

1. Key Features of the Deposit Protection Agency Act

Feature	Deposit Protection Agency Act
1. Objectives , powers and responsibilities	<p><u>Objectives</u></p> <ul style="list-style-type: none"> (1) to provide protection for deposits in insured financial institutions, (2) to maintain confidence and stability in the financial system, (3) to manage insured financial institutions under control according to the Financial Institution Act and to liquidate insured financial institutions whose licenses have been revoked. <p><u>Powers & Responsibilities</u></p> <ul style="list-style-type: none"> (1) to manage the Deposit Protection Agency (DPA) fund, capital and assets (2) to collect premiums from insured financial institutions, make compensation to depositors (3) to hold rights in assets and engage in any contracts (4) to issue financial notes, bonds and other financial instruments (5) to invest in government bonds or other debt instruments guaranteed by the government or other securities according to the permission of the DPA Board and approval from the Minister (6) to deposit money in financial institutions, the Bank of Thailand or specialized financial institutions for its normal business purposes or according to the permission of the DPA Board. (7) to execute any other related task.
2. Organization	<p>- A juristic person.</p>
3. Initial Capital	<p>- Not to exceed 1 billion Baht to be provided by the government.</p>

4. Management Structure	<ul style="list-style-type: none"> - Governed by the DPA Board comprising a chairman, a representative from the Bank of Thailand, a representative from the Ministry of Finance (MOF), and 3-5 other qualified persons (at least 2 of which should be specialized in Finance and Law). - Director of the Institution shall be an ex officio Board member and secretary of the Board. - Board members have a four-year term and members may be reappointed not exceeding two consecutive terms - The Minister shall nominate candidates for the Chairmanship of the DPA and 3-5 qualified members with approval from the Cabinet.
5. Premium	<ul style="list-style-type: none"> - The maximum annual premium rate shall not exceed 1% of the average total deposits of the insured institution. The rate will be announced in the Royal Decree. - A flat rate premium will be applied initially and differential premium system may be applied in the future.
6. Coverage and Insured Deposits	<ul style="list-style-type: none"> - Deposits and accrued interest denominated in Thai Baht accounts and shall not exceed 1 million Baht per depositor per institution. - Excluding “Non-resident Baht accounts” which are accounts open for specific purposes according to the Exchange Control Act.
7. Membership	<ul style="list-style-type: none"> - Compulsory for all insured institutions. - Insured institutions to include: commercial banks, financial institutions and credit foncier companies including foreign bank branches in the country. - Financial institutions established under special laws and which accept deposits from the public can be included in the scheme by issuing a Royal Decree.
8. Reimbursement to depositors	<ul style="list-style-type: none"> - Reimbursement of insured deposits shall be made within 30 days after receiving insurance claims from depositors.
9. Follow up on the performance and condition of financial institutions	<ul style="list-style-type: none"> - The DPA to be granted access to examination reports from the Bank of Thailand, may share any relevant information and may directly request financial institutions to submit information. - The DPA may request the Bank of Thailand or other regulating authorities to conduct an on-site examination on certain issues where there is a suspicion that the condition or operation of that insured financial institution may cause damage to the public interest,

	and DPA may accompany the Bank of Thailand or other regulating authorities in the examination.
10. Resolution and Control Committee (Role of the DPA during intervention in an insured financial)	<ul style="list-style-type: none"> - When the Bank of Thailand issues an order to intervene in an insured financial institution, the DPA shall propose a name list of person(s) to the Bank of Thailand to be appointed as a committee(s) in the Control Committee. - The Control Committee shall take over the operation and run the intervened financial institution according to the Financial Institution Act.
11. Liquidation	<ul style="list-style-type: none"> - DPA shall be appointed as a liquidator and be responsible for paying compensation to depositors. - the liquidator shall sell assets and collect all debts - the liquidator shall pay the DPA back the amount paid to depositors - the liquidator may pay other creditors if it receives consent from creditors - the liquidator shall file a request for a court order to liquidate the failed financial institution. When a court order is issued for the absolute and immediate control over debtor's properties, the liquidator shall transfer money, properties and all documents to the appointed official receiver and the DPA shall be relieved from all powers and duties as liquidator onwards. Further liquidation process shall be in accordance with the law on bankruptcy.
12. Transition from blanket guarantee	<p>The blanket guarantee shall be gradually phased-out to limited coverage of 1 million Baht within 4 years as follows :</p> <p>1st year : full amount of deposit (11 Aug 2008 – 10 Aug 2009) 2nd year : full amount of deposit (11 Aug 2009 – 10 Aug 2010) 3rd year : full amount of deposit (11 Aug 2010 – 10 Aug 2011) 4th year : 50 million Baht (11 Aug 2011 – 10 Aug 2012) 5th year : 1 million Baht (11 Aug 2012 onwards)</p>

2. Bank run

From Wikipedia, the free encyclopedia

A **bank run** (also known as a **run on the bank**) occurs in a [fractional reserve banking](#) system when a large number of customers withdraw their [deposits](#) from a financial institution at the same time and either demand cash or transfer those funds into government bonds or [precious metals](#) or a safer institution because they believe that the financial institution is, or might become, [insolvent](#). As a bank run progresses, it generates its own momentum, in a kind of [self-fulfilling prophecy](#) (or [positive feedback](#) loop) – as more people withdraw their deposits, the likelihood of default increases, thus triggering further withdrawals. This can destabilize the bank to the point where it runs out of cash and thus faces sudden [bankruptcy](#).

