

Broadly, deposit insurance schemes guarantee the return of capital and interest on small deposits with banks and other regulated financial institutions. The Council of Financial Regulators in Australia calls these capital certain promises (RBA 2006). This distinguishes these deposits from those where the creditor accepts some risk of non-return of capital due to fluctuating market prices.

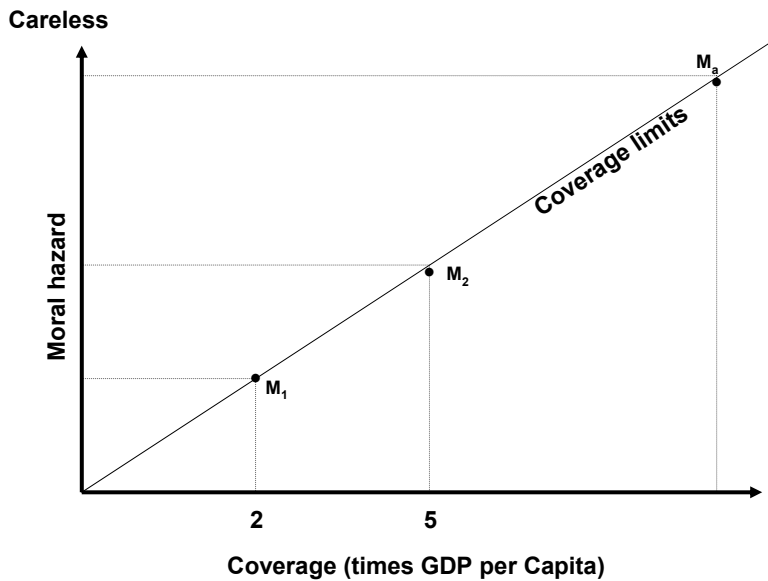
Maximum coverage

Since most schemes are designed to protect only the less sophisticated depositors and to limit the insurer's exposure, there is usually an upper limit on the capital certain promise covered. Chart 2 demonstrates that depositors' overview of their depository institution decreases with the relative increase in the amount of their cover. In other words, as the upper limit of deposit insurance increases, moral hazard by depositors also increases.

Chart 3 demonstrates the divergence in the upper limit of coverage around the world, with the average coverage being about 3 times GDP per capita. The FDIC in the USA has one of the best coverage with a maximum of \$100,000 per depositor, per financial institution (Koch & MacDonald 2006). Cover in most other countries is less than half this amount with only the coverage in Italy and Norway exceeding the USA (Garcia 1999). The FDIC has recently increased its upper limit to \$250,000 for certain retirement accounts (FDIC 2006). As practiced in

the USA, the coverage limit should be adjusted over time, perhaps to reflect higher GDP per capita and inflation, so that the scheme's coverage remain relevant.

Chart 2. **Determination of maximum coverage**



M_1 : Recommended coverage (Ketcha 1999 p. 229)

