SNA/M1.12/2.5

7th Meeting of the Advisory Expert Group on National Accounts, 23-25 April 2012, New York

Agenda item : II
: Deposit insurance and financial stability schemes

Introduction

Several countries have operated deposit insurance schemes for many years, generally on deposits up to a certain monetary level (i.e. to protect 'retail deposits'). However in the wake of the recent financial crisis a number of schemes, with levies (on banks), have been introduced in a number of countries as a form of payment for deposit insurance services provided by government and also as instruments to manage financial stability. However the advent of these schemes raises a number of questions, chiefly concerning the distinction between taxes and services, where there appears to be significant differences in the treatment of similar schemes across countries in practice, and so a need for guidance (as seen in the annex which reflects country responses to a questionnaire produced by the OECD's Centre for Tax Policy and Administration (CTPA)).

Guidance on documentation provided

A document with on deposit insurance and financial stability schemes has been attached

Main issues to be discussed

The AEG is requested to consider the questions in part two of the attached paper.

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ISSUES PAPER: DEPOSIT INSURANCE AND FINANCIAL STABILITY SCHEMES

1. Introduction

1. Several countries have operated deposit insurance schemes for many years, generally on deposits up to a certain monetary level (i.e. to protect ‘retail deposits’). However in the wake of the recent financial crisis a number of schemes, with levies (on banks), have been introduced in a number of countries as a form of payment for deposit insurance services provided by government and also as instruments to manage financial stability.

2. However the advent of these schemes raises a number of questions, chiefly concerning the distinction between taxes and services, where there appears to be significant differences in the treatment of similar schemes across countries in practice, and so a need for guidance (as seen in the annex which reflects country responses to a questionnaire produced by the OECD’s Centre for Tax Policy and Administration (CTPA)).

3. The current draft of the new GFS Manual has attempted to provide some guidance in #5.66 but, as shown in the annex below, this general approach does not appear to be uniformly applied across countries:

> More specifically, the following types of fees are considered taxes: (a) fees where the payer of the levy is not the receiver of the benefit, such as a fee collected from slaughterhouses to finance a service provided to farmers; (b) fees where government is not providing a specific service in return for the levy even though a license may be issued to the payer, such as a hunting, fishing, or shooting license that is not accompanied by the right to use a specific area of government land; (c) fees where benefits are received only by those paying the fee but the benefits received by each individual are not necessarily in proportion to the payments, such as a milk marketing levy paid by dairy farmers and used to promote the consumption of milk; and (d) **fees paid to government for deposit insurance and other guarantee schemes if they are compulsory, that is, if beneficiaries cannot opt out of the scheme and the payment is clearly out of proportion to the service provided.**

4. Three categories of scheme, identified by CTPA appear to be of relevance and are referred to as A, B and C in the annex. These can be summarily described as follows:

Stability fee and deposit protection schemes; Payments are levied by governments on financial institutions to assist ailing financial institutions. The payments may or may not be hypothecated to a special fund that is administered to provide assistance only to institutions covered (and paying into) the scheme.

In practice there appears to be some difference in how these payments should be treated across countries. However, some agreement has become apparent in the case of payments made in the absence of a hypothecated fund. In these cases the consensus goes in the direction of treating the fees as taxes.

5. In cases where a dedicated fund exists however, some differences arise. For stability fees, the majority of countries consider that this should also be a tax. But some do not on the grounds that the institutions are paying for an insurance service provided by government, and, so, although the payments may be 'compulsory' they are not 'unrequited'. The treatment of the fees as payments for a service is also the majority position of countries in the case of deposit insurance schemes, where the ultimate beneficiaries are depositors.

Deposit protection schemes – recording of realised assets of failing/failed institutions.

6. Deposit protection schemes share some characteristics with stability fee/deposit insurance schemes but the key issue of interest concerns the priority claim and acquisition of assets by government to redistribute proceeds to depositors as part of its deposit guarantee. In some countries this acquisition is treated as a capital tax and in others the acquisition is treated as payment for a service.

2. Tax revenues or Fees

7. The AEG is asked to comment on the following proposals to improve international comparability

- Compulsory payments of stability fees, bank levies and deposit insurance should be treated as tax revenues where the payments are made to General Government and allocated to the governments' consolidated or general funds so that the Government is free to make immediate use of the money for the purposes that it chooses. This should apply regardless of whether the Government has a contingency to guarantee the banks' customer deposits.

