BERMUDA MONETARY AUTHORITY

CONSULTATION PAPER

SECURING ENHANCED PROTECTION FOR DEPOSITORS
PROPOSALS FOR INTRODUCING DEPOSIT INSURANCE IN BERMUDA

SEPTEMBER 2010

Table of Contents

0. Introduction

1. The financial turmoil of recent years has caused regulators around the world to re-evaluate existing regulatory and institutional frameworks. The incidence of significant losses on the part of financial institutions globally has led to heightened interest on the part of the general public, policy makers and regulators in the key aspects of the financial safety net.

2. The financial safety net typically consists of three elements: prudential regulation and supervision, a lender of last resort, and deposit insurance. In Bermuda, which has no central bank and no deposit insurance, the safety net relies heavily on prudential regulation and supervision by the Bermuda Monetary Authority (BMA or the Authority). The setting and monitoring of requirements for capital adequacy and the assessment of risk within institutions represent key elements in the framework of prudential oversight and control applied by the Authority to help protect the interests of depositors. The approach developed and applied by the Authority in this regard has reflected the regulatory standards designed and promulgated by the Basel Committee on Banking Supervision and other international standard setting bodies. While this approach has served Bermuda well in the past, the unprecedented developments affecting banks in the major developed economies over the past three years suggest that we should now consider the establishment of a deposit insurance scheme in Bermuda to complement the role of the Authority and provide a further layer of protection to depositors.

3. This consultation paper accordingly outlines a proposal to establish a Deposit Insurance Scheme (DIS or the Scheme) in Bermuda. The paper, which sets out the rationale, objectives and proposed features of the DIS, has been drafted by the Authority in consultation with representatives from the Ministry of Finance (MoF). The local banks[1] were invited to comment on an earlier version of the paper. The Authority also

[1] Throughout this paper, the term "banks" is used to refer to institutions licensed under the Banks and Deposit Companies Act 1999, i.e. includes deposit-taking institutions.

wishes to acknowledge the assistance provided by the International Monetary Fund (IMF), which provided technical advice to this project.

4. Comments from members of the public and other interested parties are invited. Responses should be sent to policy@bma.bm by 31 October 2010.

1. Deposit Insurance

5. Deposit insurance is a guarantee to depositors in a bank that they will be compensated up to a maximum specified amount of their deposits upon failure of that institution.

6. The primary function of a DIS is to provide enhanced protection for depositors in the event that an individual banking entity has solvency or other problems that threaten its survival. A well structured DIS can also help to bolster public confidence and thereby help to reduce the risk of problems in one bank escalating into a crisis or spreading to other banks.

7. Deposit insurance should be viewed as an integral part of the arrangements for deposit protection in Bermuda. The implementation of a sound deposit insurance scheme, coupled with a prudent and effective banking regulatory and supervisory framework, would bolster the banking safety net in Bermuda.

2. Objectives of Deposit Insurance

8. The proposed DIS in Bermuda has three main objectives.

2.1. Protect Small Depositors

9. Generally, small depositors are least able to protect themselves. They may lack the resources to interpret available information and assess the soundness of banks and are

more likely to have all or most of their financial assets in the form of bank deposits. Deposit insurance offers protection to the deposits of individual account holders who are within the scope of the scheme.

2.2. Promote Stability in Bermuda's Financial System and Economy by Providing Prompt Reimbursement or Access to Insured Depositors' Funds

10. The protection of small depositors and the stability of the financial system and economy are inter-related to the extent that stability is influenced by the degree of confidence depositors have in the system and their willingness to keep funds on deposit. Loss of savings may result in a fall in local consumption and a loss of public confidence may lead depositors to transfer monies to other countries. A DIS could help prevent this.

11. Public confidence reduces the likelihood that depositors of an individual bank will panic and withdraw funds suddenly if concerns arise about the condition of that institution. Concerns about one bank have at times led to concerns about others, resulting in so-called "contagion runs". Thus, deposit insurance could support the stability and smooth operations of the entire banking system by providing prompt reimbursement or access to insured depositors' funds. Delays in reimbursement can also cause financial hardship for depositors, who may need funds for everyday living expenses. A scheme that provides prompt reimbursement should aid in enhancing public confidence in Bermuda's banking sector and economy.

