

## **Proposed Research Plan for: Developing Comprehensive Guidance for Governance of Deposit Insurance Systems**

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### **Request for Comments and Submissions**

Deposit insurers and other interested parties are asked to comment on their experiences as they relate to “Issues to Be Addressed” below. Individuals and organizations that would like to submit a paper on the issues raised in this Business Plan are requested to inform David Walker at [dwalker@cdic.ca](mailto:dwalker@cdic.ca) or Joshua Lattimore at [jlattimore@cdic.ca](mailto:jlattimore@cdic.ca) by 8 May 2006.

### **Purpose**

To develop comprehensive and detailed guidance on the governance of deposit insurance systems.

### **Introduction**

Governance can be said to refer to the processes, structures and information used for directing and overseeing the management of an organisation. Importantly, governance speaks also to the framework through which a deposit insurer balances its independence against its accountability to a higher authority. A strong governance framework is thus an integral component of a deposit insurance system’s ability to fulfill its objectives and mandate effectively. An effective deposit insurer with a strong governance framework can also help reinforce financial system stability.

A deposit insurance system can be governed in a number of different ways. Some are set up as government departments, while others are established as separate government agencies or state-owned enterprises. Others still are run entirely in the private sector, usually by industry associations of deposit-taking institutions. Whatever structure a deposit insurance system takes, governance largely remains a matter of direction, oversight and accountability.

Within this overarching concept of direction, oversight and accountability, a number of important issues are worthy of consideration. The Financial Stability Forum’s Working Group on Deposit Insurance laid out four such issues in its 2001 background document on Structure and Organisation of Deposit Insurers. They are: form of governance system; the composition of the governance body and its duties and responsibilities; internal control processes and mechanisms; and the development of appropriate

transparency and disclosure regimes. In addition, work by the APEC Policy Dialogue on Deposit Insurance in 2004, which was subsequently adopted as guidance by the International Association of Deposit Insurers (“IADI”), stresses the importance of independence, accountability, integrity and transparency as critical components of the governance framework for a deposit insurance system.

Given the importance of good governance in building an effective deposit insurance system, there is a need for detailed and comprehensive guidance in this area. In order to develop such guidance for countries considering the establishment of a deposit insurance system or the enhancement of an existing deposit insurance system, the International Association of Deposit Insurers (“IADI”) proposes to develop a discussion paper to set out comprehensive guidance in this area.

The main focus of the paper will be (1) to identify the different types or forms of governance systems used by deposit insurance systems; (2) to explore the relevant governance issues for a deposit insurance system; (3) to examine the advantages and disadvantages of various approaches to governance; and (4) to provide guidance on appropriate practices in governance for a deposit insurance system taking into account the different types of systems that exist. The following research plan sets out an initial list of key issues to be addressed in the proposed discussion paper.

### **Issues to Be Addressed**

#### **Form or type of Governance System**

1. What forms or types of governance structures exist for a deposit insurance system (e.g. government departments, separate government agencies, state-owned enterprises, private industry associations.)?

#### **Methods of Direction, Oversight and Accountability**

2. From what types of authorities (e.g. legislatures, central banks, supervisory agencies, Ministers of Finance, industry associations) does the deposit insurance systems receive its mandate and powers?
3. Through what means does the deposit insurer receive its mandate (e.g. through legislation, a formal periodic statement from the government or industry association, a memorandum of understanding)?
4. To what types of authorities is the deposit insurance system held accountable (e.g. deposit insurance systems accountable to central banks, supervisory agencies, departments of finance, Ministers of Finance, legislatures, or industry associations)?
5. What form does this accountability reporting take (e.g. reporting through corporate plans, annual reports, annual general meetings)?

## **Degree of Independence**

6. What mechanisms exist to protect a deposit insurance system against undue political, industry or other interference?
7. In what ways is the deposit insurance system's degree of independence balanced against the need for the system, its governing body, and/or senior executives to be accountable to the authority from which the deposit insurance system receives its mandate, and to member banks?
8. Does the deposit insurance system have the authority to summon the supervisor to explain its actions in respect of a failed or troubled bank?