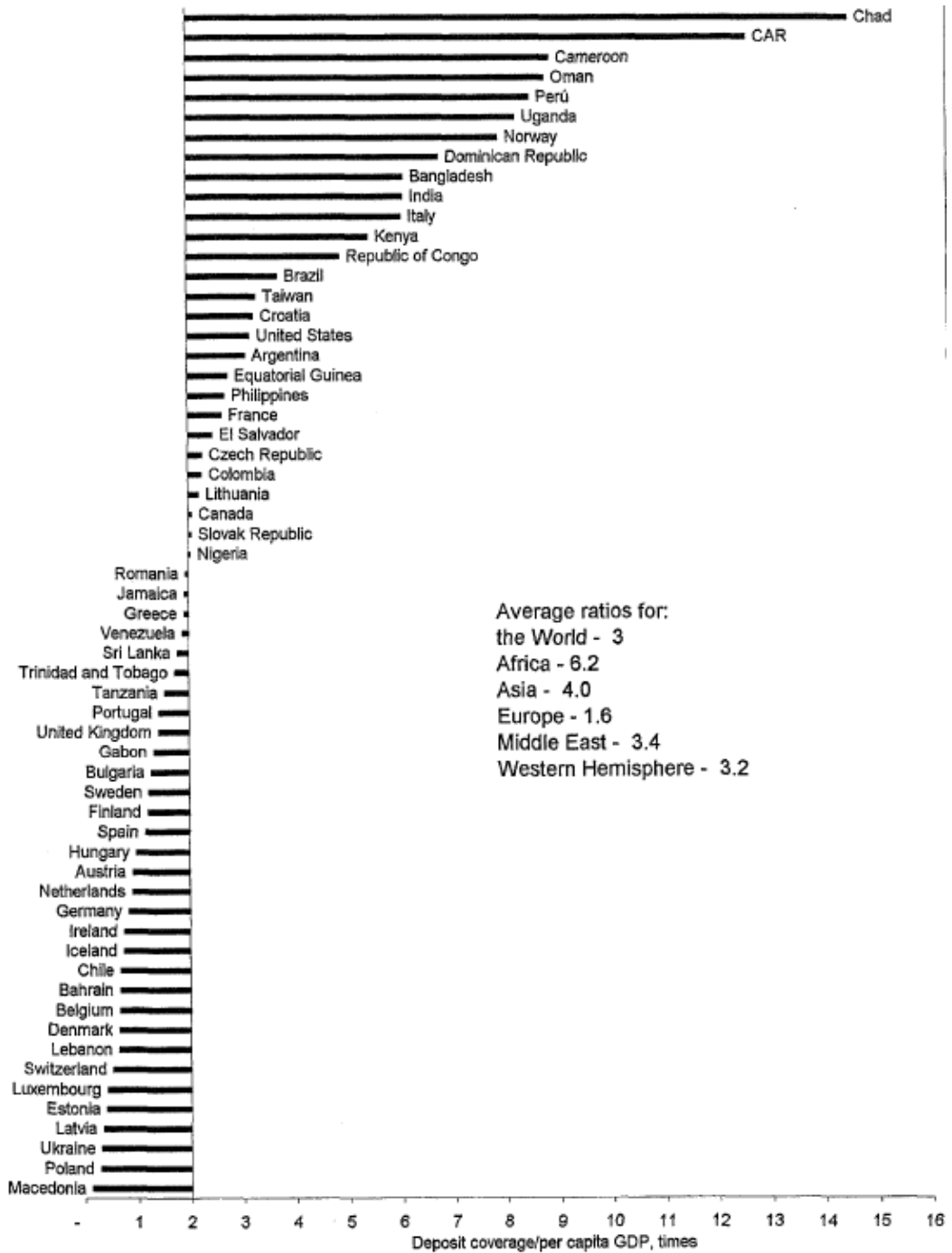
M_2 : Maximum coverage in Vietnam as of 2000

M_a : Blanket coverage (no limit)

Co-insurance

Additionally there may be some loss-sharing by the depositor up to that maxima. This is referred to a co-insurance – the depositor will lose some of their capital certain promise in the event of a bank failure. In most countries outside the European Union, including the USA, deposits are insured for 100% up to the maximum limit. However in the European Union there is co-insurance with depositors generally only covered for 90% of their insured deposits (Garcia 1999).

Chart 3. Ratios of Deposit Coverage to per capita GDP in Selected Countries, 1999



Source: GDP per capita for 1998, WEO.

Source: Garcia, 1999, p. 49

Deposit Accepting Institutions Covered

There is also a divergence in the breadth of financial institutions at which deposits are insured.

The FDIC only covers deposits with commercial banks and thrifts, with credit unions in the USA having their own separate scheme (Koch & MacDonald 2006). Singapore's new deposit insurance scheme includes deposits with finance companies (MAS 2006) whilst the scheme mooted for Australia includes deposits with credit unions, building societies and premiums paid on general insurance (RBA 2006).

Form of deposits covered

The form of deposits covered also varies significantly. For example many countries exclude foreign currency deposits; those of other financial institutions; or those of directors, significant shareholders and subsidiaries. On the other hand some countries cover all deposits (Garcia 1999).

The aims of deposit insurance

Deposit insurance is considered as only one mechanism of a financial safety net which can contribute to the stability of credit institutions and ensure the safety and soundness in their operations by protecting the interests of depositors.