2.3. Promote Competition

12. Deposit insurance schemes promote competitive efficiency and level the playing field to some degree, for large and small institutions. Under the proposals set out in this paper, depositors in all Bermuda's banks would have access to depositor protection in the amounts specified by the DIS coverage rules.

3. Costs of Deposit Insurance

13. Deposit insurance is not without cost. In the first instance, there is the direct cost of funding the scheme, falling initially on the banks. This will depend on a number of factors, principally the maximum amount it is decided to insure under the scheme (see section 5). As a very rough guide, at a level of $25,000, the recommended maximum amount (see section 5.1), the direct cost is likely to be in the order of $7.8 million to $11.7 million a year. At $50,000, the cost could be some $15.6 million to $19.5 million a year. This equates to roughly $40 - $100 a year for each account covered under the scheme. While only rough estimates, these figures provide some indication of the potential cost of deposit insurance at different levels of coverage and suggest that affordability is an important consideration to bear in mind when deciding the scope of coverage of the Scheme.

14. In addition to the direct funding costs, there will be the costs of administering the scheme itself. Under the proposals set out in this paper (see section 4), it would be intended that these be kept as low as possible. There will in addition be certain indirect costs associated with the introduction of the Scheme. These will include the cost to the Bermuda Government of providing liquidity support to the Scheme while the fund is being built up (see section 7.2) as well as some additional administrative and marketing costs incurred by the banks in complying with the requirements of the Scheme.

15. Although not a direct cost, a related risk of introducing deposit insurance is the possibility that banks will take more risks with depositors' money and depositors will be less concerned if they do when deposit insurance is in place – the moral hazard problem. The Authority's prudent supervision and regulation of insured institutions, along with a carefully implemented and well designed DIS are essential for controlling potential moral hazard.

4. Design of Deposit Insurance

4.1. Structure and Administration

16. It is proposed that the DIS in Bermuda will be established under new legislation to be entitled the "Deposit Insurance Act" (the Act). The Act shall define the establishment, functions and basic operations of the DIS. It is further proposed that the DIS shall be administered by a body to be established and called the Bermuda Deposit Insurance Corporation (BDIC). The BDIC is expected to be an independent statutory institution, headed by a Board of Directors, which shall consist of a Chairman; the Chief Executive Officer of the BMA; the officer of the BMA responsible for the supervision of banks; the Financial Secretary as ex officio members; and not less than two and not more than four other directors. The MoF (after consultation with the Authority) shall appoint the Chairman and other directors of the BDIC from amongst persons with proven experience in banking or financial services.

4.2. Mandate

17. A DIS may be established either with a broad or a narrow mandate. A broad mandate, an example of which would be that under which the Federal Deposit Insurance Corporation in the US operates, would involve incorporating an additional supervisory role to include the active monitoring and inspection of institutions. A narrow mandate would allow the BDIC simply to institute and manage a deposit insurance scheme in Bermuda.

Key Recommendation 1

Given the relatively small size of the banking sector in Bermuda and the desirability of minimizing costs, it is proposed that the BDIC should have a narrow mandate which would not duplicate the supervisory role of the Authority.

4.3. Functions of the Bermuda Deposit Insurance Corporation (BDIC)

18. In the management of the DIS, the BDIC shall exercise the following principal functions:

- (i) collect premiums from participating financial institutions;
- (ii) assess claims made against the DIS fund and determine the eligibility and entitlement of claimants;
- (iii) make compensation payments to eligible depositors as determined;
- (iv) recover any amount paid out to a failed participating bank's depositors from the assets of the failed bank; and
- (v) educate the public on matters relating to deposit insurance arrangements in Bermuda.

4.4. Powers of the Board of Directors

19. In order for the BDIC to discharge its functions effectively, the Board of Directors shall have the necessary powers to finance compensation payments, borrow where necessary to ensure prompt reimbursement to depositors, enter into contracts, invest the DIS fund in the manner specified in the Act, set internal operating budgets and procedures, obtain information from participating banks and appoint agents or authorise third parties to perform any of the functions of the Board of Directors under the Act.

4.5. Relationship between the BDIC and the Bermuda Monetary Authority

20. As part of the Bermuda financial safety net system, the roles of the BMA and BDIC shall complement each other in achieving the common objectives of protecting depositors and promoting stability in the banking system. It is important to have a clear separation of powers and responsibilities and ensure an appropriate balance between these functions. As stated above, under the narrow mandate proposed for the DIS, it would not have prudential regulatory or supervisory responsibilities.