A **banking panic** or **bank panic** is a [financial crisis](#) that occurs when many banks suffer runs at the same time, as people suddenly try to convert their threatened deposits into cash or try to get out of their domestic banking system altogether. A **systemic banking crisis** is one where all or almost all of the banking capital in a country is wiped out. The resulting chain of bankruptcies can cause a long [economic recession](#) as domestic businesses and consumers are starved of capital as the domestic banking system shuts down.^[3] Much of the [Great Depression](#)'s economic damage was caused directly by bank runs. The cost of cleaning up a systemic banking crisis can be huge, with fiscal costs averaging 13% of [GDP](#) and economic output losses averaging 20% of GDP for important crises from 1970 to 2007.^[2]

Several techniques have been used to try to prevent or mitigate the effects of bank runs. They have included government [bailouts](#) of banks, [supervision and regulation](#) of commercial banks, the organization of [central banks](#) that act as a [lender of last resort](#), the protection of [deposit insurance](#) systems such as the U.S. [Federal Deposit Insurance Corporation](#),^[1] and after a run has started, a temporary suspension of withdrawals.^[5] These techniques do not always work: for example, even with deposit insurance, depositors may still be motivated by beliefs they may lack immediate access to deposits during bank reorganization.

Bank runs first appeared as part of [cycles of credit expansion](#) and its subsequent contraction. In the 16th century onwards, English goldsmiths issuing promissory notes suffered severe failures due to bad harvests, plummeting parts of the country into famine and unrest. Other examples are the Dutch [Tulip manias](#) (1634–1637), the British [South Sea Bubble \(1717–1719\)](#), the French [Mississippi Company](#) (1717–1720), the post-Napoleonic depression (1815–1830) and the [Great Depression](#) (1929–1939).

History

Bank runs have also been used to blackmail individuals or governments. In 1832, for example, the British government under [the Duke of Wellington](#) overturned a majority government on the orders of the king, [George IV](#), to prevent reform (the later [1832 Reform Act](#)). Wellesley's actions angered reformers, and they threatened a run on the banks under the rallying cry "*Stop the Duke, go for gold!*".

Many of the [recessions in the United States](#) were caused by banking panics. The Great Depression contained several banking crises consisting of runs on multiple banks from 1929 to 1933; some of these were specific to regions of the U.S.^[3] Banking panics began in October 1930, one year after the stock market crash, triggered by the collapse of correspondent networks; the bank runs became worse after financial conglomerates in New York and Los Angeles failed in prominently-covered scandals.^[7] Much of the Depression's economic damage was caused directly by bank runs,^[4] and institutions put into place after the Depression have prevented runs on U.S. commercial banks since the 1930s,^[8] even under conditions such as the [U.S. savings and loan crisis of the 1980s and 1990s](#).^[9] The Depression's bank runs left a lasting mark on the American psyche, exhibited in sometimes disturbing images such as the bleak scenes in the movie [It's a Wonderful Life](#),^[10] where the fictional hero [George Bailey](#) struggles to keep his Building & Loan open with a crowd of customers demanding their deposits.

The [global financial crisis that began in 2007](#) was centered around market-liquidity failures that were comparable to a bank run. The crisis contained a wave of bank nationalizations, including those associated with [Northern Rock](#) of the UK and [IndyMac](#) of the U.S. This crisis was caused by low real interest rates stimulating an asset price bubble fuelled by new financial products that were not stress tested and that failed in the downturn.

3. Too big to fail

From Wikipedia, the free encyclopedia

The "too big to fail" theory asserts that certain financial institutions are so large and so interconnected that their failure would be disastrous to the economy, and they therefore must be supported by government when they face difficulty. The colloquial term "too big to fail" was popularized by U.S. Congressman Stewart McKinney in a 1984 Congressional hearing, discussing the Federal Deposit Insurance Corporation's intervention with Continental Illinois. The term had previously been used occasionally in the press.

Proponents of this theory believe that some institutions are so important that they should become recipients of beneficial financial and economic policies from governments or central banks. Some economists such as Paul Krugman hold that economies of scale in banks and in other businesses are worth preserving, so long as they are well regulated in proportion to their economic clout, and therefore that "too big to fail" status can be acceptable. The global economic system must also deal with sovereign states being too big to fail.

Opponents believe that one of the problems that arises is moral hazard whereby a company that benefits from these protective policies will seek to profit by it, deliberately taking positions (see Asset allocation) that are high-risk high-return, as they are able to leverage these risks based on the policy preference they receive. The term has emerged as prominent in public discourse since the 2007–2010 global financial crisis. Critics see the policy as counterproductive and that large banks or other institutions should be left to fail if their risk management is not effective. Some critics, such as Alan Greenspan, believe that such large organizations should be deliberately broken up: "If they're too big to fail, they're too big". More than fifty prominent economists, financial experts, bankers, finance industry groups, and banks themselves have called for breaking up large banks into smaller institutions.