Choi (2000) identifies the following aims of deposit insurance:

- i. To protect depositors, especially small depositors who are less financially sophisticated or those who find it hard to assess the financial conditions of banks and their governance;
- ii. To contribute to the maintenance of stability of the financial system and make the financial transactions more efficient by preventing bank failures;

- iii. To develop a competitive and fair market for financial institutions that differ widely in size and development level in order to reinforce the renovation of banking operations; and
- iv. To clarify the responsibilities and rights of both depositors and credit institutions and
- v. To minimize the burden on taxpayer in the case of bank failures.

The role of deposit insurance

The critical role of deposit insurance is to foster an appropriate combination of objectives that improve the quality of banking operation, maximize the attraction of temporarily un-used funds from the community and encourage the active participation of the community through the principle of mutual benefit. Therefore, favorable conditions for steady economic development can be created. In short, the role of deposit insurance toward a nation can be indirectly expressed through its intermediary role in the nation's financial system, which can be summarized in three aspects: (i) contributing to strengthening public confidence in national banking system, (ii) creating favorable conditions for the development of the national banking system, (iii) promoting savings mobilization for investment and sustainable development.

Countries such as Australia without deposit insurance believe their financial systems to be robust without the need of deposit insurance (Cornell 2006). However the IMF claims that to wait until a crisis is imminent or in progress before acting to protect depositors will not prevent a flight to quality of deposit funds, or worse, a flight from the currency. (Garcia 1999). Thus a deposit insurance scheme should be introduced before a banking crisis occurs.

Risks of Deposit insurance

While deposit insurance is considered as one tool to enhance the stability of a nation's banking system, it also has potential risks. Garcia (2000) identifies three types of risks in deposit insurance: (1) Moral hazard, (2) Adverse selection, (3) Agency problems.

Moral hazard

Moral hazard arises with both the depositor and the management of the financial institution. Both can lead to adverse effects on deposit insurance scheme and threatens the safety of the banking system.

Depositor moral hazard is caused by their negligent or mercenary selection of banking services. For example, when deposits are insured or they believe that their deposits are insured, depositors will be careless in accessing and collecting banking information to monitor the condition of their bank or financial institution. Thus, some weak banks may be able to mobilize deposits at interest rates that are not comparable with the corresponding risk level.

Moral hazard within financial institutions occurs when insured banks believe that the failure of their bank could not be happened or in the event it occurred, that no one will lose they funds. Therefore a bank may accept a high-risk level in its operations, or reduce capital and reserve fund, putting itself in a more difficult position in dealing with liquidity problem, especially in case of a banking crisis.

Moral hazard may therefore affect the supply and demand of deposits and bring a harmful impact to the operational stability of a banking system.

Moral hazard within the financial institution may be addressed in either of two ways: co-insurance; and/or discriminatory pricing of coverage

Co-insurance

The use of co-insurance is aimed at addressing moral hazard. Under this arrangement depositors will lose some of their deposit in the event of bank failure. This encourages depositors to apply market disciplines toward deposit-taking institutions through requiring interest rates weighted according to the risk to their deposits. By placing a limit on the maximum deposit coverage, financial institutions will face greater scrutiny from these large, presumably more sophisticated depositors. Additionally, from the bank's point of view, there will now be significant losses not met by the deposit insurance scheme which should temper their risk strategies.

As a result, deposit insurance can enhance indirectly the monitoring and regulating mechanisms of banking operations.

Discriminatory pricing

Most newly established deposit insurance systems initially adopt a flat - rate premium system due to its ease of implementation. In addition, most systems require that mandatory membership is applied for all institutions located in the country to reduce the incidence of adverse selection. Cull (1998) found that deposit insurance systems adopting flat-rate premium will encourage their member bank in excessive risks taking.

Risk-adjusted differential premiums are an unavoidable trend for deposit insurance systems. The application of a risk-adjusted premium system provides a fair mechanism for dealing with all insured institutions and indicates market tendency in deposit insurance's operation. Consequently, it encourages member banks to practice more prudent risk-management in order to incur lower premiums. Moreover, risk-premium systems can mitigate moral hazard arising from flat-rate system because high-risk banks will incur higher premiums.

