



TECHNICAL

NOTES & MANUALS

Sibling Rivalry in the Financial Safety Net: Governance Arrangements for Bank Resolution and Deposit Insurance

Atilla Arda and Jan Nolte

TNM 2025/05

This page intentionally left blank

TECHNICAL NOTES AND MANUALS

Sibling Rivalry in the Financial Safety Net: Governance Arrangements for Bank Resolution and Deposit Insurance

Atilla Arda and Jan Nolte

Authorized for distribution by Tobias Adrian

This technical note addresses the following questions:

- What are the pros and cons of vesting bank resolution and deposit insurance functions in one or more authorities and in existing or newly established, stand-alone authorities?
- What potential policy conflicts may arise between bank resolution and deposit insurance functions, with other financial safety net authorities, and with the financial industry?
- How to manage overlapping objectives, shared responsibilities, and potential conflicts of interest between bank resolution and deposit insurance functions, whether housed in separate or a single authority?
- What are good practices for effective governance arrangements that can mitigate potential policy conflicts?
- What statutory and operational arrangements should be adopted to ensure effective legal protection for individuals responsible for implementing these two functions?
- How can governance arrangements ensure the effective use of—single or multiple—funds for deposit insurance and resolution?

© 2025 International Monetary Fund
Cover Design: IMF Creative Solutions
Cataloging-in-Publication Data
IMF Library

Names: Arda, Atilla, author. | Nolte, Jan, author. | International Monetary Fund, publisher.

Title: Sibling rivalry in the financial safety net: governance arrangements for bank resolution and deposit insurance / Atilla Arda and Jan Nolte

Other titles: Governance arrangements for bank resolution and deposit insurance. | Technical notes and manuals. | International Monetary Fund. Monetary and Capital Markets Department (Series).

Description: Washington, DC : International Monetary Fund, 2025. | Feb. 2025. | Includes bibliographical references.

Identifiers: ISBN:

9798400293795 (paper)

9798400294686 (ePub)

9798400293856 (web PDF)

Subjects: LCSH: Deposit insurance. | Banks and banking. | Bank failures | Global Financial Crisis 2008-2009

Classification: LCC HG1662.A7 2025

DISCLAIMER:

This Technical Note should not be reported as representing the views of the IMF. The views expressed in this paper are those of the authors and do not necessarily represent the views of the IMF, its Executive Board, or IMF management.

Recommended citation:

Arda, Atilla, and Jan Nolte. 2025. "Sibling Rivalry in the Financial Safety Net: Governance Arrangements for Bank Resolution and Deposit Insurance." IMF Technical Notes and Manuals 2025/05. International Monetary Fund, Washington, DC.

Please send orders to:

International Monetary Fund, Publication Services

PO Box 92780, Washington, DC 20090, USA

Tel: (202) 623-7430 | Fax: (202) 623-7201

publications@IMF.org

eLibrary.IMF.org

bookstore.IMF.org

Contents

Abbreviations	1
I. Executive Summary	2
II. Introduction	4
III. Location, Location, Location	5
IV. A Tale of Two Mandates and Their Powers	7
A. Complementary and Interdependent Mandates	7
B. Preparedness and Other Routine Activities	7
C. Early Intervention	8
D. Resolution and Crisis Management	9
V. Agree to Disagree	10
A. Potential Conflicts between Bank Resolution and Deposit Insurance Functions	10
B. Potential Conflicts with Other Financial Safety Net Authorities	10
C. Potential Conflicts with the Industry	11
VI. Governance	13
A. Autonomy and Noninterference	13
B. Composition of the Board	15
C. Interagency/Functional Cooperation	17
D. Scaling Up	18
E. Transparency and Accountability	18
VII. Legal Protection	20
VIII. Two Funds in One?	21
Appendix 1. International Standards on Bank Resolution and Deposit Insurance	24
Appendix 2. International Standards on Governance	25
References	27

EDITOR'S NOTE (2/20/25)

After the original publication of this note, in the second paragraph on page 5, "Finland and Sweden" was corrected to "Sweden."

This page intentionally left blank

Abbreviations

BCP	Basel Core Principles for Effective Banking Supervision
CP	Core Principles for Effective Deposit Insurance Systems; Core Principle(s)
DIA	deposit insurance agency
DIF	deposit insurance fund
DIS	deposit insurance system
ELA	emergency liquidity assistance
FDIC	Federal Deposit Insurance Corporation
FSB	Financial Stability Board
IADI	International Association of Deposit Insurers
KA	Key Attributes of Effective Resolution Regimes for Financial Institutions; Key Attribute(s)
MOF	ministry of finance
RA	resolution authority

I. Executive Summary

Bank resolution and deposit insurance functions are intertwined and present similar challenges and considerations for their governance structures. The Financial Stability Board Key Attributes of Effective Resolution Regimes for Financial Institutions and the International Association of Deposit Insurers Core Principles for Effective Deposit Insurance Systems recognize these functions' interdependency, including that they both aim to protect depositors and contribute to financial stability. The two functions share similar potential conflicts of interest with other components of a country's financial safety net and with the banking industry.

Although countries have a choice on where to house these two mandates, for smaller jurisdictions there are good arguments for assigning these functions to existing agencies. About two-thirds of jurisdictions have housed the bank resolution function in an agency with multiple mandates. Typically, the resolution function is combined with the bank supervision function or with the central bank—especially when the latter is also responsible for bank supervision. Several jurisdictions have combined resolution and deposit insurance functions. A stand-alone resolution authority is quite uncommon. In contrast, most countries have established stand-alone deposit insurance agencies, albeit mostly under a paybox or paybox plus mandate. In countries with low capacity, housing the deposit insurance function within an existing agency may most efficiently use existing capabilities and scarce expertise, provided that the deposit insurance function can be exercised with autonomy and that potential policy conflicts between mandates are mitigated.

Institutional arrangements must identify and properly manage material conflicts of interest. Irrespective of whether financial safety net functions are assigned to one or more agencies, in certain resolution scenarios these functions may potentially conflict, for example, the bank resolution authority selling (parts of) the failed bank during resolution, the bank supervisor being concerned about the health of the purchasing bank, the central bank being a large creditor because of liquidity assistance, and the government aiming to mitigate taxpayer risks. The extent of potential policy conflicts partly depends on the mandate of the deposit insurance system and has a lower intensity for a narrow paybox plan. Moreover, severe conflicts of interest may arise with the banking industry, for example, if representatives of the latter reside in the governance structures of the resolution and deposit insurance functions.

The governance structures for bank resolution and deposit insurance functions should reflect the need for autonomy, functional separation, agility, and technical expertise. Where these functions are combined with other mandates, functional separation should be supported with dedicated teams, separate reporting lines, and transparent decision making. This is critical to ensure prompt action in time-sensitive, high-stress, information-limited resolution cases. The composition of a multimandated agency's governing body should reflect its broad mandate and ensure that the specialized expertise and experience that these functions require are sufficiently represented in the governing body. Irrespective of where these functions are housed, the composition of the governing bodies tasked with these functions should reinforce their autonomy and mitigate potential conflicts of interest with the industry, politics, and other financial safety net members. Furthermore, operational modalities should enable flexibly expanding the bank resolution and deposit insurance functions' resources as a bank approaches failure.

Particularly in jurisdictions that are newly establishing a deposit insurance system, authorities should consider integrating the deposit insurance function within their resolution authority. With special bank resolution frameworks becoming more prevalent, depositor payouts can be expected to become less the norm. A resolution action that transfers insured deposits will likely deliver better outcomes than liquidation and deposit payout by instilling confidence, because depositors do not lose access to their deposits, and by minimizing costs to a deposit insurance fund, because asset values are better preserved.

The banking turmoil in early 2023 demonstrated that the speed of restoring depositor access to their funds is becoming more important in an era of 24/7 internet banking, social media, and shifting depositor expectations. An integrated mandate for resolution and deposit insurance may most efficiently use scarce expertise (particularly) in countries with low capacity, with one authority responsible for dealing with problem banks in the interest of financial stability and depositor protection. This authority would be a strong partner for other members of the safety net, thereby strengthening the overall financial stability framework. Whichever approach is taken, establishing sound governance arrangements to manage complementary or even overlapping mandates and potential conflicts of interest is critical, and this is the focus of this note.