- If the compulsory payments are made to general government and placed in dedicated funds in the Government sector, with the funds earmarked to be channelled back to paying companies if contingencies are called, they should still be treated as tax revenues, if the sums paid in over time exceed any reasonable estimate of expected payouts. In practice it may be simplest to always assume that this is the case. *This implies a difference compared to the draft guidance suggested in the new GFS which proposes to treat payments as taxes when they are <u>clearly out of proportion.</u>*

- If the compulsory payments are made to a fund managed by a public corporation the payments should be treated as fees, and treated as payments for insurance services, unless the payments are in excess of any expected payouts/contingencies, in which case the public corporation should be reclassified to the Government sector.

- Any payments which involve governments realising the assets of a failed institution or receiving a priority claim on its assets in liquidation in order to fund payments of compensation to customers for their lost deposits should be treated as a fee for a service as opposed to tax revenues, with the fee reflecting part of the difference between assets acquired and distributed by government. Any additional levy that may be imposed by government to make up any shortfall should be treated as a tax.

Compulsory payments that are made to funds operated outside the Government sector and all payments to voluntary schemes should not be treated as tax revenues.

8. The AEG is also asked to consider whether more detailed information concerning these schemes should be developed and included in the new GFS Manual, and not merely presented as a footnote within the current paragraph 5.66.

Annex I

CATEGORY A: STABILITY FEE SCHEMES

1. Austria

A new scheme took effect from 1 January 2011. A stability levy will paid by all entities classified as banks according to the Austrian Bank Act. The levy will be calculated as a percentage of a bank's balance sheet totals after subtracting secured deposits, equity and trust transactions. It will be structured progressively, with no payments for the first bracket up to € 1000 million, 0.055 per cent for the bracket up to € 20 000 million and 0.085 per cent for any amount exceeding this threshold. There will also be an additional levy on the trading volume of derivatives, amounting to 0.013 per cent of a bank's trading volume. The trading volume and balance sheet totals of 2010 will be used as the tax base for the levies paid between 2011 and 2013. These revenues will be paid to the general budget and there is no earmarking or financing of special funds.

At present, it is expected that these payments will be treated as tax revenue in both National Accounts and OECD Revenue Statistics.

2. France

A stability levy was introduced with effect from 1 January 2011. It is expected to raise 0.5 billion euros per year.

3. Germany

The German Federal Government has decided on 25 August 2010 on a draft bill for the introduction of a restructuring and liquidation regime for ailing banks. The introduction of a bank levy, with the proceeds being channelled into a special restructuring fund to be administered by the Federal Agency for Financial Market Stabilisation (Bundesanstalt für Finanzmarktsstablisisierung, FMSA) is part of this legislative proposal.

The levy will be paid by all credit institutions under German supervision and aims to charge the size and connectedness of a bank/credit institution. The base of the main component of the levy are an institution's liabilities, excluding equity capital and non-bank deposits (liabilities to clients), since these are fully insured in Germany. This base is charged with a progressive rate (0.02 percent until 10 billion €, 0.03 percent for amounts from 10-100 billion € and 0.04 percent for amounts above 100 billion €). In addition to this is a smaller component which charges the nominal value of derivatives held by an institution (on- and off- balance-sheet) with a rate of 0.00015 percent.

In Germany, the bank levy cannot be organised as a tax because of constitutional constraints – a payment obligation limited to a specific sub-group of taxpayers such as financial institutions, can not be levied as a general tax funding the general budget, but only as a special levy (Sonderabgabe) financing.

Such a levy has to meet certain requirements in order to pass a possible review by the Federal Constitutional Court, which can be initiated by individual complaint from anyone charged with the levy:

- The special levy has to serve a specific purpose going beyond the mere raising of general revenue.
- The subjects charged must belong to a homogeneous group, in this case financial institutions.
- The purpose, for which the levy is intended to be used, must fall mainly within the field of responsibility of the members of the group charged. In this case it is the restructuring fund which allows for the protection of financial stability in the restructuring of ailing systemic banks.
- The revenues raised by such a levy must be spent to serve interests of the group charged. According to the Constitutional Court, this precludes these revenues from flowing into the regular budget, but requires allocation to a special purpose fund, such as the planned restructuring fund.

As the bill is not yet in force, final decisions on the classification of the fees in National Accounts have yet to be made. According to the German statistical office (destatis) these fees will presumably be treated as tax revenue.

The bank levy has the same constructional characteristics as the waste water charge. As a result, the German Delegate would prefer to treat the revenue as a fee for service and not as tax revenue for the purposes of OECD Revenue Statistics.