## **Composition of the Governance Body and its Duties and Responsibilities**

9. What is the composition of the deposit insurance system's governing body?
10. What types of sub-committees are common across deposit insurance system governing bodies?
11. Who selects members of the governing body and management? How long are membership terms of governing body members, chair persons, chief executives, and other senior officers?
12. What are common types of qualifications, skills, or sector-based requirements for governing body members?
13. What are the selection and appointment processes for governing body and leadership positions (e.g. Chairpersons and Chief Executive Officers)? What role does the governing body play in the appointment, performance evaluation, remuneration, and succession of the Chief Executive Officer?
14. In the case where a deposit insurance system is governed by a board of directors, are the positions of Chairperson and Chief Executive separate from one another? What are the advantages and disadvantages of the separation of those positions?
15. What are the roles of the deposit insurance system governing body (e.g. board) vis-à-vis management? In what ways are these roles defined?
16. To what extent is the deposit insurance system's governing body able to rely on the work of its own staff? What are the advantages and disadvantages of a governing body being able to rely on the work of its own staff versus outsourcing functions to other organisations?

17. To what extent are the governing body's responsibilities and its expectations of management codified in governance policies or charters? Where such policies or charters exist, what key concepts do they describe?
18. What role does the governing body play in setting deposit insurance system strategy and objectives?
19. What role does the governing body play in the management of significant risks (including non-insurance related risks) faced by the deposit insurance system? How does management support the governing body in its risk management oversight role?
20. Are potential conflicts of interest a concern with respect to members of the deposit insurance system governing body? If so, how are they dealt with?
21. In cases where a given governing body member may also be a senior official at a government department or other safety net organisation or an officer of a member bank, how are potential conflicts handled between the interests of the deposit insurance system and those of the individual's "home" organisation?
22. To what extent do deposit insurers have codes of conduct and ethical behaviour for employees, senior officers, and governing body members?
23. To what extent should orientation and on-going training programmes exist for new governing body members? What types of issues should these programmes deal with?
24. What types of mechanisms exist to provide for the governing body's self-assessment of its performance?
25. In what ways are governing body members remunerated? Is remuneration sufficient to recruit quality governing body members?
26. What types of mechanisms, if any, exist to protect governing body members, officers and employees of a deposit insurance system against legal action over decisions or actions taken or omissions made in good faith and while discharging the deposit insurance system's mandate?
27. What means exist to balance officers', governing body members' and employees' legal protection against potential abuses of power on the part of those individuals (e.g. codes of conduct, ethical standards)?

### **Transparency and Disclosure Regimes and Internal Control Processes**

28. What types of disclosure regimes exist for a deposit insurance system (e.g. government freedom of information statutes)?

29. To what extent does a deposit insurance system disclose pertinent financial and non-financial details about its operations (e.g. financial statements, staffing details, executive compensation and bonuses, fund investment policies and performance levels) and provide management discussion and analysis?
30. What tradeoffs are there between the public's and industry's desire for transparency and the deposit insurance system's and member banks' needs for confidentiality?
31. What types of approaches exist for conducting external audits of a deposit insurance system?
32. Does a deposit insurance system make use of internal audit functions? Where they exist, what types of procedures and reporting structures do internal audit functions follow?
33. What types of frameworks exist to ensure an appropriate and effective internal control environment?

### **Research Methodology**

The research methodology will include a review of relevant literature and case studies that document the governance frameworks and experiences of IADI members.

#### **1. Analysis of issues**

The relevant literature will be reviewed by a Subcommittee of members established by the IADI Research and Guidance Committee. In addition, Subcommittee members will be requested to provide a description of the governance frameworks of their respective deposit insurance systems and to respond to the questions laid out in the **Issues to be Addressed** section above.

#### **2. Subcommittee survey**

In addition to the specific reports requested from Subcommittee members, other deposit insurance systems and interested parties will be asked to comment on their experience as it relates to the **Issues to be Addressed**, listed above. The request for comments will be posted on the IADI website ([www.iadi.org](http://www.iadi.org)).