II. Introduction

The 2008–09 global financial crisis revealed that many countries’ financial safety nets needed to be significantly strengthened.¹ To address key gaps in financial safety nets,² the Financial Stability Board (FSB) developed the Key Attributes of Effective Resolution Regimes for Financial Institutions (Key Attributes; KA; FSB 2014), and the International Association of Deposit Insurers (IADI) issued the Core Principles for Effective Deposit Insurance Systems (Core Principles; CP; IADI 2014).³

Bank resolution and deposit insurance functions complement each other and require sound governance structures. The international standards acknowledge the interdependencies of the two functions: they both aim to protect depositors and contribute to financial stability. These functions share (real or potential) conflicts of interest with other components of a country’s financial safety net and with the banking industry. Moreover, resolution actions—be they restructuring or liquidation—are typically more intrusive than regular supervision, with shareholders and creditors at risk of having their property rights overridden. Accordingly, both the resolution authority (RA) and the deposit insurance system (DIS) must be supported by robust governance structures and legal safeguards to mitigate potential conflicts (see Appendix 2). Adding these functions to existing institutions (such as a central bank or a banking supervisor) or establishing separate agencies in the form of a deposit insurance agency (DIA) will affect potential conflicts, which is a focus of this note.

There are several options for the institutional setup of bank resolution and deposit insurance functions, and each option may create different governance challenges. Typically, a country’s choice is guided by the existing institutional arrangements, the financial sector structure, and cost/capacity considerations (see “Location, Location, Location”). The different mandates and roles of RAs and DISs (see “A Tale of Two Mandates and Their Powers”) may trigger policy conflicts (see “Agree to Disagree”), which need to be addressed through an appropriate governance structure (see “Governance”). Furthermore, a sufficient level of legal protection is critical for agency autonomy (see “Legal Protection”), and resolution funding adds to the complexities. Combining these mandates efficiently would use existing capabilities and expertise, provided that each function can be autonomously exercised and potential interfunctional conflicts are mitigated (see “Two Funds in One?”).

¹ The financial safety net comprises early intervention (including recovery), resolution, deposit insurance, and idiosyncratic liquidity assistance.

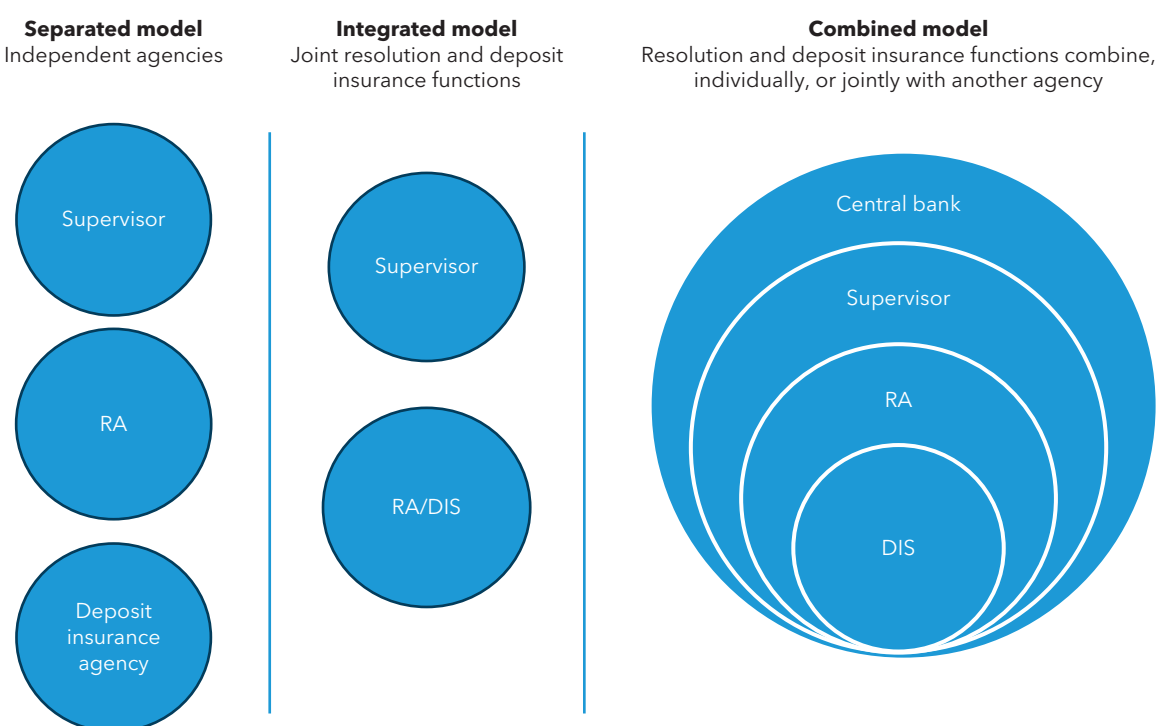
² IMF (2014) summarizes the key gaps as inadequate (1) resolution powers and tools, (2) cross-border cooperation frameworks, and (3) mechanisms for loss allocation.

³ See Appendix 1 for a brief description.

III. Location, Location, Location

When setting up an RA or a DIS, policymakers will have to decide where to allocate the functions. Jurisdictions can decide to add the bank resolution and deposit insurance functions to an existing institution (central bank or supervisor if separate) or establish a new stand-alone agency for one or both functions (Figure 1).

Figure 1. Institutional Setup of the Safety Net



Source: IMF staff.

Note: DIS = deposit insurance system; RA = resolution authority.

A large majority of jurisdictions have placed the resolution mandate in either the supervisory agency or the central bank.⁴ A stand-alone RA is quite uncommon among the 63 member jurisdictions of the Bank for International Settlements, with notable exceptions, including the Single Resolution Board of the European Banking Union. About two-thirds of the jurisdictions have housed the resolution function in an agency with multiple mandates. Typically, the resolution function is combined with the bank supervision function or the central bank—especially where the latter is also responsible for bank supervision. Several jurisdictions have combined resolution and deposit insurance functions. Only in a few cases, the RA is vested in another agency, such as the debt office in Sweden, reflecting these institutions' roles in managing past financial crises and the public funds that were deployed.

⁴ Bank for International Settlements (2021) gives a descriptive overview of the setup of the resolution function and other institutional arrangements.

In contrast, most countries have established stand-alone DIAs.⁵ In less than 20 percent of the 92 jurisdictions included in the IADI annual surveys, the deposit insurance function is housed within the central bank or another financial authority, such as the RA (for example, Australia, Mexico, the Netherlands) and—in rare cases—in the Ministry of Finance (MOF) (for example, Belgium). Most other countries have a stand-alone DIA, albeit limited in their mandate to either deposit payout (paybox mandate) or some responsibility in resolution funding (paybox plus).⁶ A stand-alone DIA may be appropriate in countries with a large banking sector, providing sufficient financial resources and operational needs to justify the organizational infrastructure, including personnel, IT infrastructure, and premises. Housing the deposit insurance function within the central bank or banking supervisory agency may be more appropriate in countries with limited capacity (IMF 2019).

⁵ This paper focuses on DISs administered by national DIAs, not regional arrangements.

⁶ Based on the 2022 International Association of Deposit Insurers survey, 74 public DISs for banks are identified as set up as a separate entity, of which 60 operate under a paybox/paybox plus mandate, 11 agencies have a joined RA/DIS mandate, and the remaining 3 agencies combine additional supervisory powers (source: IADI, Fund staff).

IV. A Tale of Two Mandates and Their Powers

A. Complementary and Interdependent Mandates

The international standards underline the complementarity and interdependency of prudential supervision, deposit insurance, and bank resolution. The effectiveness of a DIS relies, to a significant degree, on the strength of prudential supervision and regulation, giving assurances about banks' financial health, and of the resolution regime, giving assurances that failed banks can be resolved in an orderly fashion and at least cost to the DIS. In turn, well-developed deposit insurance and prudential supervision are preconditions for effective resolution regimes. For example, deposit insurance protects the most vulnerable depositors from losses in resolution (for example, insured deposits are excluded from a bail-in), and the DIS may be allowed to provide resolution funding subject to safeguards (for example, by funding the transfer of deposits to a healthy bank). Sound governance of the financial safety net agencies and effective legal protection for their current and former decision makers, staff, and agents are required in the international standards (see Appendix 1).⁷ The roles and responsibilities of the resolution and deposit insurance functions intersect in different ways depending on whether they are undertaking routine activities, or preparing to, or intervening in a failing bank or a wider crisis.

B. Preparedness and Other Routine Activities

Irrespective of their location, both bank resolution and deposit insurance functions should undertake extensive planning to enhance their preparedness to deal with failing banks.