4. Hungary

As from September 2010, financial corporations are obliged to pay surtax in Hungary. The tax assessment rules vary between institutions engaged in different activities. For example, banks and credit institutions must pay the surtax on the basis of the total amount of balance sheet (modified with some elements), and the applicable tax rate is 0.15 per cent up to HUF 50 billion and 0.5 per cent above that level. Insurance companies are obliged to pay on the basis of the amount of insurance premiums received at a rate of 6.2 per cent. These amounts paid provide proceeds for the central government for financing general budget purposes. The projected budget revenue from this new tax amounts to HUF 187 billion in 2010 - 0.7 per cent of GDP.

These payments will be treated as tax revenue in both National Accounts and OECD Revenue Statistics.

5. Sweden

The Swedish ‘Stability fee’ was introduced towards the end of 2009 with the aim of financing measures required to counteract the risk of serious disturbance to the financial system in Sweden. It is paid by banks and other credit institutions and is levied on all of an institution’s liabilities, excluding equity capital and some junior securities at a rate of 0.036%. The proceeds are to be channelled into a special stability fund to be administered by the Swedish Debt Office with a view to accumulating a fund equivalent to 2.5% of the gross domestic product in 15 years.

It has been decided that the Stability fee will be treated as a tax in the Swedish National Accounts.

Sweden would prefer to regard the payment as a fee for service and not a tax for the purposes of OECD Revenue Statistics on the grounds that the payments are entirely are channelled back to the sector of the economy where companies are subject to the payment. The stability fee is levied on all companies that are eligible for support in case of financial problems. The fee may thus be unrequited for an entity but for the sector as a whole it does finance a potential service.

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6. United Kingdom

A bank levy was introduced with effect from 1 January 2011. It applies to the consolidated balance sheet of UK banking groups and building societies; the aggregated subsidiary and branch balance sheets of foreign banks and banking groups operating in the UK; and the balance sheets of UK banks in non-banking groups.

The levy will be based on total liabilities, excluding Tier 1 capital; insured retail deposits; repos secured on sovereign debt; and policy holder liabilities of retail insurance business within banking groups.

The levy is set at 0.05 per cent from 1 January to 28 February 2011, 0.01 per cent from 1 March 2011 to 30 April 2011, 0.075 per cent from 1 May 2011 to 31 December 2011 and 0.078 per cent thereafter.

It is expected that the revenue will be treated as a tax in both the UK National Accounts and in OECD Revenue Statistics.

7. United States

Under the recently passed (July 2010) Financial Reform law, Federal government regulators will have the power to seize and dismantle troubled financial firms whose collapse might pull other companies down as well. Hence, there is a stabilization purpose. This resolution authority would be overseen by the Federal Deposit Insurance Corporation (FDIC). Taxpayers would pay for upfront costs, but regulators would then be required to recoup the money by levying fees on financial firms with more than $50 billion in assets.

No economic transactions related to this provision have yet occurred. Hence BEA has not yet had to record such a transaction in the National Income and Product Accounts (NIPAs) or in the System of National Accounts (SNA). It is likely that the relevant fee would be treated as a fee for a service and classified as a “current transfer receipt from business” in the NIPAs, because the financial industry would be receiving the benefit of financial stabilization. In the SNA, the corresponding line (in SNA Table 200) would be TRD7REC: “Other Current Transfers, Receivable.”

It is not expected that these fees will be treated as taxes in either National Accounts or OECD Revenue Statistics.

CATEGORY B: SCHEMES SIMILAR TO THE DEPOSIT PROTECTION SCHEME OPERATING IN THE UNITED KINGDOM

1. Australia

The Financial Claims Scheme (FCS) is a post-funded deposit protection scheme applying to deposits held in Australian-incorporated authorised deposit-taking institutions (ADIs). If an ADI becomes insolvent, the Australian Prudential Regulation Authority (APRA, the administrator of the FCS) will pay depositors the value of their deposits, up to $1 million per depositor, per ADI. The FCS is intended to be a permanent part of Australia's deposit protection framework, but the $1 million cap will be reviewed from 11 October 2011.

No up-front fee is charged for FCS protection. If an ADI becomes insolvent, APRA receives a priority claim on its assets in liquidation, for its payout and administrative costs. If there are insufficient assets, APRA may levy the ADI industry to make up the shortfall. The levy power is set out in an Act; to implement it, a regulation would be passed.