From January 1 1993 the FDIC in the USA adopted a risk-based premium system, with well run banks paying no premium (FDIC, 1998). By the end of the decade, 93.3% of all banks insured by the FDIC paid no premium. The FDIC's income comes from the remaining risky banks and income earned on capital, aided by the low bank failure rate (Koch & Macdonald 2006).

Adverse selection

First of all, the cost of the deposit insurance scheme is born by the insured financial institution. However, insured institutions themselves should have a clear understanding about their activities and the risk level of those activities. Financial institutions may not want to participate in deposit insurance, particularly strong institutions who operate with low-risk levels, and have good creditability and good financial standing. Australian banks perceive themselves in this position (Cornell 2006). On the other hand, weaker banks or those with higher risk levels normally need to be insured to promote credibility and to protect themselves from risk. In other words, they seek to transfer their risk to the deposit insurer.

In countries with voluntary membership of their deposit insurance schemes, the insurer will not always have current and exact information on the banks, even in the case of banks they do insure. Therefore, the deposit insurer may make mistakes by accepting weak institutions under its cover, or allowing the sounder institutions under its cover to deteriorate. Thus the deposit insurer is facing adverse selection, with a disproportionate coverage of weak financial institutions.

Adverse selection creates an immediate financial risk for the deposit insurer and it also breaks mutual community mechanisms which are aimed at ensuring sustainability of deposit insurance. Hence, mandatory membership of the deposit insurance scheme should be required of all deposit-

taking institutions located in the country. Also, this is an argument for locating the deposit insurance function within the bank regulator, rather than as a separate regulatory body.

Agency problems

Deposit insurance is assessed as effective when it achieves its stated main objectives. In order to achieve these objectives, the following aspects of deposit insurance need to be taken into account:

(i) Organizational type, (ii) Operational fund, (iii) roles and functions of the deposit insurance agency. Agency problems appear when these aspects of a deposit insurance are not adequately applied.

Organizational type

The deposit insurer cannot fulfill its role and functions if it is not independent in its operations; does not have adequate financial resources; and does not have a strong and highly effective legal framework. Choi's (2000) found that for a deposit insurer to operate effectively and efficiently, it had to earn the confidence of the public. For this reason, the deposit insurance system should be a public and non-profit institution. With this kind of organization, depositors and financial institutions should enjoy the lowest cost of insurance and have the confidence of sufficient financial backing to meet any emergency.

A non-government sponsored deposit insurance system may only be possible in those countries that have a fully developed banking system, where the market disciplines are applied strictly; the banks have a large capitals base; and there is a strong legal framework for fair competition.

Australia would appear to meet these criteria.

Operational Funding

Funding for the deposit insurance scheme needs to be adequate to fund the insurer's normal supervisory activities; to allow for timely assistance for insured institutions; and for immediate reimbursement of insured depositors when an insured institution fails.

If the funding of the deposit insurance agency is inadequate, depositors may lose confidence in the whole financial system, leading to closure of otherwise sound financial institutions.

This has been a rare event but in the US, from 1907-1930, deposit insurance programs in eight states were closed as insurers were unable to meet all claims (FDIC 1998). Another scheme in Rhode Island failed in 1991 after 45 state-licensed banks and credit unions failed (*The Australian*, "Uncle Sam to pump \$1bn into institution", 8/1/1991, pp. 13)

Roles and functions of deposit insurance agency

Inadequately stipulated roles and responsibilities of the deposit insurance agency and ineffective implementation of these provisions will hinder the deposit insurance agency in achieving its aims. If the deposit insurance agency's role is only to merely manage funds to compensate insured depositors of failed banks, it will not achieve its purposes in a banking crisis.

Consequently in many countries the deposit insurance function is just part of the duties of the bank regulator.

In the USA for example, the FDIC supervises all State licensed banks as well as providing insurance coverage to these same banks and all Federally licensed banks. The scheme in Vietnam also incorporates bank supervision and regulation within Deposit Insurance Vietnam. The scheme mooted by the Council of Financial Regulators in Australia proposes that the deposit insurance

function be incorporated under APRA (RBA 2006). On the other hand, the new scheme implemented in Singapore has been established as a separate body (MAS 2006).