Key Preparedness Activities of Both Functions

Crisis preparedness. Together with other financial safety net members, RAs and DISs—potentially overseen by a national crisis management committee—should undertake regular event-specific (for example, bank runs) and comprehensive crisis-simulation exercises. They should assign responsibilities to regularly update crisis management plans, protocols, and communication strategies individually and collectively and have escalation procedures for live contingency preparations in the lead-up to a bank failure.⁸

Managing funds. A DIS should include a DIF that is ex ante funded, with annual levies collected from member banks. Although a well-funded DIF that is authorized to contribute to resolution measures should be prioritized (IMF 2018), some countries have also established separate resolution funds. Where resolution funds exist, RAs (and sometimes the DIA for the RA⁹) manage these. Public backstops are critical for both funds in case the collected premiums prove insufficient. Backstops should be operationalized, for example, through memorandums of understanding with sufficient detail on procedures and timelines agreed with the MOF and complemented with loan documentation potentially with the central bank as the government's fiscal agent.

Cross-border cooperation. RAs and DISs will need to engage with their foreign counterparts to develop shared understandings and common approaches to orderly resolution of cross-border banks. In

⁷ Other "preconditions" under the standards are sound financial stability risk monitoring and policy formulation, a well-developed legal framework, a well-functioning judiciary, and robust accounting, auditing, and disclosures.

⁸ For examples of such escalation procedures, see IMF (2022b).

⁹ In Albania and France, the DIA is tasked with collecting fees for and managing the resolution fund on behalf of the RA.

currency unions, cross-border cooperation would typically be built into the resolution framework and the supporting institutional setup.¹⁰

Key Preparedness Activities of the Resolution Function

Resolution planning. Building on their resolution policies and legal powers, RAs develop bank-specific resolution plans based on their preferred resolution strategy supported by a funding plan and complemented by a secondary strategy. In the resolution planning stage, an RA will need to consult with the other financial safety net members to get their input and advice, including with respect to banks' recovery plans that are regularly evaluated under the oversight of the supervisor and with the central bank on the availability of liquidity in resolution.

Resolvability assessments. RAs undertake resolvability assessments that may reveal obstacles to resolution, which should be removed by, for example, requiring changes in a bank's business practices, structure, or organization, in order to reduce the complexity and cost of resolution and to ensure that critical functions can be segregated legally and operationally.

Key Preparedness Activities of the Deposit Insurance Function

Reimbursement strategies. A DIS should prepare strategies for banks in liquidation on how to reimburse depositors through various methods, such as channeling reimbursement through other banks or making direct payments to depositors. For prompt reimbursements, a DIS will need to regularly verify depositor records on site and test the availability of depositor data.

Public awareness. A DIS, together with banks, should inform depositors and the general public about the benefits and limitations of deposit insurance. Providing such information through media channels and member institutions will help maintain confidence in the banking system and the DIS and help mitigate the risk of deposit runs at times of stress.

C. Early Intervention

With early intervention measures, a banking supervisor aims to address failings in a weak bank. The Basel Core Principles for Effective Banking Supervision (BCP) require that a supervisor has a clear framework with a broad range of measures for early intervention to handle banks in the buildup to and during times of stress. Such measures include, for example, the ability to impose sanctions or require a bank to take timely corrective action, restricting the current activities of the bank, withholding approval for new activities or acquisitions, replacing or restricting the powers of a bank's management, or imposing more stringent prudential limits and requirements—all of which may form part of a formal (for example, prompt corrective action) framework to deal with problem banks. Recovery plans, annually prepared by banks and reviewed by the supervisor, support this process by giving a bank and its management a menu of recovery options with clear triggers.

RAs and DISs should get more involved when a bank's supervisory risk assessment worsens. The supervisor should inform both functions about any early intervention measures. Tying this requirement to the supervisory escalation process makes interagency coordination predictable and allows both functions to

¹⁰ The governance arrangements for the resolution and deposit insurance functions in these unions—for example, a supranational RA in addition to or in place of national RAs—are informed by broader political and historical considerations, which fall outside the scope of this paper.

undertake timely preparatory steps in anticipation of a bank failure. The RA will need to update a distressed bank's resolution plan or prepare a contingency plan for potentially imminent resolution action. The DIS will need to confirm insured depositor data and that it has sufficient cash on hand for a potential deposit reimbursement. A lack of early information exchange can significantly hamper the safety net's preparedness and effectiveness when a bank fails.¹¹

D. Resolution and Crisis Management

RAs and DISs are expected to play critical roles when dealing with failing banks. Once resolution triggers are met, the supervisor should hand over the nonviable bank to the RA,¹² and the bank resolution and deposit insurance functions should pursue their respective mandates in close coordination, building on interagency cooperation arrangements and planning prepared in normal times.

The RA would take the lead in determining the resolution strategy for a nonviable bank. Building on, but not bound by, the resolution plan, the RA would apply one or more resolution powers, such as transfer powers, a bridge bank, bailing in shareholders and unsecured creditors, or liquidation. A DIS with a "paybox plus" mandate could fund such resolution measures subject to a least-cost safeguard. Apart from the funding, the DIS would identify insured deposits in the nonviable bank and provide the RA with the necessary data, for example, to transfer insured deposits.

In a liquidation without a transfer of insured deposits, the DIS would prepare and execute the reimbursement of insured deposits. When the RA decides to resolve a bank through liquidation, this should trigger the payout of insured deposits. The DIS would then promptly (ideally within seven working days) reimburse depositors. Bank liquidation, including distributing recoveries to creditors, would be executed by an administrator, with some involvement of the RA or the DIS (through either oversight or direct responsibility).

In a broader financial crisis, the roles of the two authorities may change. A DIS is typically not (expected to be) sufficiently well funded to deal with systemic failures, making a payout in such events an unrealistic option. An RA, on the other hand, may be expected to manage the failure of a systemic bank. Although the DIS may not be directly involved, it would still play a crucial role in crisis communications to reinforce public awareness of deposit protection and help mitigate the risk of deposit runs.

¹¹ This is not only the case for the RA and the DIS but also the case for the central bank with its lender of last resort function, which requires involvement at an early stage.

¹² The KA require that the authorities be able to intervene and resolve a bank when it is (or is likely to become) no longer viable with no reasonable prospect of return to viability. This may occur before a bank is balance sheet insolvent, including circumstances in which regulatory capital or required liquidity fall significantly below minimum requirements; there is a serious impairment of a bank's access to funding sources; or it is expected in the near future to be unable to pay liabilities as they fall due.

V. Agree to Disagree

Potential conflicts of interest may arise both between financial safety net authorities and with industry participants. Irrespective of whether financial safety net functions are assigned to one or more agencies, in certain resolution scenarios these functions may potentially conflict, for example, the RA selling (parts of) the nonviable bank during resolution, the supervisor being concerned about the health of the purchasing bank, the DIS funding a transfer of insured deposits in a resolution, the central bank being a creditor from the provision of emergency liquidity assistance (ELA), and the MOF seeking to minimize taxpayers' risks.

A. Potential Conflicts between Bank Resolution and Deposit Insurance Functions

The extent of potential policy conflicts partly depends on the mandate and the level of discretion of the DIS. A DIS can have different mandates: from paybox (deposit payout) and paybox plus (resolution funding) mandates to more sophisticated loss and risk minimizer mandates, which combine deposit insurance functions with those of resolution and—in addition—supervision. A simple paybox mandate requires less discretion of the DIS: it would collect and invest funds and reimburse insured depositors when banks fail. In the case of a DIS with mandates that extend into responsibilities for funding or implementing resolution measures, the discretion of the DIS and the potential for conflicts may increase. In these cases, having ex officio members from other financial safety net authorities on the DIS board may, for example, raise autonomy concerns, which would be less of a concern in the case of a paybox mandate only. Under a paybox plus mandate, DIF resources are available for the RA to protect (insured) depositors in resolution, for example, through a transfer to another bank or bridge bank, if a resolution measure were expected to be less costly for the DIS than the counterfactual of liquidation and depositor payout. This least-cost test, a safeguard limiting the financial obligation of the DIS in a resolution, may bring this potential conflict of interest to the fore. When the RA and the DIS are separate, autonomous agencies—rather than an integrated agency with a dual mandate—they may take different views on whether the safeguards (including the least-cost test) are met.¹³ They may also disagree on the credibility of the resolution strategy.