21. The BDIC will, however, need access to timely and accurate information. It is proposed, to avoid duplication of effort and functions, that the BDIC should have access to prudential information and analysis from the BMA. The draft legislation accordingly

makes provision for the sharing of information among safety net participants – the BDIC, BMA and MOF. The BDIC, BMA and MOF employees shall be subject to strict confidentiality obligations, which shall be applicable over cross-departmental boundaries.

4.6. Cross-border Issues

22. As matters stand, local depositors in those Bermuda banks that are subsidiaries of overseas banks are not covered by the home country's deposit insurance scheme. This means, for example, that depositors with accounts at HSBC Bank Bermuda Limited are not covered by the UK Financial Services Compensation Scheme. Nor is it proposed that the DIS in Bermuda will cover deposits held in overseas subsidiaries or branches of Bermuda banks, for example the overseas subsidiaries of Butterfield Bank. Nevertheless, the proposed DIS shall provide for close coordination with other deposit insurers in order to address issues regarding coverage, asset disposition and the reimbursement process.

4.7. Membership

23. Compulsory participation of banks in a DIS is the practice usually adopted internationally. This is to promote comprehensive protection to small depositors and avoid adverse selection, which might give rise to instability in the banking system especially in a case such as Bermuda where there are only a few institutions in the market. Accordingly, it is proposed that the DIS will cover all four banks and the one deposit company licensed to take deposits in Bermuda – HSBC Bank Bermuda Limited, Bank of N.T. Butterfield & Son Limited, Capital G Bank Limited, Bermuda Commercial Bank Limited and First Bermuda Group Ltd.

Key Recommendation 2

It is proposed that membership of the DIS should be mandatory for all four commercial banks and the one deposit company licensed under the Banks and Deposit Companies Act 1999. Feedback is sought as to whether the Scheme should also be extended to cover the savings of qualified members of the credit union.

5. Coverage of Deposit Insurance

5.1. Amount of Coverage

24. A key consideration for any DIS is the maximum amount a depositor can claim from the DIS in the event of a bank failure. The decision on coverage involves consideration of the balance between the desire to instill greater financial stability in times of stress on the one hand, and the need to minimize funding costs and moral hazard on the other. The higher the guarantee, the greater is the risk of moral hazard on the part of depositors and deposit-taking institutions. By contrast, specifying too low a coverage limit could partly negate two of the principal purposes of deposit insurance, namely to protect small depositors and maintain public confidence in the banking system.

25. A rule of thumb that is commonly used and is also recommended by the IMF to help determine the amount of coverage is the 80/20 rule, whereby the maximum amount protected is set at a level that fully covers 80% of insurable deposits[2] by number and 20% by value.

26. Based on account-level data received from the institutions, such an approach in Bermuda would indicate that the maximum amount covered should be set somewhere within the range of $25,000 to $50,000. As Figure 1 below indicates, a level of $25,000 would fully cover approximately 87% of the total number of insurable deposits and 13% by value. A level of $50,000 would fully cover approximately 92% of insurable deposits by number of accounts and 22% by value. Either level, or indeed any point in between, would therefore in broad terms achieve the aim of providing protection to small depositors, who form a large majority of all retail depositors.

27. It should be pointed out that depositors with more than the maximum coverage amount in their bank account would be partially covered. Extending the above calculation