In this paper we will ignore the regulatory role of the deposit insurance agency.

Development of human resources

Until recently, the awareness of the roles and procedures to establish deposit insurance schemes were independently developed in each country. It was only in 2003 that the International Association of Deposit Insurer was established to foster the development and research into the effectiveness of deposit insurance schemes (IADI 2006). This is particularly important for developing countries such as Vietnam with a limited supply of skilled resources and where the insured institutions have a higher level of sophistication and technical expertise than the insurer.

In this context, deposit insurers need human resource development strategies to both respond to the requirement of bank depositors but also the insured institutions.

Deposit Insurance of Vietnam (DIV)

The establishment and development of DIV

Deposit protection in Vietnam had its foundations in the national renovation plan of 1988 designed to reduce inflation and consolidate the public confidence in Vietnam's banking system. Unfortunately this led to the systemic failure of the rural people's credit funds and the urban people's credit funds in the period 1988-1990. The deployment of deposit insurance activities after rebuilding the people's credit funds is considered to be the first explicit deposit insurance operation in Vietnam. However this developed slowly and revealed many shortcomings in achieving the key elements of success expected.

The financial and monetary crisis in the Asia - Pacific region in 1997 partly affected the banking activities of Vietnam. Furthermore, whilst the trend towards regional and international integration brought many opportunities to the Vietnamese banking system, it also raised many challenges and risks.

Accordingly, Article 17, Item 1 of the Law on Credit Institution published in 1997 required “Credit Institutions ... to participate in a deposit guarantee or deposit insurance organization” to protect the rights of depositors. This required the State to establish a true deposit insurance organization and Deposit Insurance of Vietnam (DIV) commenced operation on 7th July 2000.

Key objectives and major activities

DIV is a State owned financial institution established under the Prime Minister’s Decision with a view to: (1) protecting legitimate rights and interests of depositors, (2) contributing to the maintenance of the stability of credit institutions and (3) ensuring the safe and sound development of the banking activities.

The main operations of DIV are as follow:

- i. license new deposit institutions, issue supplementary deposit institution licenses and withdraw deposit institution licenses;
- ii. Collect insurance premium;
- iii. Monitor, supervise and inspect the compliance with the Decree of the Government on Deposit Insurance and prudential regulations on banking operations of the insured Institution;
- iv. Reimburse depositors within the regulated limitation of cover;
- v. Debt collection for financial institutions in liquidation;

- vi. Publicize and popularize the deposit insurance activities of DIV;
- vii. Provide financial assistance for insured institutions; and
- viii. Provide financial investment from idle capital in order to protect the capital allocated by the State and cover its expenses.

The organizational structure of DIV includes: the Board of Directors, the Board of Management, Departments of Head Quarter and 6 Regional Branches.

Funds for operations

Initially, the chartered legal capital of DIV allocated by the Government were VND 1,000 billion divided in to batches with the final installments on 21 May 2003. Initially with only its charter legal capital around VND 424 billion, DIV faced difficulties. As of 31 December 2004, its operational fund was VND 1,635 billion including its charter legal fund of VND 1,000 billion and the operational provisioning fund of VND 508 billion. The operational provisioning fund was formed mainly from collected insurance premiums over the past 5 years and has been used for reimbursement of insured deposits (DIV, 2004).

The Operations of DIV

Participants

Participating in the deposit insurance scheme is compulsory, at the present for the following types of institutions:

- i. State-owned commercial banks;
- ii. Joint-stock commercial banks;

- iii. Joint-venture commercial banks;
- iv. Branches of foreign banks;
- v. Finance companies;
- vi. finance lease companies;
- vii. People' credit funds.

There are 972 banks participating in the Vietnamese deposit insurance scheme as of March 2006.