B. Potential Conflicts with Other Financial Safety Net Authorities

The timely handover of distressed banks from supervision to resolution is critically important for cost-effective resolution. The supervisor and the RA may have different viewpoints when dealing with problem banks. For going-concern considerations, the supervisor could delay acknowledging that a bank has become, or is at risk of becoming, nonviable, whereas the RA—from a gone-concern perspective—may want such determination to be made as early as possible before net assets, liquidity, and franchise value are further eroded. For example, focusing on rehabilitating a problem bank, the supervisor may argue for more time to turn the bank around, whereas the RA may deem the bank no longer viable.¹⁴ Delaying the decision to trigger resolution may increase resolution costs as a bank's portfolio and franchise value further deteriorate, and asset stripping or "gambling for redemption" may occur. Similar conflicts can also exist between

¹³ To allow for a swift resolution implementation, a DIS should authorize the use of its funds on the positive assessment of the RA that the least-cost test and any other safeguards are being met. Should an ex post assessment find that the DIF provided more resolution funding than it would have in a payout scenario, monetary compensation for the DIF from the RA could be considered. See, for example, the proposed mechanism in the UK's Bank Resolution (Recapitalization) Bill (<https://bills.parliament.uk/bills/3734>; draft).

¹⁴ To counter the risk of delays in supervisory action, an RA could be given backup authority to trigger resolution. However, this could, particularly in smaller jurisdictions, misallocate scarce supervisory resources to the RA and may not necessarily result in earlier interventions (for example, in a system where legal protection and accountability are weak).

supervision and deposit insurance functions, especially around the entry into liquidation/resolution, recognizing that earlier intervention could result in a higher recovery rate for the DIF during the liquidation.

Liquidity needs of banks in resolution give central banks a key role in resolution decisions. In resolution, the RA will determine the resolution strategy, including resolution funding options. A failing bank may have received ELA from the central bank before resolution, and further ELA might be needed to address liquidity pressures after resolution (see Dobler and others 2016). Although the supervisory authority would make a positive determination of viability, it should be at the sole discretion of the central bank to decide on (further) ELA provision. Consequently, where the RA and the central bank have different views on the credibility of the resolution strategy and the ability of the recipient to repay the central bank, resolution decisions could be delayed or hampered.¹⁵

Government ministers will have wider interests at play in resolution cases. Involving ministers or other political bodies in resolution decision making could risk political pressure to delay resolution or undue influence on the preferred resolution strategy (for example, to protect national interests). Accordingly, resolution measures that do not require public funds—that is, they can be undertaken with the industry-funded resources of the DIF or resolution fund—should fall under the RA’s sole mandate, without the need for government consent. The MOF should nevertheless be informed to monitor whether taxpayer money could become at risk, because, for example, the DIS may have MOF backstopping.

Requiring other safety net authorities’ consent for certain decisions of the DIS should not be considered undue interference. For example, a DIS may not have sole authority to change the deposit insurance coverage level, the bank levy rates, or the DIF target level. Decisions that affect not only the DIS but also the (profitability of) levy-paying member banks, or increase the contingency liabilities of a public backstop, may not be taken exclusively by the DIS. These decisions will need to be informed by wider financial stability and fiscal considerations, which may merit the involvement of other financial safety net authorities.

C. Potential Conflicts with the Industry

Significant conflicts of interest may arise if active banking-industry representatives are involved in the governance structure of a DIS or an RA. Both functions deal with confidential supervisory data, ratings, and assessments and with market-sensitive information, which should not be available to active bankers or their representatives—be it about their own bank or competitors. For resolution, the RA will have to take decisions that may interfere with the property rights of shareholders and creditors (including other banks) when allocating losses. For deposit insurance, levied institutions will have an interest in keeping premiums low and may impede sufficient industry funding of the DIF. Even the perception of conflicts of interest may make other safety net members (especially the banking supervisor) reluctant to share pertinent information with an RA or a DIS, undermining their effectiveness, for example, in preparing sufficiently early for a specific bank failure.

Whereas RAs are usually public sector agencies, some DISs are set up as private or hybrid systems with the involvement of the banking industry.¹⁶ The CP do not rule out private and hybrid DISs, but in practice, this type of DIS may be difficult to fully integrate into the financial safety net and crisis management arrangements, particularly in systems with significant overlaps between bank resolution and deposit insurance functions.¹⁷ Representatives or nominees from the banking industry (including the banking

¹⁵ For traditional ELA, central banks would rely on the supervisor’s solvency assessment. Similarly, central banks should rely on the RA’s viability assessment.

¹⁶ Globally, close to 30 percent of jurisdictions have either a private or hybrid DIS. A hybrid DIS is government regulated but privately administered. In a hybrid DIS, the government entrusts a private law body (for example, a limited company) to perform the public service of running the DIS within the parameters of a public law.

¹⁷ For example, where a DIF can be used in resolution, or the DIA has a resolution-related mandate.

association) can create a conflict of interest because of their (perceived) closeness to banks. For reasons of confidentiality and broader governance concerns caused by a close affiliation with banks, tasking privately owned systems and (sometimes also) a hybrid DIS with a wider mandate may create significant conflicts of interest.

Allowing an RA or a DIS to hold ownership stakes in banks may also create conflicts of interest.

In some jurisdictions, a DIS or an RA is allowed to recapitalize a nonviable bank to restructure it afterward. Similarly, some RAs (for example, in Japan, Mexico, and Switzerland) would be responsible for operating a bridge bank. In both instances, these banks would still be active in the market and could have an interest in expanding their deposit base or loan portfolio, whereas the RA or DIS would aim to limit risks to their own balance sheets. These conflicts are exacerbated when an RA or a DIS is housed together with the banking supervisors. It would be best if the MOF assumes the ownership of a bank in these cases and manages the bank at arm's length through an independent party (IMF 2022a).

VI. Governance

A. Autonomy and Noninterference

The operational autonomy prescribed by the KA and the CP (see Appendix 2) comprises four components, subject to the constraints and directions laid down in legislation.¹⁸

Institutional autonomy. RAs and DISs should neither seek nor accept instructions from political bodies and the financial industry. Moreover, these stakeholders should be prohibited and refrain from giving instructions to RAs and DISs. A critical requirement of institutional autonomy is that the resolution and deposit insurance functions are housed within an organization that has its own legal personality and is separate from any political (MOF) or commercial entity (banking association), but not necessarily separate from other autonomously exercised financial sector mandates (for example, both functions are housed together or combined with a supervisory authority).

Functional autonomy. RAs and DISs should be free to adopt the policies and choose the most appropriate of their statutory powers to achieve their objectives, for example, the preferred resolution strategies and tools, and depositor payouts outright or by channeling reimbursements through other banks. RAs and DISs should also autonomously adopt their annual and multiyear workplans underpinning their strategic goals and operational activities. They should also have the expertise to undertake their own risk and policy analyses when these functions are combined with other mandates.

Personal autonomy. The appointment and dismissal procedures for the senior officials tasked with overseeing and executing the resolution and deposit insurance functions should ensure that these officials can freely fulfill their responsibilities, consistent with the concepts of institutional and functional autonomy. This should include transparent processes for appointment on set terms—preferably longer than the political cycle—and removal from office only for reasons set out in law, internal statutes, or rules of professional conduct, and not without cause. Autonomy also requires strong legal protection for the current and former decision makers, staff, and agents of an RA or a DIS (see “Legal Protection”).

Financial autonomy. RAs and DISs should have sufficient financial means to execute their mandate effectively. This requires budgetary autonomy to determine operational financing needs, funding for investments (for example, IT), and staffing levels. Resources of the DIF and resolution fund should not be comingled with other funds, and both functions should have their own budget line if housed in other financial safety net authorities.

To ensure the autonomous execution of the resolution and deposit insurance functions, they should be functionally separated from the other mandates with which they are combined. Although housing these functions, for example, in a central bank or a supervisory authority has the appeal of achieving synergies, such combination also gives rise to potential policy conflicts among different mandates, as discussed in the previous section. Functional separation is critical to effectively deliver on each of these mandates (and also applies to the ELA function).¹⁹ In some jurisdictions, such as the European Union, this is prescribed by law.

¹⁸ Although international standards refer to “independence” or “operational independence,” we prefer the concept of “autonomy.” The latter acknowledges the reality wherein public entities depend by design on political stakeholders (for their existence, mandate, funding, and leadership) and asserts these public entities’ ability to execute their statutory mandates freely, but within the constraints and directions stated in legislation.

¹⁹ Functional separation need not entail separate boards or committees within an agency for its several mandates.

Several organizational measures should support functional separation.

