
COMMUNIQUE

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Deposit Guarantee Fund Size Guidance

The Credit Union Prudential Supervisors Association (CUPSA) established a working group composed of several of its members to develop guidance for determining an appropriate size for deposit guarantee funds.

The working group, with the support of CUPSA, has now released “Guiding Principles for Developing an Appropriate Deposit Guarantee Fund,” which sets out the elements considered desirable in developing a suitable deposit guarantee fund.

These guiding principles are intended for use by Canadian credit union and caisse populaire deposit insurers and are consistent with guidance provided by the [Basel Committee on Banking Supervision](#) (BCBS) and the [International Association of Deposit Insurers](#) (IADI). CUPSA members are encouraged to consider these guiding principles when establishing target fund sizes.

CUPSA will continue to monitor national and international research and guidance related to deposit insurance in order to continuously enhance the effectiveness of Canadian credit union and caisse populaire deposit insurance systems.

About CUPSA

The Credit Union Prudential Supervisors Association (CUPSA) is an interprovincial association composed of credit union deposit insurers and prudential supervisors across Canada. CUPSA works toward maintaining a sound and sustainable credit union sector through joint actions. For more information, visit CUPSA’s website at www.cupsa-aspc.ca.

Guiding Principles

Developing an Appropriate Deposit Guarantee Fund

These guiding principles have been developed by the Canadian Credit Union Prudential Supervisors Association (CUPSA) and incorporate the elements considered desirable in developing an appropriate deposit guarantee fund. They are intended for use by an organization charged with the responsibility of providing a deposit guarantee to depositors of credit unions and caisses populaires. Deficiencies in adherence to these principles will likely result in a higher fund requirement.

These principles are consistent with the guidance established by the [Basel Committee on Banking Supervision](#) (BCBS) and the [International Association of Deposit Insurers](#) (IADI).

Guiding Principle 1 – Legal and Operational Structure

The public policy objectives of the deposit guarantee program should be formally specified through the legislative framework in place and well integrated into its design. The mandate and powers of the organization should be clearly and formally specified and consistent with the stated public policy objectives and the powers and responsibilities assigned to the organization. The organization should be operationally independent, transparent, accountable and insulated from undue political and industry influence. A legal framework should be in place to provide legal protection for the organization and its employees. The organization should be required to follow codes of conduct to ensure accountability.

Guiding Principle 2 - Deposit Guarantee Program

1. Design

The deposit guarantee program as well as the other elements of the financial system safety net should be designed to mitigate moral hazard risks. Coverage limits on deposits should be clearly defined in law, regulations or by-laws and adequate to cover the large majority of depositors consistent with public policy. Where coverage is unlimited, additional safeguards should be considered to mitigate the potential moral hazard risks.

2. Funding

The program should provide an ex-ante fund with access to all funds, including back-up funding for liquidity purposes and other funding mechanisms in order to ensure the prompt reimbursement of depositors' claims. Where practical, risk based differential premium systems should be used for assessing insurance premiums and include transparent criteria to calculate premiums.

3. Prudential Oversight

An appropriate prudential oversight regime should be in place with the following elements included:

- Clearly defined permissible activities with specified limits;
- Criteria to accept or reject applications for the establishment of a credit union or caisse populaire;
- Supervisory powers to review major business transactions such as acquisitions or new lines of business;
- Supervisory reporting, data collection and risk assessment;
- On-site examination programs;
- Supervisory powers to require corrective action including failure resolution; and
- Powers to allow the supervisor to act expeditiously to minimize losses to the deposit guarantee fund.

Guiding Principle 3 - Credit Union/Caisse Populaire System Characteristics

At a minimum, a comprehensive approach to determining an appropriate deposit guarantee fund should include consideration of the following factors:

1. External Environment

The external environment in which the deposit insurance program operates includes factors such as:

- The general economic conditions and outlook in which the institutions operate including the sensitivity to business cycles, specific industries, etc.;
- The impact of any self-regulating or self-help organizations operating within the sector including stabilization funds and centrals or federations; and
- The number and size of institutions within the sector.

2. Individual Institutional Risk Profiles

The risk profile of each individual institution insured by the program can have a significant impact on the size of the fund. The following elements of the risk profile should be considered:

- Strength of governance of the institution including its risk appetite and risk management capability;
- Capital adequacy and excess capital;
- Asset quality including credit risks, concentration and large exposures;
- Appropriate levels of liquidity and access to contingency liquidity resources;
- Operational risk and internal controls;
- Exposure to other risks including non-financial and reputational risks; and

- Geographic concentration risk.

3. Size of Institution

The size of the institution including:

- Total assets, deposits and insured deposits;
- Scope and complexity of operations and product offerings; and
- Other operating entities including subsidiaries.

4. Probability & Cost of Failure

Each individual institution should be assessed for the following:

- Probability of failure;
- Probability of change from one risk level to another; and
- Likely impact of failure.

Guiding Principle 4 - Deposit Fund Characteristics

The deposit fund characteristics should be considered when developing an appropriate fund size. These characteristics include:

- Projected revenues and expenses to run the deposit guarantee program including the costs of regulatory oversight, if appropriate;
- Growth in insured deposits;
- Yield on investments in the fund;
- Actual loss experience and recoveries over time;
- Projected losses to the fund resulting from failures; and
- Desired level of confidence that the fund will be adequate to meet future scenarios.

These factors taken together form the basic framework for determining an appropriate fund size. However, there may be additional considerations that should be included in special or unusual circumstances.