While no fees have been received to date, if the scheme were to be activated, it is likely that the revenues would be treated as follows:

- A priority claim on the ADI's assets in liquidation would be treated as a fee for service.
- A levy to cover any shortfall would be treated as a tax.

2. United Kingdom

In the UK, there is a deposit protection scheme operated by the Financial Services Compensation Scheme (FSCS) which is in the Central Government sector. It is responsible for compensating depositors with assets up to a certain threshold. Recently the Government has taken direct responsibility for any compensation of additional amounts above the threshold but there are no guarantees that it will do so in the future. During 2008 the UK undertook a number of financial sector interventions via FSCS whereby depositors were compensated for the loss of their deposits caused by the failure of certain financial institutions

The Scheme is not operated as a fund and therefore does not have a ready source of compensation to draw on when defaults occur. Its sources of income are as follows;

- An annual levy on banks and building societies to fund its operating costs (along with interest payments on debt).
- Realising the assets of failed institutions - when a financial institution is deemed to be in default, FSCS protection is triggered. In the short term the compensation payments to depositors are financed by borrowing but in time this borrowing is repaid as the assets of the failed institutions are realised. If the realisation of assets proves to be insufficient, then the FSCS will levy the other banks and building societies to meet the shortfall.

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The treatment of these transactions in the UK National Accounts is as follows:

- The levy covering the operating costs is recorded as a current tax on production on the banks and building societies and is included as a tax in the *Revenue Statistics*.

- The realisation of the assets of failed institutions to finance the compensation of depositors is recorded as a capital tax. Thus in National Accounting terms this income is recognised as a tax rather than a service as it is deemed to be providing services to depositors rather than the financial institutions that fund it.

In the UK public sector finances, the classification of the realisation of assets is different compared to that in National Accounts. In this environment, capital taxes have traditionally been recorded alongside current revenues, as from the perspective of government traditional capital taxes (such as Inheritance Tax) produce a regular income stream. This is not the case for the depositor compensation transactions and so these have been recorded in the capital account. The transactions are recorded as ‘capital transfers’ as opposed to tax revenues in order to offset the transfers to householders.

The UK Delegate also considers that there are other points that support the case for not treating this income stream as tax revenue in either the UK public sector finances or OECD *Revenue Statistics.*

- The transactions record situations where rights are transferred to government to cover payments paid to depositors of failing financial institutions. These are unusual transactions for a number of reasons. One is that taking into account that they offset the compensation payments that accrue at the same time; they have no positive net impact on government borrowing. In addition, they are only directed at specific institutions.

- Government will not receive a net profit from the taxes though in theory it could record a loss. The amounts from the realisation of assets that are recorded as tax revenues in National Accounts will not be greater than the corresponding amounts paid to depositors in compensation. The same is the case in respect of any additional compensation over and above the FSCS limits that is made directly by the government.

CATEGORY C: OTHER GOVERNMENT SECTOR DEPOSIT PROTECTION SCHEMES

1. Australia

The Guarantee Scheme for Large Deposits and Wholesale Funding (‘Guarantee Scheme’) covers Australian-incorporated authorised deposit-taking institutions’ (ADIs) eligible wholesale funding instruments and the portions of large deposits held in them (over $1 million per depositor, per ADI). Under the Guarantee Scheme, ADIs pay a fee, based on their credit rating, of between 70 bps and 150 bps for coverage. The fee is paid into the Consolidated Revenue Fund. The Guarantee Scheme closed to new liabilities on 31 March 2010. Existing liabilities are covered until maturity (the maximum maturity is five years), or until October 2015 for large deposits.

The National Accounts classifies these payments as fee for a service. The payments are not classified as taxes in either National Accounts or OECD Revenue Statistics.

2. Belgium

At the end of 2008, the cover offered to deposit holders under the existing **Protection Fund** was raised from 20,000 to 100,000 euro, and insurance companies were offered, on a voluntary basis, the opportunity to guarantee class 21 life insurance products in a similar way. For this purpose, the government set up the **Special Protection Fund** for deposits and life insurances. This new Fund was intended to cover class 21 life insurance products, and the 50,000 to 100,000 euro tranche of deposits with credit institutions, the first tranche of 0 to 50,000 euro being covered by the existing Protection Fund. The cover provided by the investor protection scheme remained fixed at 20,000 euro per person and per institution.

