

CENTRAL BANK OF NIGERIA'S REVIEW OF THE DRAFT REVISED IADI CORE PRINCIPLES ISSUED BY THE INTERNATIONAL ASSOCIATION OF DEPOSIT INSURERS (IADI)

1.0 INTRODUCTION

The IADI Core Principles serve as the international standard for effective deposit insurance systems, designed to protect depositors and contribute to financial stability. The 2024 revision addresses evolving challenges such as digital innovation, increased resolution roles for deposit insurers, and lessons from the 2023 banking turmoil. This report assesses the draft principles to identify gaps and proposes recommendations to strengthen their applicability across diverse jurisdictions.

2.0 GAP ANALYSIS

The following gaps were identified in the IADI Core Principles:

a. Limited Guidance on Fintech and Digitalisation Risks

- **Issue:** Principle 9 (Funding) and Principle 15 (Reimbursement) address fintech and digitalisation in terms of opportunities (e.g., digital payment methods for reimbursement) but lack comprehensive guidance on managing associated risks, such as cybersecurity threats, third-party dependencies, and rapid depositor runs amplified by digital channels (Page 21-22).
- **Impact:** Without specific risk management criteria, deposit insurers may be unprepared for systemic risks arising from fintech disruptions, potentially undermining financial stability.
- **Evidence:** The document notes digitalisation's potential to amplify liquidity and operational risks but does not mandate specific risk assessment or mitigation strategies (Page 22).

b. Insufficient Emphasis on Climate-Related Financial Risks

- **Issue:** Principle 10 (Public Awareness) and the section on ESG factors (Page 22-23) acknowledge climate change risks but treat them as optional considerations rather than mandatory components of risk management and fund investment policies.
- **Impact:** Climate-related financial risks could significantly affect insured deposit-taking institutions' default risks and resolution costs, yet the principles lack enforceable criteria for integrating these risks into deposit insurance frameworks.
- **Evidence:** The document highlights climate risks but notes that their consideration is not widespread among deposit insurers and faces legal and practical hurdles (Page 23).

c. Inadequate Cross-Border Coordination Mechanisms

- **Issue:** Principle 18 (Cross-Border Cooperation) establishes requirements for cooperation with foreign jurisdictions but lacks specificity on operational protocols, such as standardized data formats or crisis simulation exercises involving multiple jurisdictions (Page 46).
- **Impact:** Weak cross-border coordination could delay resolution and reimbursement processes for foreign depositors, particularly in jurisdictions with significant foreign bank presence, risking financial instability.
- **Evidence:** The principle outlines general requirements for information sharing but does not address practical implementation challenges (Page 46).

d. Ambiguity in Accountability for Parties at Fault

- **Issue:** Principle 12 (Dealing with Parties at Fault) requires investigation and sanctions for those responsible for institutional failures but does not specify the deposit insurer's role or coordination mechanisms with other authorities (Page 39).
- **Impact:** Ambiguity may lead to inconsistent accountability enforcement, reducing deterrence against reckless behavior and increasing moral hazard.
- **Evidence:** The principle allows for investigations by various authorities but lacks clarity on the deposit insurer's involvement (Page 39).

3.0 RECOMMENDATIONS

To address the identified gaps, the following recommendations are proposed:

a. Integrate Fintech and Digitalisation Risk Management

- **Action:** Amend Principle 15 (Reimbursement) to include essential criteria requiring deposit insurers to conduct regular cybersecurity risk assessments and simulate different scenario tests for digital reimbursement systems. Add a new criterion under Principle 9 (Funding) mandating policies to mitigate third-party technology provider risks.
- **Rationale:** This ensures deposit insurers are equipped to handle fintech-related systemic risks, enhancing operational resilience and depositor confidence.
- **Implementation:** Require deposit insurers to develop fintech risk management frameworks with periodic reviews.

b. Mandate Climate-Related Financial Risk Assessments

- **Action:** Revise Principle 9 (Funding) to include an essential criterion requiring deposit insurers to integrate climate-related financial risks into fund management and risk assessment processes. A guidance on permitted ESG investments aligned with capital preservation goals.
- **Rationale:** Mandatory climate risk integration strengthens deposit insurers' ability to manage emerging risks, aligning with global financial stability objectives.
- **Implementation:** Collaborate with the Financial Stability Board (FSB) to develop standardized climate risk assessment tools for deposit insurers.

c. Strengthen Cross-Border Coordination Frameworks

- **Action:** Enhance Principle 18 (Cross-Border Cooperation) by adding essential criteria for standardized data-sharing protocols and mandatory cross-border crisis simulation exercises.
- **Rationale:** Robust cross-border mechanisms improve resolution efficiency and depositor protection in jurisdictions with foreign bank presence, reducing systemic risks.
- **Implementation:** Establish a working group under IADI to develop cross-border coordination guidelines.

d. Clarify Accountability Mechanisms for Parties at Fault

- **Action:** Amend Principle 12 (Dealing with Parties at Fault) to specify the deposit insurer's role in coordinating with supervisory and criminal authorities to investigate failures. Include criteria for transparent reporting on accountability actions.
- **Rationale:** Clear roles and transparency enhance deterrence and reduce moral hazard, supporting public policy objectives.
- **Implementation:** Require deposit insurers to publish annual reports on accountability actions.

4.0 CONCLUSION

The IADI Core Principles provide a robust framework for effective deposit insurance systems but require enhancements to address emerging challenges. By integrating fintech risk management, mandating climate risk assessments, strengthening cross-border coordination, and clarifying accountability mechanisms, the principles can better support financial stability and depositor protection. These recommendations ensure the Core Principles remain forward-looking and adaptable to diverse jurisdictional needs, reinforcing their role as a global standard.