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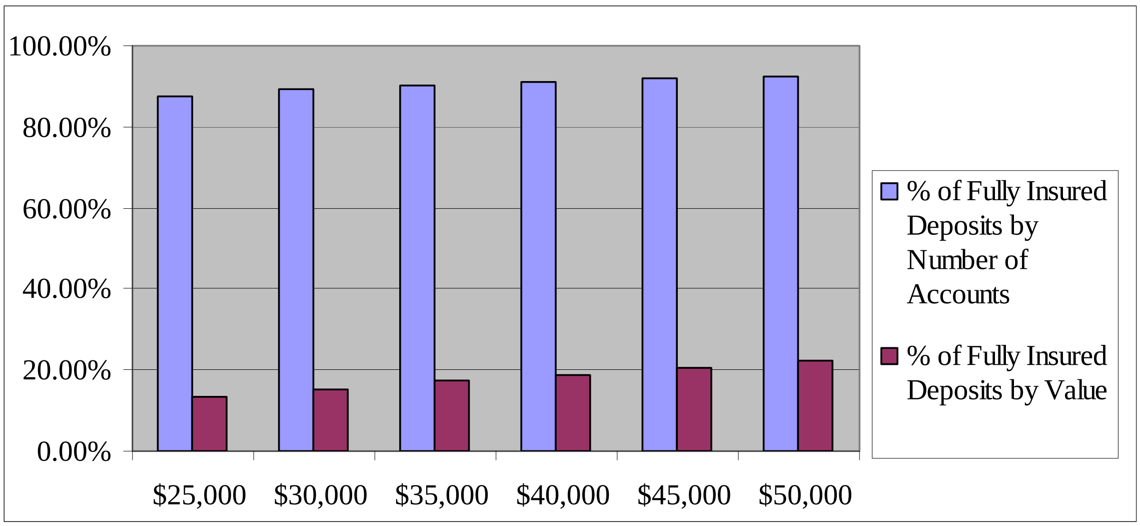
[2] Insured deposits are that portion of the insurable deposits that are protected within the limit of insurance or coverage level. Insurable deposits include all deposits in all categories that are insured, including amounts in excess of the limit on insurance claims.

to include larger deposits covered up to the maximum cap but not fully covered under the Scheme, it is estimated that, at a $25,000 threshold, the total of insured deposits would amount to some 30% of total insurable deposits (or, to put it another way, some 70% of the value of total retail deposits would not be covered by deposit insurance) while, at a $50,000 limit, the figure would be 42% (i.e. 58% would be uninsured).

Figure 1. Deposit Insurance Coverage (Percent)

December 2009



28. Once set, coverage may be reviewed and adjusted from time to time.

Key Recommendation 3

In light of the analysis above, and bearing in mind affordability considerations, it is recommended that the threshold limit initially be set at $25,000. The limit should be reviewed periodically to ensure it remains appropriate.

The Authority seeks views from the public and other interested parties on what an appropriate coverage limit for Bermuda should be. When submitting comments, respondents are asked to bear in mind the objectives of deposit insurance and the fact that a higher threshold will involve higher costs.

5.2. Scope of Coverage

Key Recommendation 4

In line with the objective of small depositor protection at reasonable cost, it is proposed that the DIS shall cover 'retail deposits' only. While there is no precise definition of what constitutes a 'retail deposit', one approach would be to include the following: deposits owned by individuals, trusts, small businesses[3] and charitable organizations[4]. We would welcome comments on this proposal, in particular whether respondents think the definition is too wide or too narrow, and on the definition of 'small business' (see below).

29. It is proposed that insurable deposits of retail depositors shall include:

(i) savings, demand and time accounts;

(ii) cheques[5]; and

(iii) money orders, certified cheques, bank drafts and traveller's cheques issued by the member institution[6].

30. It is further proposed that the following deposits shall be excluded from the DIS coverage:

(i) interbank, government, large corporate deposits;

(ii) insider and related-party deposits, including close relatives and third-parties acting on their behalf (i.e. directors, controllers, senior executives, controlling shareholders, attorneys and auditors of a failed institution); and

(iii) deposits that are related to criminal activity (e.g. money laundering proceeds).

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[3] Small businesses shall include sole proprietors, partnerships and incorporated entities based on the member institution's definition/criteria of "small business".

[4] Charitable organisation (as defined by Charities Act 1978), means any person or body of persons having charitable purposes and relying for its funds substantially upon contributions from members of the public in Bermuda, which is registered under Section 4 of the Charities Act 1978, specified in the Schedule to the Act and excepted by rules made under the Act.

[5] In the case of cheques drawn but not yet cleared, the drawer's account has not been debited yet, thus, the drawer will be entitled to the claim for the total balance of his chequing account up to the coverage limit.

[6] Holders of these instruments, whether the purchaser or payee, will be entitled to the claim, up to the coverage limit.

31. Two further questions relating to scope are whether the Scheme should cover non-residents as well as residents and whether it should cover Bermuda dollar deposits only or be extended to include foreign currency deposits.

32. Estimates suggest that non-resident retail deposits comprise around 19% by value and 15% by number of total retail deposits. This is a material amount. In addition, research has shown that schemes in many other countries do not differentiate between resident and non-resident deposits.

Key Recommendation 5

Bearing in mind the objectives of the Scheme, it is proposed that the DIS cover insurable deposits held by non-residents as well as residents. Extending the Scheme in this way would, we estimate, increase the Scheme's insurable coverage and therefore costs by approximately 24%.