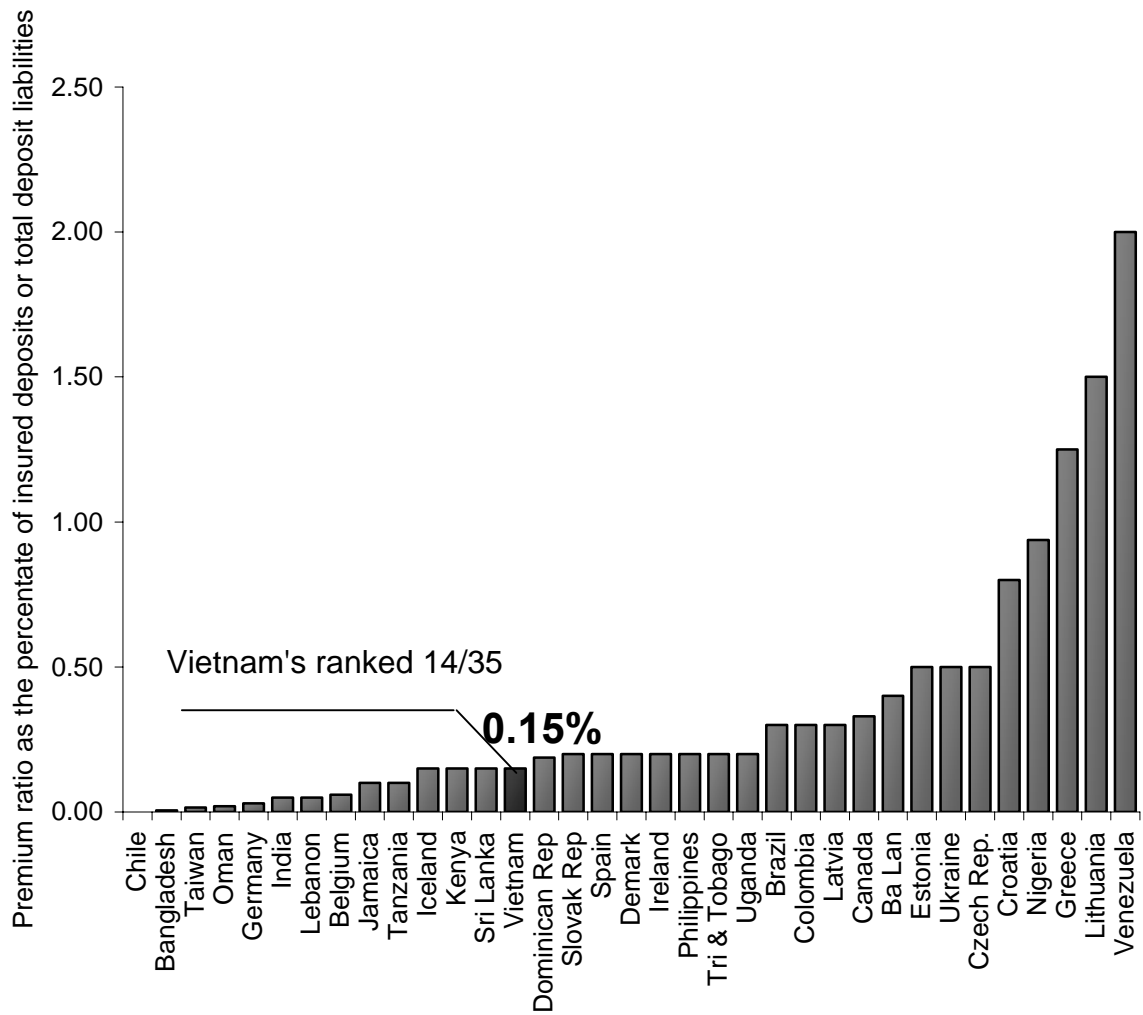
Premium

Insured institutions are required to pay a flat rate annual deposit insurance premium of 0.15% of total insured deposits at each insured institution. This cost of deposit insurance is at the lower end of flat-fees charges around the world as Chart 4 show.

