

I Overview

Deposit insurance systems have developed and expanded rapidly in recent years. A large number of countries have modified their systems, either adopting explicit deposit insurance systems or introducing significant modifications to existing systems. In addition, the international community has participated in the debate on the appropriate design of safety nets in general and deposit insurance in particular. In 2001, a working group of the Financial Stability Forum (FSF) published a report on the broad range of options for establishing a deposit insurance system. In 2003, the International Association of Deposit Insurers (IADI) was established to promote international cooperation and to encourage widespread international contact among deposit insurers.

In light of these recent developments, this paper has two broad objectives. First, recently established insurance systems are described, identifying emerging trends. A number of studies have surveyed deposit insurance practices. Two previous IMF publications (Garcia, 1996, 2000) remain valuable references as do the surveys conducted by the IADI in 2002 and 2003 on 47 countries.¹ This paper updates those surveys.² It is based on public information obtained from central banks, ministries of finance, and deposit insurance agencies and on the 2003 update of the World Bank's database on banking regulation.

The second objective of this paper is to identify sound practices in deposit insurance based on recent experience. The starting point is the FSF report (FSF, 2001) containing over 40 recommendations, ranging from broad policy considerations to detailed directions on the management and operation of a deposit insurance system. The paper builds on that guidance, identifies good practices in the design of deposit insurance systems, and provides evidence for resolving the trade-offs identified by the FSF.

This paper also seeks to place these policy recommendations within the growing body of economic literature on deposit insurance systems. Recent years have

seen a number of attempts to develop econometric tests of the influence exercised by explicit deposit insurance, as well as the impact of different design features of deposit insurance systems. This work requires careful consideration, not least because some of it has been used to draw policy conclusions about the merits of adopting explicit deposit insurance. A number of these studies conclude that the existence of explicit systems increases the risk of banking crises, and also points to design features—such as the desirability of ex post funding—that run counter to the views of many deposit insurance practitioners.

The sound practices described in this paper are not meant to become “best practices” or “core principles” such as those developed by international standard setters.³ Rather, they are meant to outline international experience in resolving the most important issues related to deposit insurance alternatives, illustrating that some design features can be seen as comparatively more efficient than others. Authorities may well opt for practices different from those described here, reflecting concerns about local conditions or specialized objectives. The description of the procedures contained here is not meant to change such decisions. Rather, the paper seeks to ensure that relevant factors are taken into consideration as such decisions are made.

The structure of this paper is as follows. Section II includes a discussion of explicit and implicit deposit insurance, including recent academic literature and policy recommendations. Section III reviews the conditions to be weighed when considering the introduction of a deposit insurance system, including policy objectives and necessary preconditions. Section IV provides specific design features of deposit insurance systems, including mandates, powers, accountability, transparency, funding, membership, cover, and public awareness. Section V discusses design features aimed at minimizing the impact of moral hazard.

¹The completed questionnaires as well as a brief summary of findings are available at www.iadi.org.

²Approximately 200 countries have been included and updated in the survey.

³For example, the Basel Committee developed the Basel Core Principles for Effective Banking Supervision, and both the Organization of Economic Cooperation and Development and the International Association of Insurance Supervisors have developed core principles for the supervision and regulation of securities markets and insurance companies, respectively.