#### **3. Preparation of the Subcommittee's Discussion Paper**

An initial draft Discussion Paper will be prepared by the Subcommittee and then presented to the Advisory Group of the Research and Guidance Committee (RGC) then subsequently to the RGC. The basis for the draft discussion paper will be the submissions of the individual members of IADI, comments received from survey

respondents, and the literature review. Once the Research and Guidance Committee has reviewed and commented on the draft paper, a revised version will be provided to IADI membership for review and comments at the Annual General Meeting in November 2006.

## Research Schedule

| Timelines in 2006                                       | Deliverables  |
|---|---|
| <b>23 March</b><br><b>(RGC Meeting in Basel)</b>        | <ul style="list-style-type: none"> <li>● Completion of detailed research outline and work plan/business plan</li> <li>● Work assignments to Subcommittee members</li> <li>● Approval of Advisory Group/RGC for plans</li> </ul> |
| 17 April  | ● Posting of research plan on IADI web site for public consultation   |
| <b>15 May</b><br><b>(RGC/EXCO Meeting in Basel)</b>     | ● Progress report by the Subcommittee Chair to RGC  |
| 31 May  | ● Subcommittee members' assignments due   |
| 31 July   | ● First draft of guidance paper completed and sent to RGC/Advisory Group members for comments   |
| 20 August   | ● Deadline for comments by RGC members  |
| 1 September   | ● Second draft completed and sent to Exco for comments  |
| <b>12-13 September</b><br><b>(RGC/EXCO Meeting)</b>     | ● Deadline for Exco comments during the Exco meeting  |
| 4 <sup>th</sup> week of September                       | ● First draft guidance paper for public consultation completed and sent to RGC members  |
| <b>4 October</b><br><b>(RGC Meeting in Chicago)</b>     | ● Discussion of the first draft for public consultation   |
| Mid-October   | ● Second draft guidance paper for public consultation completed and sent to 2006 Conference Task Force  |
| <b>16-17 November (IADI AGM Meeting and conference)</b> | ● Presentation of the second draft for public consultation in the Rio Conference  |

## Appendix I

### Guidance Provided in the FSF Working Group on Deposit Insurance Final Report of September 1, 2001

#### Definition:

**corporate governance** - The processes, structures, and information used for directing and overseeing the management of an organisation.

#### Guidance:

#### 9. Governance

- (a) The form of governance utilised in a deposit insurance system should reflect the mandate and the degree to which the deposit insurer is legally separated from the other financial safety-net participants. The governing body of the deposit insurance system should include individuals with requisite knowledge to understand the organisation's activities and the environment in which it operates, and they should have the authority to make decisions. The deposit insurer should have access to the input and views of the other safety-net participants and relevant interested parties. Members of the governing body and management of the deposit insurer should be subject to a fit-and-proper test, and they should be free from conflicts of interest. (page 17)
- (b) Governance systems and practices should be developed on the basis of sound strategic planning, risk-management processes, and good internal-control and audit systems. The governance structure should be transparent and subject to clear oversight and accountability. Rules specifying corporate governance practices should be developed. (page 17)

## **Appendix II**

### **Guidance Provided at the APEC Policy Dialogue on Deposit Insurance, February 16-18, 2004, and subsequently adopted as Official IADI Guidance, June 2005**

#### **Governance and interrelationship management among financial safety net participants**

- The sound governance of organizations comprising the safety net strengthens the financial system's architecture and contributes directly to system stability. The four major elements comprising sound governance of organizations are: independence, accountability, transparency and integrity. All are equally important and reinforce each other in supporting good governance practices.
- The view that operationally independent and accountable safety net organizations, with clear mandates and which are insulated from undue political and industry influence, provide greater integrity, credibility and legitimacy than entities lacking such independence is embodied in the standards that are assessed in the World Bank-IMF Financial Sector Assessment Program (FSAP).
- Experience also shows that a separate, operationally independent and accountable deposit insurance entity working within the financial safety net is the "best practice" model available to provide: (1) the most effective incentives for the control of moral hazard affecting a deposit insurer; (2) the greatest protection of the interests of depositors; (3) more balanced and effective decision-making; and (4) promotes more extensive monitoring of potential conflicts than entities lacking such independence.