Maximum coverage

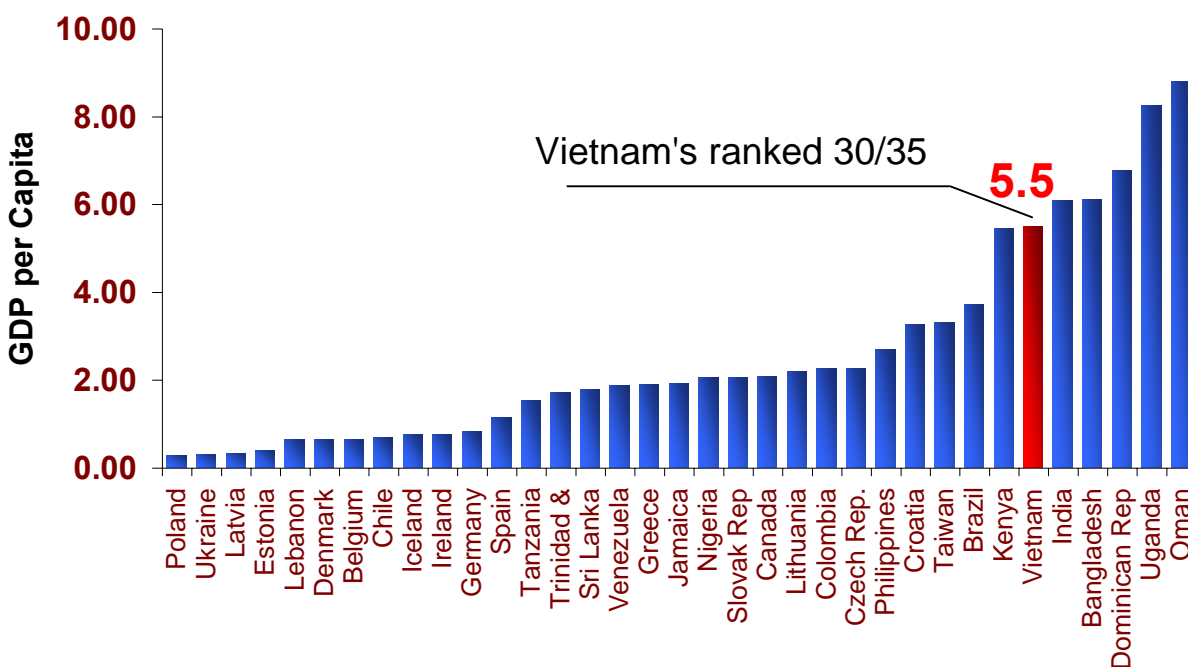
Until 19th September 2005, according to Decree N°89 of Government (ND89/CP), the maximum deposit insurance coverage for all deposits (including principal and interest) of an individual at an insured institution was VND 30 million (around US\$1,900). Due to the difference of purchasing power of country currency, to compare the level of maximum coverage from one scheme to other one, GDP per capita is commonly used.

Chart 4: **Flat premium of 35 selected schemes**



Source: Kunt and Sobaci, 2000

Chart 5: Maximum coverage of 35 selected schemes



Source: Kunt and Sobaci, 2000

At the time of establishment, the coverage of the Vietnamese scheme was ranked 30th out of 35 selected schemes (see chart 5).

Following Decree N°109 of Government (ND109/2005/ND-CP) the maximum deposit insurance coverage has now been increased VND 50 million per insured institution (around US\$3,200).

Type of insured deposits

Deposits insured are those in local currency only, for individuals, households, co-operative associations, private enterprise, and partnership companies, except some principal cases according to regulation in Decree N°109/2005/ND-CP.

Achievements after 5 years' operation

The following achievements relate to both DIV's off-site and on-site supervisory activities, not purely limited to its deposit insurance function:

- i. DIV has contributed to the implementation of the national renovation policy, especially in the financial markets by:
 - a. protecting the legitimate interests of depositors;
 - b. maintaining the stable growth of the insured institutions;
 - c. ensuring the safe and sound development of banking operation; and
 - d. ensuring social and political stability through the mobilization of internal resources for socio-economic stability and development.
- ii. DIV has given bank depositors a sense of safety during bank runs in 2003 (Phuong Nam Bank) and 2005 (ACB Bank).
- iii. The prompt payment of insurance money to 1,476 depositors at 33 people credit funds in 10 cities and provinces; and
- iv. prompt fund mobilization particularly in the case of Peoples Credit funds that started the banking reforms.

Difficulties and challenges of DIV

- Firstly, the legal infrastructure is inconsistent with DIV's mission and International standards.