- **Dedicated teams.** First and foremost, a dedicated expert team should be assigned to each function. The team should be responsible for business-as-usual activities in regular times, including resolution planning and verifying depositor data. It is important, though, that live contingency planning activities—when the failure of a distressed bank appears to be imminent—and determining and executing the resolution strategy, including postresolution restructuring, are led by the resolution function. Dedicated teams entail staff who are working full time on the core tasks of the resolution and deposit insurance function, which can be supplemented with additional resources at surge times.
- **Reporting lines.** Although a multimandate organization may centralize the oversight of all powers at the highest level—typically the senior executive management or board—functions should report to different sublevels, such as deputy governors or executive directors.²⁰ To ensure equal standing within the organization, the resolution function should report to the same seniority of official as the supervision function.
- **Transparent decision making.** To ensure well-informed and balanced decision making with appropriate accountability, the several perspectives on, and analyses of, a bank failure and the required interventions should be transparently presented to the highest decision-making body and the outcome of its deliberations documented.
- **Agility.** The foregoing should not prevent prompt decision making in time-sensitive, high-stress, information-limited cases. Functional separation should not come at the cost of an authority's agility and allow timely escalation of decision making. Similar to banks being required to ensure agile governance structures for recovery measures, which complement regular decision-making procedures for business-as-usual risk management, financial authorities, too, should have accelerated decision-making procedures as part of their contingency preparations.

BOX 1. Multimandated Resolution Authorities—Governance Arrangements in the Netherlands, South Africa, and the United Kingdom

The Netherlands

The Dutch central bank (De Nederlandsche Bank [DNB]) is tasked with supervising the financial sector, administering the deposit insurance system, extending emergency liquidity assistance, and resolution of financial firms. DNB is managed by a Governing Board, comprising a president and four executive directors. Although the Governing Board members are jointly responsible for DNB's management, one executive director is responsible for resolution (and has, among others, a casting vote on certain resolution matters), and two executive directors are, in principle, mandated with the supervisory task that ensures functional separation. Decision making on supervision and resolution is being prepared by a Supervision Council and a Resolution Council, respectively.

South Africa

The resolution mandate is carried out by the Resolution Planning Division of the South African Reserve Bank. The division is part of the Financial Stability Department, which reports to the deputy governor for financial stability. The recently established Corporation for Deposit Insurance is reporting to the

²⁰ See, for example, the different approaches in the RAs in the Netherlands, South Africa, and the United Kingdom (Box 1).

same deputy governor. The resolution and deposit insurance functions are operationally distinct from the Prudential Authority, whose CEO is another deputy governor of the South African Reserve Bank.

United Kingdom (UK)

The Bank of England (BOE) is the resolution authority. The BOE is responsible for liquidity support, including traditional emergency liquidity assistance, and where it is acting to resolve a firm, the resolution liquidity framework is also available to it. Through its Prudential Regulation Authority (PRA) responsibilities, the BOE supervises financial firms. The PRA is tasked with determining whether an institution is failing or likely to fail and is consulted on other resolution decisions. The most important resolution decisions are reserved for, or may be escalated to, the governor (who is advised by the deputy governors in the Executive Committee). Day-to-day management of resolution matters is the responsibility of the executive director for resolution who reports to the deputy governor for markets and banking. A Resolution Committee, which has members from across the BOE, including the PRA, advises the deputy governor on the most significant firms. The executive director for resolution decides (after advice from another committee, the Resolution Advisory Committee) on most other resolution matters.

B. Composition of the Board

Oversight should be clearly distinguished from executive management. Typically, the role of a governing body is to direct and oversee senior management and to provide strategic direction. A board will most likely also deal with major plans of action, risk management and investment policies, internal control systems, the integrity of accounting and financial reporting systems, annual budgets, business plans, and the agency's overall performance. Senior management is responsible for translating the governing body's directions into action and for carrying out the agency's daily operations. In the case of a single board where the executives sit on the agency's board, there should be a majority of non-executive members to mitigate potential conflicts of interest and to ensure effective oversight over the executives.²¹ Furthermore, the responsible manager or executive should not chair the board, because this could diminish a board's oversight function. Last, the executives should not participate in deliberations and decisions regarding the discharge of their duties or in matters where they, or their (extended) family members, have an interest.

When the resolution and deposit insurance functions are combined with other mandates, the composition of the authority's governing body should reflect its broad mandate.²² These functions require specialized expertise and experience, distinct from an authority's other mandates. Those responsible for nominating and appointing the members of the governing body and senior management of a multimandate agency, including resolution and deposit insurance, should ensure that pertinent expertise is in place on the board for all its mandates.

The composition of a board that is responsible for resolution and deposit insurance functions should reinforce their autonomy and mitigate conflicts of interest with the industry, politics, and

²¹ Irrespective of a single or dual board structure, a board should have an uneven number of members to reduce the need for the chairperson to cast a tie-breaking vote.

²² Strengthening the skill set of a multimandated agency's governing body is to be preferred over creating an additional committee or board within the agency for the resolution or deposit insurance function.

other safety net members. In the case of ex officio members, legislation should require all governing body members to act in the best interest of that body instead of their home authority.

- **Industry.** Active managers, shareholders, and creditors of financial firms, their industry associations and their representatives or nominees, should not serve on RA or DIS boards. The autonomy of the RA or DIS from the industry is more important than accountability to the (levy-paying) industry or the utilization of commercial banking expertise.²³ For stakeholder consultations, bankers and bank-affiliated experts could be involved through an advisory council.
- **Political appointments.** To prevent politicizing firm-specific resolution and deposit insurance decisions, members of elected or appointed political bodies should not be involved in the governance of an RA and a DIS, especially if they are also creditors and shareholders particularly of state-owned banks. Their involvement (when taxpayer money is at risk) does not warrant a board seat and can be addressed through consent in the resolution decision-making framework.
- **Financial safety net.** Especially when a separately established DIS has an expanded mandate, including resolution powers, real or perceived conflicts of interest could arise if representatives from other safety net agencies such as the supervisor or the MOF act as chair or have a voting majority. Arguably, the same holds for RAs and resolution colleges. Other agencies' expertise and views can be captured through interagency consultation and do not warrant a board seat. If these agencies' representatives have a board seat, a majority of independent, qualified experts must act as a counterweight.

In addition to the above-listed incompatibilities, rules on (dis)qualifications and conduct should provide further assurances of integrity.

- **Qualifications.** Members of a governing body and senior management should meet formal qualifications (for example, a pertinent higher education degree) and have pertinent professional experience (for example, in banking, economics, law, or finance). Besides these personal qualifications, the composition of boards should ensure sufficient collective expertise across the agency's mandates.
- **Disqualifications.** Persons with a criminal record or histories of bankruptcies and professional misconduct should be excluded in statute from the governing body or senior management.
- **Code of conduct.** Binding members to relevant laws, conflict of interest codes (including recusal rules), and codes of conduct will lessen the potential for conflict of interest or misconduct. That said, such safeguards cannot undo the fundamental concerns raised by the participation of active bankers and politicians in the governance of resolution and deposit insurance functions.

Clear rules and procedures for the appointment and dismissal of members of the governing body and its management further serve integrity, autonomy, and noninterference. The law should set out the process for appointing and removing board members and senior management. Ideally, two political bodies should be involved (in addition to a potential [proposing] role of the relevant agency itself, for example, nomination and hearing by a parliamentary committee and appointed by MOF/Cabinet). The personal autonomy of decision makers is further supported through security of tenure (with set terms longer than the political cycle) and protection against arbitrary and capricious dismissal.²⁴ Only specific and exceptional

²³ Mechanisms (such as "Chinese Walls" or strict recusal rules) to prevent industry representatives from accessing firm-specific confidential information and participation in firm-specific decision making could address conflict of interest concerns. However, these mechanisms would beg the question of why industry representatives are present at all. These mechanisms would also hamper the effective overall governance and performance of an RA or a DIS.

²⁴ Furthermore, cascading appointment schedules among board members ensure continuity of leadership by preventing a concurrent replacement of several decision makers.

grounds, such as criminal behavior or gross misconduct, should allow for the removal or disqualification during the term in office. In the case of an early dismissal, subject to legal safeguards (for example, appeal to a judicial body), the grounds for dismissal should be publicly disclosed. Provisions regarding subsequent services (such as a cooling-off period before taking up a position in the financial industry) can also help to prevent conflicts of interest during the tenure.