From January 2011 onwards, the responsibilities of the Special Protection Fund will increase substantially. First; the participation of the insurance companies issuing class 21 life insurance products will become compulsory. Second, the covering of deposits by the Protection Fund will partly be shifted to the Special Protection Fund. In case of default of a financial institution, the covering of the first tranche of 50,000 of deposits by the Protection Fund will be lowered to only its “available means” after settlement of the claims of financial instrument investors; the remaining (up to 100,000) being covered by the Special Protection Fund. This shift of responsibilities is accompanied by a change (increase) in the fee structures.

The federal Treasury has to pre-finance compensations to depositors and investors if the cost of interventions exceeds the available funding. Then in subsequent years, a proportion of the payments made by contributing institutions will be allocated to paying back this pre-financing.

The Special Protection Fund is administered by the federal Treasury. It is classified as belonging to the federal government sector in the national accounts (ESA95 S.1311) which classifies these payments as fee for a service. The payments are not classified as taxes in either National Accounts or OECD Revenue Statistics.

3. Canada

In Canada there is the federally controlled crown corporation, Canada Deposit Insurance Corporation (CDIC), and as well as two provincial government corporations, the Deposit Insurance Corporation of Ontario and the Credit Union Deposit Guarantee Corporation of Alberta, that collect insurance premium revenue from financial corporations to insure deposits made in the financial corporations.

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CDIC is a federal Crown corporation created by Parliament. It works at arm's length from the government and reports to Parliament through the federal Minister of Finance. It was created to insure deposits held in CDIC member banks, trust companies, loan companies and associations governed by the Cooperative Credit Associations Act. Its work is governed by the CDIC Act.

(CDIC) insures eligible deposits at each CDIC member institution up to a maximum of $100,000 (principal and interest combined) **per depositor** (or, in the case of joint deposits, **per set of joint owners**), for each of various different types of accounts. To be eligible for deposit insurance, deposits must be payable in Canada, and in Canadian currency. As a general rule, a deposit is considered to be payable in Canada if it is held at a branch or office of a CDIC member institution in Canada.

Each year, every member institution is classified into one of four premium categories. Except under special circumstances, classification is based on a system that scores a member institution according to a number of factors including capital adequacy, profitability, asset quality and concentration.

At present, insurance premiums paid by financial corporations to federal and provincial deposit insurance plans are classified as taxes in both National Accounts and OECD Revenue Statistics.

4. Denmark

To ensure trust in the Danish financial sector, a political agreement was formed in October 2008. Through the Bank Package the Danish State issued a general two-year guarantee for deposits and simple claims in all Danish financial institutions who are members of the Private Contingency Association (Det Private Beredskab). This covers 99 per cent of the financial sector.

The Bank Package established the Financial Stability Company (Finansiel Stabilitet A/S) to ensure the coverage of the unsecured creditors' claims in case a bank becomes financially distressed. The Company is responsible for ensuring the timely payment of all due claims of unsecured creditors and depositors and also to take over the liabilities of distressed financial institutions. The Company is state-owned through the Danish Ministry of Economic and Business Affairs.

To benefit from the state guarantees of the Bank Package each financial institution involved pays a fee according to their relative size. In total the financial institutions pay a 15 billion DKK fee to the state. Furthermore, the participants guarantee 20 billion DKK to cover any potential loss in relation to the liquidation of financial institutions in distress. Thus, the total fee paid by the financial sector depends on the amount of losses from distressed members of the Private Contingency Association but amounts to between 15 and 35 billion DKK. Any additional liabilities were to be covered by the Danish State.

When the unlimited deposits guarantee of the Bank Package expired at the end of September 2010, deposits are covered by The Depositors' Guarantee Fund from October 1st 2010 and onwards (see Annex D).

The premium paid by the financial institutions for the two year coverage is actually neither a tax nor a payment for service. Instead this insurance premium is classified as a capital transfer to the Financial Stability Company and thus not part of public administration in the National Accounts.

5. Germany

There are two mandatory Deposit Guarantee Schemes that insure especially deposits of private persons and small & medium enterprises up to 50,000 € according to EU-Directive 94/9/EC. There are also several voluntary schemes operated by banks.

These payments are classified as fee for a service. The payments are not classified as taxes in either National Accounts or OECD Revenue Statistics.

6. United States

There is an already existing program of deposit insurance, including fees paid by banks, that is administered by the Federal Deposit Insurance Corporation (FDIC). In response to the 2008-09 financial crises, the Federal government instituted:

- a one-time special assessment on banks for deposit insurance
- prepayments of FDIC fees

These payments are classified as fee for a service in National Accounts. The payments are not classified as taxes in either National Accounts or OECD Revenue Statistics.