



Governance of Deposit Insurance Systems

Introduction

As part of its Mission, IADI undertakes research on relevant deposit insurance issues and provides guidance to improve the functioning of deposit insurance systems. This Research Letter highlights suggested Guidance in the form of IADI Core Principles and Effective Practices to enhance the sound governance of deposit insurance systems. The guidance points are articulated in the discussion paper on “Governance of Deposit Insurance Systems” which was released on the IADI web site (www.iadi.org) for public consultation on 22 November 2007.¹

Governance generally refers to the processes, structures and information used for directing and overseeing the management of an organisation. Importantly, governance also pertains to the relationship between the depositor protection system and the authority from which it receives its mandate or other authority to which it is ultimately held accountable. Thus, a sound governance framework is a critical component of an effective deposit insurance system. The key elements or principles underlying a sound governance framework are: operational independence; accountability; integrity; and transparency and disclosure. All are equally important and reinforce each other in supporting sound governance.²

Experiences also shows that a separate, operationally independent and accountable deposit insurance entity working within the financial safety net is a “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.³

What are the main topics and suggested guidance in the discussion paper?

Just as the mandates, roles and responsibilities of deposit insurers can vary across countries, so too can governance structures. Whatever the governance structure chosen, all share certain common characteristics. All deposit insurance systems include some form of higher authority from which they receive their mandates or to which they are ultimately held accountable; a governing body (e.g. board of directors or supervisory board, or even a department head); and the deposit insurer’s management. The discussion paper

¹ IADI Guidance is information, advice, counsel or instructions which are widely accepted as being sound and prudent. Forms of guidance include fundamental or “core” principles as well as more specific guidance in the form of good or effective practices.

² These four key elements have already been mentioned in the APEC Policy Dialogue on Deposit Insurance (2004) which was adopted as official guidance by IADI:

<http://www.iadi.org/Guidance%20Papers/IADI%20-%20APEC%20Guidance%20June%202005.pdf>

³ Recited from the APEC Policy Dialogue on Deposit Insurance. [Financial Stability Forum’s Guidance on Deposit Insurance](#) also notes that 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.

considers deposit insurance governance structures; relationships; the governing body and management; audit and legal protection; and transparency and disclosure.

The guidance points summarise the main conclusions of the paper and set out proposed IADI Core Principles and Effective Practices, which support sound governance frameworks particularly with respect to promoting accountability, integrity, operational independence, transparency, and disclosure.⁴ The suggested Core Principles and Effective practices are reflective of, and adaptable to, a broad range of settings, circumstances and structures:

Governance structures

- The mandate and responsibilities of a deposit insurance system should be clearly defined and preferably set out in legislation. (**Core Principle**)
- The deposit insurance system should have a governing body and the governing body should be held accountable to the authority from which the deposit insurance system receives its mandate. (**Core Principle**)
- It is an **effective practice** for the deposit insurer to have operational independence in using the powers and means accorded to it to fulfil its mandate.

Governance relationships

- The governing body of a deposit insurance system should be structured to prevent undue influence from political forces, the financial services industry, or other safety-net participants. (**Core Principle**)
- The deposit insurance system should be structured such that the potential for conflicts of interest respecting members of the governing body and management is minimised. (**Core Principle**)

Governing body and management

- It is an **effective practice** for governing body members, senior officers, and employees of a deposit insurance system to be subject to laws and/or codes respecting conflicts of interest and ethical behaviour.
- It is an **effective practice** for a deposit insurance system to maintain a profile of desired skills for its senior executive and governing body members and for those individuals to be appointed based on competence and skill.

⁴ **Operational Independence** is defined as the ability of an organization to use the powers and means assigned to it without undue influence from external parties. An organization that is operationally independent does not have the authority, however, to control its objects and mandate, as these are set by a higher authority. **Accountability** means that individuals and organizations should be responsible for their actions and for fulfilling their objectives. **Integrity** describes two concepts. The first is the principle that individuals should pursue the objectives of their organization without compromising them due to their own or others' behaviour or self-interest. Second, integrity also refers to the wholeness and soundness of an organization. The integrity of a deposit insurance system can be affected in many ways, such as through the appointment of governing body members and head of management and through the terms of office and criteria for removal of those individuals. **Transparency** is the principle fostered when the actions and decisions of an organization, such as a deposit insurer, are revealed and clarified to the organization's stakeholders. **Disclosure** refers to the release to stakeholders of information necessary for them to judge the effectiveness of the deposit insurer's conduct.



Performance assessment

- It is an **effective practice** for the governing body to conduct meaningful self-assessments.

Roles of the governing body and management

- It is an **effective practice** for the governing body to set the strategic direction of the deposit insurance system and for management to take action to carry out that strategic direction.
- It is an **effective practice** for the governing body to have a charter or policy in place that lays out the governing body's responsibilities.

Audit and legal protection

- It is an **effective practice** for governing body members, senior officers and employees of a deposit insurance system to be provided with legal protection for decisions made, omissions, and actions taken in good faith and while discharging the mandate of the deposit insurance system.
- It is an **effective practice** for a deposit insurance system to be subject to regular external audits and examinations and for those audits and examinations to be made public.
- It is an **effective practice** for a deposit insurer to subject its daily operations to internal audits and for the internal audit function to report to the governing body.

Transparency and disclosure

- A deposit insurer should be as transparent as possible and disclose appropriate information on its activities, governance practices, structure, and financial results. (**Core Principle**)

Where to get further information on the Governance Paper?

The latest version of the discussion paper can be accessed in the following linked IADI website: [Discussion Paper – Governance of Deposit Insurance Systems](#).

Comments on the paper are welcome and should kindly be sent by 24 December 2007 to David Walker at dwalker@cdic.ca.

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