C. Interagency/Functional Cooperation

Interagency cooperation underpins good governance and is critical for an effective financial safety net. The pertinent international standards require close interagency cooperation among financial safety net members, including analysis and information sharing (for example, IADI CP 4, KA 12.1, and BCP 3). Primary law should ensure cooperation by allowing interagency information exchange and outlining areas for cooperation and coordination, typically through a national crisis management committee. A memorandum of understanding or an equivalent should detail the operational modalities for the exchange and cooperation duties, including identifying contact persons and timelines to exchange pertinent information. The division of labor and interagency interaction requirements for preparing to deal with bank failures or a system-wide crisis should be clearly defined and publicly disclosed. For example, procedures should specify when and how the banking supervisor and the ELA provider should inform the RA and the DIS about certain developments and interventions at distressed banks. Furthermore, an RA and a DIS should coordinate their contingency plans with each other, and the wider safety net, to ensure the plans' complementarity and cohesiveness. For example, although the RA has the power to enable a transfer of insured deposits from a failing bank to another bank, it will need to rely on depositor data verified by the DIS. Clear mandates and procedures also help to manage potential conflicts of interest and support a coordinated response. These arrangements can also reveal and resolve at an early juncture any differences in opinion between the several safety net functions.

Cooperation arrangements should respect the autonomy of each financial safety net authority. They should not be subjugated to the will of other safety net members (for example, by a majority vote in committees). As best practice, such committees should be of a consultative nature without decision-making powers. Where these committees do decide, for example, whether certain resolution tools can be used (for example, bail-in only in systemic cases), the committee's deliberations and decisions should be transparently documented to enable accountability and protect the RA. Moreover, prompt resolution decision making and agency autonomy should be balanced. For example, when a resolution strategy requires DIF funding, these funds must be provided with certainty, but subject to prescribed safeguards, including that the DIA receives sufficient advance notification and information to fulfill its obligations. Cooperation arrangements should specify the information needs and deadlines for making DIF funds available in resolution.

Even when several functions are housed within one agency, formal arrangements for information exchange and coordination are needed. Where, for example, resolution and supervisory functions are domiciled in a single agency, functional separation should be complemented with formal arrangements specifying when and how the two functions should exchange information and coordinate their actions.²⁵ Although being one authority could support coordination, it cannot be taken for granted that both functions will always exchange pertinent information on time and that different supervision and resolution viewpoints are transparently presented to the decision makers. As these functions' autonomy needs to be safeguarded, arrangements also need to counter the risk of a silo mentality. An internal coordination committee or other

²⁵ This could be done either between the two departments or with the approval of senior management (or board) depending on the agency's practices.

in-house cooperation arrangements could, for example, serve as a platform for exchanging information, planning efforts, preparing decisions, and resolving conflicts of interest.

D. Scaling Up

Operational modalities should enable flexibly expanding the resources for the resolution and deposit insurance functions as a bank approaches failure.²⁶ The resolution team, for example, will need more staffing and different expertise during prolonged periods of live contingency planning and implementation and in the case of postresolution restructuring. The team should be able to draw additional resources from within and outside the organization. Internal policies and budgeting rules should make this readily possible; external expertise may need to be retained for legal, valuation, and IT work, among others.²⁷ Similar arrangements should be in place for the deposit insurance function, for example, to confirm depositor data, recalculate payout amounts, undertake payouts, and oversee liquidators. Establishing these arrangements in peacetime will allow these functions to scale up for decisive action promptly and flexibly.

E. Transparency and Accountability

The resolution and deposit insurance functions should be transparently executed and held accountable. The KA prescribe rigorous accountability mechanisms for RAs to evaluate their effectiveness. The IADI CP require that the DIS be held accountable to a higher (political) authority, be regularly assessed on the extent to which it fulfills its mandate, and regularly disclose pertinent information. If these functions are combined with other mandates, the transparency and accountability framework could be afforded by, for example, dedicated sections in an agency's annual report and financial statements. Indeed, typically, RAs and DISs publish an annual report and ex post assessment reports (postmortem) on individual resolution or compensation cases, and they also report to a higher authority, such as the government or parliament.²⁸

- **Transparency.** Transparency enables accountability and serves other goals, for example, raising the general public's awareness about the DIS and managing public expectations for resolution. External audits of industry-funded DIFs and resolution funds should be published. Transparency rules must balance the aims of disclosure for public scrutiny and oversight and legitimate needs for confidentiality (for example, protection of market-sensitive or confidential prudential/banking information).²⁹ Public disclosure requirements should not include publishing detailed firm-specific resolution plans or risk assessments of individual banks, for example, for the purpose of calculating risk-based contributions to the DIF.³⁰

²⁶ General staffing needs, particularly the skill set, may change over time. Initially, policymakers are needed to translate legislation into policies, then staff who understand banks to review recovery plans and develop a resolvability assessment framework. Finally, experts with more technical market knowledge are needed to develop execution procedures to implement resolution tools such as (cross-border) bail-in and transfer powers.

²⁷ The authorities should have a list of vetted and approved experts to help with the management of a bridge bank or an institution undergoing resolution.

²⁸ For example, the Federal Deposit Insurance Corporation (FDIC) regularly conducts informal reviews of actions taken during the course of the resolution of a failed insured depository institution. In addition, the FDIC inspector general must conduct a review and prepare a report (<https://www.fdicog.gov/reports-publications/bank-failures>) when the DIF incurs a material loss related to a bank for which the FDIC is appointed receiver.

²⁹ Freedom of information rules should not require disclosing information that could threaten financial stability.

³⁰ Confidentiality policies should clearly guide and justify disclosures of sensitive and confidential information, even when prescribed by law (see also, the IMF n.d.) or clarify when, for example, public versions of the resolution plans may be published (as is the practice in the United States).

- **Accountability mechanisms.** Accountability mechanisms (such as external and internal audits) should ensure that RAs and DISs exercise their authority in a cost-effective way, consistent with (least-cost) safeguards and sound (financial and operational risks) policies. Typically, an authority's audit body or a country's supreme audit institution would undertake regular audits; in some countries, these audit organizations have also undertaken evaluations of the agency's crisis readiness.³¹

³¹ In addition to regular audits, some audit organizations undertake audits of the agency's crisis readiness. See, for example, the European Union in 2017 (<https://op.europa.eu/webpub/eca/special-reports/srb-23-2017/en/>), the United Kingdom in 2018 (<https://www.bankofengland.co.uk/-/media/boe/files/independent-evaluation-office/2018/ieo-report-resolution-june-2018>), and the United States in 2020 (<https://www.fdicig.gov/reports-publications/audits-and-evaluations/fdics-readiness-crises>).

VII. Legal Protection

Financial safety net participants and their current and former officials, staff, agents, and advisors should enjoy strong legal protection.³² Legal protection supports both accountability (vis-à-vis the judiciary) and autonomy (specifically the agencies' institutional autonomy and the personal autonomy of these agencies' decision makers, staff, and agents). International experience demonstrates that financial institutions, depositors, shareholders, and creditors are more vocal and litigious in case of bank liquidation and resolution actions, which are more intrusive than ongoing supervision. Therefore, all pertinent international standards prescribe legal protection of financial oversight authorities' current and former decision makers, staff, and agents (CP 11, KA 2.6, BCP 2).

Legal protection aims to focus judicial scrutiny of actions and omissions of financial agencies and their representatives on whether they have acted (or refrained from action) in good faith in the exercise of their official duties. Legal protection should not cover criminal offenses, nor does it constitute legal immunity but rather a standard against which (in)actions will be judged in administrative and judicial proceedings. Legal protection should cover the financial cost of litigation. This applies to all legal costs, including damages, legal fees, and other associated costs, which should be borne upfront by the authorities and not by the individuals.

Operational arrangements are needed to make legal protection effective. These arrangements should cover such issues as the choice and (timing of) payment of legal representation and protection against self-incrimination during internal investigations, including when building a case to defend the authorities. Liability and legal aid insurance must cover realistic monetary amounts, considering the high financial stakes at play in resolution cases. Although such insurance is an integral part of an effective framework for legal protection, neither insurance nor contractual indemnity is sufficient, and statutory provisions on legal protection are needed.

³² On the design and practice of legal protection frameworks, see Khan (2018).

VIII. Two Funds in One?

DIFs should contribute to funding bank resolution measures but cannot be expected to have sufficient funds for a systemic event. Funding resolution measures—rather than direct payouts—in nonsystemic cases could help lower the costs for DIFs. For systemic cases, separate funding arrangements are needed to protect uninsured depositors when needed to prevent contagion.³³

Rather than establishing a separate ex ante resolution fund, countries should ensure mechanisms for prompt resolution funding by the government with ex post recovery from the banking sector. It is important that countries use bank levies to prioritize sufficiently funded DIFs (with a paybox plus model which would also allow its use for resolution funding) to deal with regular bank failures instead of establishing separate resolution funds for infrequent (systemic) events.