33. The question whether or not to include foreign currency deposits is a significant one, with important consequences for the coverage and cost of the scheme. An argument for inclusion is that the US dollar plays an important role as a medium of exchange within the Bermuda economy. Some 30% by value and 16% by number of total retail deposits as defined above are foreign currency deposits. In addition, a good proportion are small deposits, with 82% of the total number (accounting for 7% of the total value) of insurable foreign currency deposits amounting to less than $25,000 and 88% (13% of total value) amounting to less than $50,000. Arguments against are that people who have foreign currency accounts are likely to be more sophisticated and also that their inclusion would increase the cost of the Scheme.

Key Recommendation 6

The Authority's preliminary view is that foreign currency deposits should be included, reflecting their number and relative importance within the local banking market and the role foreign currency, in particular the US dollar, plays in the local economy.

We would, however, invite comments on both recommendations 5 and 6 concerning coverage of the Scheme.

34. Note that, should foreign currency deposits be included, they would be converted to Bermuda dollars before payout.

35. It is proposed that the DIS be extended on a per depositor and per institution basis. However, accounts held by sole proprietors will be aggregated to the individual accounts and capped to the maximum coverage limit. Also, in cases of joint accounts, balances shall be split equally between account holders, unless there is an express provision to the contrary in the books of the Scheme member. Shares in joint accounts would then be aggregated to individual accounts and capped to the maximum coverage limit. Please refer to Table 1 below for an example of this proposal.

Table 1. Example of Deposit Aggregation

Scenario 1. Depositors A and B maintain individual accounts in the amount of $5,000, each. In addition, they maintain a joint account in the amount $50,000. A separate account is also maintained by Depositor A in his capacity as a sole business proprietor in the amount of $20,000.

	Depositor A	**Depositor B**
Individual account	$ 5,000	$ 5,000
Equal share in joint account	$25,000	$25,000
Sole proprietor account	$20,000	-
Total deposit	$50,000	$30,000
At $25,000 coverage	$25,000	$25,000
At $50,000 coverage	$50,000	$30,000

Scenario 2. Depositors A and B maintain individual accounts in the amount of $40,000 and $10,000, respectively. In addition, they maintain a joint account in the amount of $50,000. A separate account is also maintained by Depositor A in his capacity as a sole business proprietor in the amount of $20,000.

	Depositor A	**Depositor B**
Individual account	$40,000	$10,000
Equal share in joint account	$25,000	$25,000
Sole proprietor account	$20,000	-
Total deposit	$85,000	$35,000
At $25,000 coverage	$25,000	$25,000
At $50,000 coverage	$50,000	$35,000

36. Additionally, liabilities of a depositor covered by the DIS (e.g. loans and advances) may be netted against deposits made with the same institution. Involuntary offsets will be applied to the insured deposit amount only in cases of past due or matured debt obligations. On the other hand, voluntary offsets will be allowed, wherein the depositor could apply part or all of the deposit amounts to obligations which are not yet due.

6. Funding of Deposit Insurance

6.1. Funding Source

37. In order for a DIS to be well-structured and effective, it must have ready access to adequate funds to ensure prompt reimbursement of depositors' claims. The DIS can be funded in diverse ways. Funding sources can be public, private or a blend of government and bank sources.

6.2. Funding Method

38. Contributions may be levied up front to build up a deposit insurance fund (pre-funded), after a bank failure (post-funded) or a combination of both. Post-funding provides finance to the DIS after a bank fails. While this method requires less administrative, maintenance and funding costs, funding requirements may impose a financial burden on the system as the need to pay assessments or levies to deal with failures occurs at an inopportune time. Thus, most countries favour some form of pre-funded scheme. Pre-funding uses periodic contributions by member institutions to build up resources for payouts to depositors in the case of a bank failure. This ensures that a liquid pool will be readily available to make quick payments to depositors, reduces the need for cross-subsidisation (i.e. financial burden being absorbed by surviving institutions) and helps reinforce public confidence in the DIS.

Key Recommendation 7

For these reasons, it is proposed that the DIS in Bermuda should be a pre-funded scheme. Funding will come from the banks that are members of the Scheme although the Bermuda Government may choose to make an initial contribution should it see fit.