- Secondly, the subject, scale and content of deposit insurance operation is currently too narrow, with the role of DIV being not fully reflected in the risk control systems of the national financial system.
- Thirdly, the financial capacity of DIV are still limited.
- Fourthly, some of DIV's staff lack the necessary knowledge and experience to identify risks in advanced banking systems.
- Fifthly, at present, there are still a number of insured institutions and depositors in Vietnam unaware of how important the deposit insurance operations are in maintaining the stability and development of individual financial institutions as well the nation's financial system.

Strategies for future development

After 5 years' of operation, these first achievements of DIV have been significant and have contributed greatly to the confidence in the nation's banking system. Despite this, the deposit insurance operations still require further development:

- i. Strengthening of the legal infrastructure to better implement deposit insurance operation;
- ii. Strengthening financial capacities (implement comprehensive activities by suitable route, capital mobilizing structure and capital investment)
- iii. Implementing effective activities in order to obtain basic objectives of deposit insurance policy;
- iv. International cooperation in developing deposit insurance operation;
- v. Improved human resources capacity in deposit insurance operations; and

vi. Applying technological science to data analysis.

Implications for depositor protection in Australia

Australia can no more isolate its financial markets from the impact of internationally transmitted financial crisis than Vietnam can. According to APRA (2006), Australia currently has 180 locally owned approved deposit-taking institutions. It is inconceivable that the smallest credit union or building society can be staffed by equally highly qualified staff as the major banks. It is therefore inevitable that at some point in time, one or more financial institutions in Australia will fail.

When this happens the 60% of Australians (and opportunistic politicians) who believe we have an explicit deposit protection scheme, will call for protection for those depositors faced with loss of their life savings. We have seen this recently with investors in the failed WestPoint group of companies calling for support for lost funds (McCarthy 2006); and in the 1980s with the collapse of Tricontinental which led to massive losses by the State Bank of Victoria and brought down the State Labor government (ABC 2003). Neither of these groups were supervised by the bank regulator but that didn't stop a call for protection for those losing their life savings. Imagine if it were a bank supervised by the Australian Prudential Regulation Authority!

The IMF has recently completed its assessment of the Australian financial sector and is now expected to report in September 2006. At the time of writing, it is expected this report will highlight deficiencies in the failure and crisis management procedures within our financial system, notably the lack of a depositor protection scheme (Cornell 2006). As we have already pointed out above, the IMF is also of the view that it is too late to implement such protection after failure has occurred or is imminent.

Consequently we believe Australia should adopt an explicit deposit insurance scheme as soon as possible based along the lines proposed by the Australian Council of Financial Regulators (Davis 2005) but with variations as noted below:

- i. The Scheme to be established under the existing regulatory structure within APRA such that there is one supervisor as in Vietnam;
- ii. The funding of claims against the Scheme will be by the Treasury of the Australian Federal Government which will be reimbursed from sale of the assets of the failed ADI. Any deficit will be shared amongst the ADIs in proportion to their insured deposits.
- iii. The costs of administering the Scheme will be funded by a levy based upon each ADIs proportion of their insured deposits.
- iv. We also believe that the scheme should be limited to ADIs authorized by APRA unlike the Council of Financial Regulators who proposed that it be extended to claims by policy holders of life and general insurers.
- v. The Scheme should apply to retail deposits of less than \$50,000 per person, per institution. Here we differ from the recommendation and believe claims should be limited to retail deposits of individuals and small businesses using the same definition for small business that applies in the Code of Banking Practice. Deposits in excess of the \$50,000 limit will still rank in priority to all other creditors as at present, but will not receive prompt repayment of their deposit and will be subject to the availability of assets. The proposed limit is between 4 and 5 times average GDP per head of population as at 30th June 2006 (ABS 2006).
- vi. The maximum claim per person should be limited to 90% of the insured deposit in common with the European Union, to address moral hazard issues. The unpaid 10% of

deposits will still rank in priority to all other creditors as at present, but will be subject to the availability of assets.

- vii. Finally, a time frame for payment of insured deposits should be defined in the terms of reference and we suggest a period of 5 working days in line with recent achievements by the FDIC in the USA (FDIC 2002).

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