Where ex ante funded DIFs and resolution funds coexist, country authorities should consider the following design features for these funds:

- **Clarity.** The use of funds and their sources should rest on a clear legal framework. Safeguards and procedures will need to be stipulated if the RA can use the DIF for resolution measures.
- **Efficiencies.** Managing the bank levies for both a DIF and a resolution fund requires the same expertise to calculate and assess levies and to invest and convert to cash the collected levies. Arguably, it is efficient to assign these responsibilities for both funds to the same entity.
- **Separation.** Where both funds are managed by a single entity, the two funds must remain legally separate. Furthermore, a resolution fund should not borrow from a DIF. Otherwise, the DIF could be underfunded while being repaid from the resolution fund.
- **Accountability.** Both DIFs and resolution funds should be externally audited and accounted for separately from the audit and annual report of the entity where these funds are housed. Additional audits by a supreme audit institute may be required to ensure compliance with the funds' statutory mandates and for value-for-money assessments.

With the emergence of more effective resolution frameworks, the role of the DIS is changing in many jurisdictions. The traditional paybox responsibility of a DIS was to ensure a prompt payout of insured deposits after a bank had been declared insolvent. With special bank resolution frameworks becoming more prevalent, such payouts may become less the norm because of more effective resolution options being available, for example, a deposit transfer tool, which better ensures continuity of depositor services and may be more cost-effective. The banking turmoil in early 2023 demonstrated that the speed of restoring depositor access to their funds is becoming more important in an era of 24-7 internet banking and shifting depositor expectations.

Jurisdictions that are newly establishing a DIS (or both the bank resolution and deposit insurance functions) should consider integrating the deposit insurance function within their RA.³⁴ To ensure the operational alignment between these highly interconnected functions requires detailed information exchange and interagency cooperation arrangements when these functions are assigned to separate agencies. Notwithstanding these arrangements, a back-and-forth between the two agencies about, for example, the resolution strategy's viability or the least-cost test makes the resolution process lengthier and less predictable. To ensure the reliability of a DIF as a funding source for resolution, the DIS's decision-making power over the use of DIFs should be limited, which begs the question of why a DIF should exist

³³ For an elaborate discussion of resolution funding, see IMF (2018).

³⁴ See Box 2 for a country example (Denmark) of an integrated resolution and deposit insurance agency.

separately from the RA. Housing the two functions in separate institutions exacerbates conflicts of interest and concerns about each institution's formal autonomy.

If an RA would be responsible for the DIF, these functions' mandates and operations could be better aligned. Such alignment can be achieved building on several considerations:

- The functions share public policy objectives to support financial stability and to protect depositors.³⁵
- The responsibilities of the functions to monitor the risk of failure of the same group or firm, their effect on depositors, and the estimated resolution costs as well as expected recoveries can be integrated.
- Contrary to supervision, both functions have a shared interest in triggering resolution (either restructuring or liquidation) early to maintain franchise value, limit costs, and keep recoveries high.
- The time-tested and cost-effective transfer tool can be applied in both restructuring and liquidation, subject to the RA's decision and in using a DIF.
- Such use of a DIF would give the resolution framework a reliable funding source and is also in the interest of insured depositors and the DIF.
- Joint staff would allow for synergies in skill sets, expertise, and operations that would enhance capabilities and capacity and reduce administrative costs while also improving integrated contingency planning and providing meaningful work for deposit insurance staff during times when there are no bank failures (for example, resolution planning and transfer simulations).

Integrating the DIF into the RA would also help mitigate potential conflicts of interest between formally autonomous institutions and ensure proper information exchange and coordination. An integrated mandate for resolution and deposit insurance may most efficiently use scarce expertise in countries with low capacity, with one authority responsible for dealing with problem banks in the interest of financial stability and depositor protection. Under this model, the RA would manage the DIF that is authorized to contribute to resolution funding in nonsystemic events, and one of the RA's teams would develop the payout capacity as a fallback option if a transfer of deposits is not feasible. The least-cost test would evolve to a requirement for the RA to choose the resolution option that costs the least in terms of the use of public resources, including the DIF, and is in the interest of financial stability. The need for a separate resolution funding vehicle would cease because the DIF would combine both functions.³⁶ This authority would be a strong partner for other members of the safety net, thereby strengthening the overall financial stability framework.

³⁵ RAs may also aim to limit the use of taxpayer money in resolution, but this would not contradict a DIS's objectives, because it should use its funds in a way that limits reliance on a public backstop.

³⁶ Nevertheless, such integration should involve legal safeguards such as legal segregation of the DIF in order to protect the RA's patrimony from the liabilities of the DIF (and vice versa, the resolution funding mechanism from the deposit insurance function). A DIF should also not completely be depleted through funding resolution in order to maintain a minimum level of funds to support depositor confidence in a functioning DIS.

BOX 2. Denmark's Finansielt Stabilitet—An Integrated Resolution and Deposit Insurance Agency

Denmark's Finansielt Stabilitet (FSC) offers an example for a combined resolution authority (RA) with deposit insurance functions. The FSC is a public entity that is an RA with deposit insurance system responsibilities. It is primarily tasked with contributing to financial stability in Denmark and discharging the responsibilities and powers assigned to it, particularly under the Resolution Act and the Deposit Insurance Act.

The FSC was established in 2008 in response to the global financial crisis with a mandate to resolve failing banks. In 2015, it was appointed RA together with the Danish supervisor. The assets and liabilities of the then separate deposit insurance system were transferred to the FSC in the same year.

The FSC manages the resolution fund, the deposit guarantee fund, and the legacy portfolios from bank support packages extended by the Danish government during the global financial crisis. Under a statutory requirement, these assets must be managed separately and segregated from each other. FSC is not liable for the guarantee fund or the resolution fund, and these are only liable for their own obligations and liabilities. The funds are not independent legal entities, and the FSC acts on their behalf, for example, when applying for backstop funding from the government.

After the use of resolution powers, the FSC is responsible for winding down the failed entity and its remaining assets and is also pursuing liability lawsuits against the former management of failed banks. In 2022, FSC had a staff of 41.

Sources: 2020 Denmark; FSAP; and Fund staff.

APPENDIX 1. International Standards on Bank Resolution and Deposit Insurance

The Key Attributes of Effective Resolution Regimes for Financial Institutions (Key Attribute(s); KA)

The KA aim to promote global convergence on managing the failure of too-big-to-fail financial firms.

The KA prescribe designating a public body as the administrative RA, with powers to ensure the continuity of critical functions through a sale or transfer of the firm's shares, a transfer of all or parts of a firm's business (purchase and assumption transaction) to a private sector purchaser or a publicly owned bridge institution,³⁷ or a mandated creditor-financed recapitalization (bail-in).³⁸ Most of the KAs apply to any financial institution that could be systemically significant or critical at the time of their failure (KA 1.1). Resolution regimes should cover global and domestic systemically important banks and other banks that could be deemed systemic at the time of failure.

The Core Principles for Effective Deposit Insurance Systems (CP)

Deposit insurance is critical in maintaining depositor confidence and preserving financial stability.

Deposit insurance minimizes the risk of bank runs and mitigates contagion risk by protecting mainly (unsophisticated) retail depositors in a bank failure. If depositors trust a deposit insurance system, they are less likely to run on a bank and exacerbate liquidity stress, undermining recovery or resolution measures. Experience during the global financial crisis underscored the criticality of deposit insurance, prompting important enhancements (FSB 2008, 2012; IADI 2012; IMF 2020a). Then the CP were adopted in 2009 and revised in 2014.³⁹ The 16 CP set a benchmark for establishing or strengthening a deposit insurance system, against which countries can judge their own system's effectiveness.

³⁷ For some RAs, such as the US Federal Deposit Insurance Company, the preferred resolution method is a purchase and assumption transaction, which is a time-tested and cost-effective tool in liquidations as well (IMF 2020b).

³⁸ RAs should also have liquidation powers to effect the orderly closure and wind-down of all or parts of a firm's business in a manner that protects retail customers (see KA Preamble and KA3.2(xii)).

³⁹ The 2010 Assessment Methodology was replaced in 2016 with an Assessment Handbook (https://www.iadi.org/uploads/IADI_CP_Assessment_Handbook_FINAL_14May2016.pdf).