39. Pre-funded schemes may also provide for an entrance fee or initial contributions from participating institutions to help build the reserve fund. The fee can be a fixed amount or a percentage of the institutions' capital. The DIS could, for example, levy an initial contribution of 0.2% or 0.4% of subscribed solo capital from all member institutions. This would be a one-off assessment which would be in addition to the annual premium for the first year. Alternatively, there could be an up-front payment of the first two years' premiums, pre-paid by all member institutions. It would be open to the Bermuda Government to match any initial contribution from public funds.

6.3. Premiums

40. When deposit insurance systems are funded, premiums can be assessed either using a flat-rate system or a risk-based system. Under a flat-rate system, all insured institutions are assessed at a given rate per unit of deposits (such as total deposits, total insured deposits or total insurable deposits) or per unit of another measure (such as total assets, total risk-weighted assets or total liabilities) that reflects the coverage provided. A risk-based system, on the other hand, charges risk-adjusted premiums which vary according to proxies of the riskiness of the member institutions. While a risk-based system addresses moral hazard, identification of a proxy for risk presents challenges and difficulties. These include: finding appropriate and acceptable methods of differentiating institutional risk; obtaining reliable and appropriate data; ensuring the transparency of the approach; and examining the potential destabilising effects of imposing high premiums on already troubled banks.

Key Recommendation 8

For these reasons, it is proposed to start with a flat-rate system while providing the DIS with the option of transferring to a risk-based system at a future date once the Scheme is well-established.

6.4. Fund Size

41. In setting up a DIS from scratch, it is important to determine in advance a target size for the fund that the DIS would aim to reach over a number of years. A number of factors are relevant here. As a general rule, the fund needs to reach a certain minimum size to achieve and retain financial viability. This cannot be measured precisely but the target level should be adequate to cover potential claims under the DIS under stressed but plausible scenarios, including the failure of one or more banks. There are several factors that need to be taken into account when calculating an appropriate target for the size of the fund. These include: scope and coverage of the DIS; characteristics of the banking sector (number and size of banks); alternative financial resources available in the event of losses; the likelihood of failures; and general economic and financial market stability.

Key Recommendation 9

Given the inherent uncertainties involved in setting an appropriate target level for the fund, it is proposed that the DIS should establish a target range rather than a fixed target. Assuming the maximum amount covered is set at $25,000, using as a working assumption a definition of retail deposit that includes both non-resident and foreign currency deposits and drawing on advice from the IMF, it is proposed that the target fund for the DIS in Bermuda should be set at 2%-3% of total insurable deposits. Based on the latest available data, the target fund size would amount to $78 million - $117 million under this proposal (see Table 2 below).

6.5. Premium Rates

42. Premium rates should be set so as to be readily affordable by the banks and to enable the target fund to be reached within a reasonable time period. For the purposes of

this consultation, it is assumed that the DIS will want to reach its target fund level within roughly ten years.

Key Recommendation 10

To achieve this, it is recommended that, at a coverage level of $25,000, premium rates should be set within the range of 0.2%-0.3% of total insurable deposits. This would mean an annual premium somewhere between $7.8 million and $11.7 million.

43. Table 2 below provides further details. It also illustrates the significant extra cost should the threshold for coverage be set at $50,000 rather than $25,000. In that case, the target fund would need to be in the range of $156 million - $195 million and annual premiums would be of the order of $15.6 million - $19.5 million.

Table 2. Building the Target Fund

$25,000 coverage level	**2% of total insurable deposits**	**3% of total insurable deposits**
Fund target	$78 million	$117 million
Years to build target fund at 0.2% premium	10	15
Years to build target fund at 0.3% premium	7	10

$50,000 coverage level	**4% of total insurable deposits**	**5% of total insurable deposits**
Fund target	$156 million	$195 million
Years to build target fund at 0.4% premium	10	12.5
Years to build target fund at 0.5% premium	8	10

44. In calculating premiums due in any year, it is recommended that the BDIC base the levy for each institution on an average of insurable deposits for the preceding year.

45. Once the fund has reached its target size, the annual premium could be reduced to a lower level or waived altogether. It is also proposed that there be provision for the DIS

to pay a rebate or levy a surcharge should the balance of the DIS fund rise above a predetermined upper limit or fall below a predetermined lower limit.

7. Other Issues

7.1. Fund Investment

46. The money collected by the BDIC should be used only for:

(i) payment of legitimate claims from depositors;

(ii) payment of principal and interest on any borrowings;

(iii) purchase of allowable investments (see below); and

(iv) payment of administrative costs.