APPENDIX 2. International Standards on Governance

Financial Stability Board Key Attributes of Effective Resolution Regimes for Financial Institutions (KA)

KA 2.5 (FSB 2014) provides that the resolution authority (RA) should have operational autonomy consistent with its statutory responsibilities, transparent processes, sound governance, and adequate resources and be subject to rigorous evaluation and accountability to assess the effectiveness of any resolution measures. It should have the expertise, resources, and operational capacity to implement resolution measures with respect to large and complex firms.

The KA Assessment Methodology for the Banking Sector (FSB 2016) clarifies that operational autonomy does not mean that the RA must be institutionally separated from other functions, such as supervision or deposit insurance. It calls for governance arrangements to manage conflicts of interest between those functions. The methodology notes that accountability is strengthened through internal and external reviews and evaluations, including the publication of an annual report. Human and financial resources need to be appropriate to allow the RA to fulfill its resolution functions.

The RA and its staff should be protected against liability for actions taken and omissions made while discharging their duties in the exercise of resolution powers in good faith, including actions in support of foreign resolution proceedings.

International Association of Deposit Insurers Core Principles for Effective Deposit Insurance Systems (CP)

CP 3 (IADI 2014) provides that the deposit insurer should be operationally autonomous, well governed, transparent, accountable, and insulated from external interference.

The CP Essential Criteria and the Assessment Handbook (IADI 2016) stress the need for the availability of adequate resources and accountability. Potential (real or perceived) conflict of interest may arise because of the involvement of active bankers and a preponderance of representatives of other safety net organizations.

CP 11 states that the deposit insurer and individuals working both currently and formerly for the deposit insurer in the discharge of its mandate must be protected from liability arising from actions, claims, lawsuits, or other proceedings for their decisions, actions, or omissions taken in good faith in the normal course of their duties.

Basel Core Principles for Effective Banking Supervision (BCP)

The BCP were revised in April 2024 to, among others, strengthen governance arrangements for supervisors. BCP 2 prescribes that the supervisor has operational autonomy, transparent processes, sound governance, budgetary processes that do not undermine autonomy, and adequate resources. The supervisor should be accountable for the discharge of its duties and use of its resources. The legal framework should protect the supervisor.⁴⁰

⁴⁰ For “legal protection,” see also KA 2.6 and CP 11.

The BCP Essential Criteria include the following requirements, among several others:

- The operational autonomy, accountability, and governance of the supervisor are prescribed in legislation and publicly disclosed. There is no government or industry interference that compromises the supervisor's operational autonomy. The supervisor has full discretion to set prudential policy and take any supervisory actions or decisions on banks under its supervision.
- The supervisor has effective internal governance and communication processes that enable timely supervisory decisions to be taken at a level appropriate to the significance of the issue and expedited procedures in the case of an emergency. The allocation of responsibilities within the organization and the delegation of authority for particular tasks or decisions are clearly defined. Supervisory processes include internal checks and balances to support effective decision making and accountability. The governing body is structured to avoid any real or perceived conflicts of interest.
- The process for the appointment and removal of the head of the supervisory authority and members of its governing body is transparent. The head of the authority is appointed for a minimum term and is removed from office only for reasons specified in law or if they are not physically or mentally capable of carrying out the role or have been found guilty of misconduct. The reason(s) for removal is (are) publicly disclosed.
- Laws provide protection to the supervisor and their staff against lawsuits for actions taken or omissions made while discharging their duties in good faith. The supervisor and their staff are adequately protected against the costs of defending their actions or omissions made while discharging their duties in good faith.

REFERENCES

- Basel Committee on Banking Supervision. 2024. "Core Principles for Effective Banking Supervision." September. <https://www.bis.org/bcbs/publ/d573.htm>.
- Bank for International Settlements. 2021. "Institutional arrangements for bank resolution." May. P. Baudino, C. Sánchez, and R. Walters. FSI Insights on Policy Implementation 32. www.bis.org/fsi/publ/insights32.pdf.
- Dobler, M., S. Gray, D. Murphy, and B. Radzewicz-Bak. 2016. "The Lender of Last Resort Function after the Global Financial Crisis." IMF Working Paper WP/16/10, International Monetary Fund, Washington, DC. <https://www.imf.org/external/pubs/ft/wp/2016/wp1610.pdf>.
- Financial Stability Board (FSB). 2008. "Report of the Financial Stability Forum on Enhancing Market and Institutional Resilience." April. https://www.fsb.org/wp-content/uploads/r_0804.pdf.
- Financial Stability Board (FSB). 2012. "Thematic Review on Deposit Insurance Systems Peer." Peer Review Report, February. https://www.fsb.org/uploads/r_120208.pdf
- Financial Stability Board (FSB). 2014. "Key Attributes of Effective Resolution Regimes for Financial Institutions." <https://www.fsb.org/2014/10/key-attributes-of-effective-resolution-regimes-for-financial-institutions-2/>.
- Financial Stability Board (FSB). 2016. "Key Attributes Assessment Methodology for the Banking Sector." <https://www.fsb.org/2016/10/key-attributes-assessment-methodology-for-the-banking-sector/>.
- International Association of Deposit Insurers (IADI). 2012. "Research Paper on Handling of Systemic Crises." October. <https://www.iadi.org/2012/10/research-paper-on-handling-of-systemic-crises/>.
- International Association of Deposit Insurers (IADI). 2014. "Core Principles of Effective Deposit Insurance Systems." <https://www.iadi.org/uploads/cprevised2014nov.pdf>.
- International Association of Deposit Insurers (IADI). 2016. "A Handbook for the Assessment of Compliance with the Core Principles for Effective Deposit Insurance Systems." https://www.iadi.org/uploads/IADI_CP_Assessment_Handbook_FINAL_14May2016.pdf.
- International Monetary Fund (IMF). 2014. "Cross-Border Bank Resolution: Recent Developments." IMF Board Paper, Washington, DC. <https://www.imf.org/external/np/pp/eng/2014/060214.pdf>.
- International Monetary Fund (IMF). 2018. "Resolution Funding: Who Pays When Financial Institutions Fail?" O. Croitoru, M. Dobler, and J. Molin. IMF Technical Notes and Manuals 2018/001, Washington, DC. <https://www.imf.org/-/media/Files/Publications/TNM/2018/tnm1801.ashx>.
- International Monetary Fund (IMF). 2019. "Macroeconomic Developments and Prospects in Low-Income Developing Countries—2019." IMF Policy Paper, Washington, DC. <https://www.imf.org/-/media/Files/Publications/PP/2019/PPEA2019039.ashx>.
- International Monetary Fund (IMF). 2020a. "Managing Systemic Banking Crises—New Lessons and Lessons Relearned." M. Dobler, M. Moretti, and A. Piris. IMF Departmental Paper Series 20/05, Washington, DC. <https://www.imf.org/~media/Files/Publications/DP/2020/English/MSFCEA.ashx>.

- International Monetary Fund (IMF). 2020b. "United States, Technical Note—Financial Crisis Preparedness and Deposit Insurance." A. Arda and P. Honohan. IMF Country Report 20/245, Washington, DC. <https://www.imf.org/-/media/Files/Publications/CR/2020/English/1USAEA2020005.ashx>.
- International Monetary Fund (IMF). 2022a. "Regulating, Supervising, and Handling Distress in Public Banks." M. Adams, H. Y. Aydin, H. K. Chon, A. Morozova, and E. S. Iskender. IMF Departmental Paper DP/2022/010, Washington, DC. <https://www.imf.org/-/media/Files/Publications/DP/2022/English/RSHDPBEA.ashx>.
- International Monetary Fund (IMF). 2022b. "United Kingdom, Technical Note—Select Issues in Financial Safety Net Arrangements and Financial Crisis Preparedness." A. Arda. IMF Country Report 22/106, Washington, DC. <https://www.imf.org/-/media/Files/Publications/CR/2022/English/1GBREA2022007.ashx>.
- International Monetary Fund (IMF). n.d. "Central Bank Transparency Code." <https://www.imf.org/external/datamapper/CBT/#:~:text=The%20CBT%20is%20an%20international,and%20contribute%20to%20policy%20effectiveness>.
- Khan, A. 2018. "Legal Protection: Liability and Immunity Arrangements of Central Banks and Financial Supervisors." IMF Working Paper 2018/176, International Monetary Fund, Washington, DC. <https://www.imf.org/-/media/Files/Publications/WP/2018/wp18176.ashx>.



PUBLICATIONS

Sibling Rivalry in the Financial Safety Net: Governance Arrangements for Bank Resolution and Deposit Insurance

TNM 2025/05

ISBN 9798400293795



9 798400 293795