47. The funds collected by the BDIC are held in a fiduciary capacity for the public (depositors) in case of a bank failure. To reflect this trust, the investments should emphasise "safety and liquidity" over "return".

Key Recommendation 11

The BDIC shall invest the funds of the DIS only in debt securities issued or guaranteed by the home government, or those of foreign states, central banks, or public international financial institutions that are rated in one of the two highest categories by an internationally recognised rating agency.

7.2. Borrowing by the BDIC

Key Recommendation 12

It is proposed that the DIS will be able to access emergency borrowing through the Bermuda Government on a "fast-track" procedure, if there are not enough funds to compensate insured depositors in the event of a bank failure. The BDIC should have the power to levy a temporary surcharge on member banks to replenish the fund, such a surcharge not to exceed two times the amount of a bank's regular annual premium and not to exceed one year's duration.

7.3. Legal Issues

48. It is proposed that the DIS shall be provided with the power to seek legal redress against those parties at fault in a bank failure. These may include claims and litigations against directors, officers, auditors and other parties related to the bank failure. These claims may result in significant recoveries and serve as a tool for fostering discipline in the financial system.

49. The legislative framework for the DIS will specifically address such areas to include the resolution process, early detection and timely intervention, legal protection and the framework for reimbursing depositors and recoveries.

50. A draft bill is attached to this consultation paper.

7.4. Public Awareness

51. In order for deposit insurance to be effective, it is essential that the public is informed on an on going basis about the characteristics of the DIS. Public awareness is particularly important for newly established deposit insurance schemes.

52. The BDIC shall initiate an on going public awareness programme, which will disseminate information concerning important functions, benefits and limitations of the DIS and how it contributes to the health of the financial system. It is proposed that the BDIC shall require member institutions to display signs with the BDIC's logo and amount of coverage prominently, on all premises and advertising. Other elements of public awareness shall include dissemination of written brochures and pamphlets and working with the print and broadcast media. Additionally, it is recommended that the BDIC should maintain a website to provide information about the DIS' activities, financial statements, terms and conditions of deposit coverage and member institutions.

53. The BDIC shall coordinate its communications strategy with other safety net participants, especially during crisis events. The BDIC, BMA and MoF shall develop

strategies and plans, which shall be publicly communicated, to deal with potential financial or systemic crises in Bermuda.

8. Summary of Proposals

The main features of the DIS proposals are summarised below:

54. The DIS in Bermuda shall have a narrow mandate which would not duplicate the supervisory role of the Authority.

55. The DIS in Bermuda shall be mandatory for all four commercial banks and the one deposit company licensed under the Banks and Deposit Companies Act 1999. It is for consideration whether or not the credit union should be included.

56. The coverage amount of the DIS shall start at $25,000 on a per depositor and per institution basis. This figure should be reviewed periodically.

57. The DIS in Bermuda shall cover 'retail deposits' only, i.e. deposits owned by individuals, trusts, small businesses and charities.

58. The DIS in Bermuda shall cover both resident and non-resident eligible depositors.

59. The DIS in Bermuda shall include both local and foreign currency deposits.

60. The DIS in Bermuda shall be pre-funded and established from contributions from member institutions although the Bermuda Government may choose to make an initial contribution should it see fit.

61. The premium contribution shall start with a uniform flat rate system although the DIS will have the option to transfer to a risk-based system at a future date once the Scheme is well-established.

62. Regarding the target size of the fund, the DIS in Bermuda shall establish a target range rather than a fixed target. A target fund of 2%-3% of total insurable deposits is proposed to match the recommended coverage limit of $25,000. This equates to a fund size of $78 million-$117 million.

63. The DIS shall set a premium rate within 0.2%-0.3% of total insurable deposits.

64. The BDIC shall invest the funds of the DIS only in debt securities issued or guaranteed by the home government, or those of foreign states, central banks, or public international financial institutions that are rated in one of the two highest categories by an internationally recognised rating agency.

65. The DIS shall be able to access emergency borrowing through the Bermuda Government on a "fast-track" procedure, if there are not enough funds to compensate insured depositors in the event of a bank failure. The BDIC shall have the power to levy a temporary surcharge on member banks to replenish the fund, such a surcharge not to exceed two times the amount of a bank's regular annual premium and not to exceed one year's duration.