On March 6, 2013, United States Attorney General Eric Holder told the Senate Judiciary Committee that the Justice Department faces difficulty charging large banks with crimes because of the risk to the economy. Four days later, Federal Reserve Bank of Dallas President Richard W. Fisher wrote in advance of a speech to the Conservative Political Action Conference that large banks should be broken up into smaller banks, and both Federal Deposit Insurance and Federal Reserve discount window access should end for large banks. Other conservatives including Thomas Hoenig, Ed Prescott, Glenn Hubbard, and David Vitter also

advocated breaking up the largest banks.

On April 10, 2013, International Monetary Fund Managing Director Christine Lagarde told the Economic Club of New York "too big to fail" banks had become "more dangerous than ever" and needed to be controlled with "comprehensive and clear regulation [and] more intensive and intrusive supervision.

Moreover, the decision to bailout large institutions does not seem a sustainable solution. It does not fix the causes; it addresses the consequences. The interesting point is that authorities have not realized that institutions that were at the center of the crisis, namely JP Morgan Chase, Bank of America, Wells Fargo and Citigroup, have become "even bigger", representing what one Democratic socialist politician, Rep. Bernie Sanders, called "the four largest banks in America. Thereby, the question that the Government should think about is: If one of these banks tends to fail, will we have the capacity to save it? The problem will certainly reach a point where it will be impossible for authorities to handle. Hence, a more sustainable method should be explored as well, such as letting the banks fail, with free market correction as the recovery.

Thus, Willem Buiters proposes a tax to internalize the massive external costs inflicted by "too big to fail" institution. "When size creates externalities, do what you would do with any negative externality: tax it. The other way to limit size is to tax size. This can be done through capital requirements that are progressive in the size of the business (as measured by value added, the size of the balance sheet or some other metric). Such measures for preventing the New Darwinism of the survival of the fittest and the politically best connected should be distinguished from regulatory interventions based on the narrow leverage ratio aimed at regulating risk (regardless of size, except for a de minimis lower limit).

4. Who's afraid of Basel III?

By: Dr. Sutapa Amornvivat

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I am certainly worried. And you should too, because starting January 2013, tougher banking rules called "Basel III" are expected to take effect. But why should we care? After all, Thailand is not a member of the Basel Committee, and aren't these rules supposed to have an impact on just banking operations, anyway?

Yes, Thai regulator does not need to adopt Basel III, but it can choose to do so, as with Basel I and II. Indeed, the Bank of Thailand adopted the previous Basel rules to upgrade bank risk management practices to par with international standards. Therefore, in the short-term, it is the banking sector that will take the most hit from strict supervision. And the markets know this; when the Indian banking regulator announced last May they will embrace the new rules, followed by the Chinese regulator just last week, their banking stocks immediately tumbled. But what about the long-term impact? It may come as a surprise but it is actually a lot closer to your business well-being than you may think. The long-term impact is in fact twofold which will become clear momentarily.

But first, let's start with what exactly is Basel III.

Similar to the first two, this third installment requires banks to hold higher levels of quality capital (e.g. retained earnings and common shares) in order to sustain unexpected loss in market downturn. Banks running short on capital can boost it up either by lowering dividend payout or by raising funds in the capital markets. But unlike in Basel I and II, banks are now asked to hold capital cushion called "buffers" as a safeguard from the repeat of Lehman Brothers' collapse. Beyond that, Basel III introduces new features called liquidity and leverage tests. These new tests are there to make sure banks are not stressing their balance sheets with loans and investments without having adequate deposits and capital, technically preventing banks from biting off more than they can chew.

The combination of old and new features implies that banks have to start withdrawing their investments in "non-core" markets-usually overseas emerging markets like Thailand-to focus more on home or "core" markets, in order to save their capital and lower the leverage level. This is also called "deleveraging." They could do so by adopting a "ring-fencing" business model whereby operations in those non-core markets will be run on a different balance sheet. This shift in business

models would create certain level of shocks on the Thai economy from the drying up of external funding. To make matters worse, **long-term investments to finance large bulky projects will turn up on the wrong side of the Basel banking law because they are not so easy to liquidate in the event of loss.** As a result, we could further see gradual retreat of institutional funds that were originally devoted to infrastructure investment in the country. This is bad news for Thais because we simply need foreign money to facilitate infrastructure development which is one of the great catalysts for economic growth at our stage.

Perhaps the most profound effect of foreign fund retractions will be on the development of Thai capital market. Financial institutions have long been among the top investors in the Thai debt market, helping to generate liquidity and stability. So, it gets complicated when Basel III has decided to penalize corporate bonds rated below A-, again for being illiquid assets. Banks in trouble to comply with Basel liquidity tests will be scrambling to unwind their positions in poorly-rated bonds, typically found in emerging markets. The result is: illiquid markets will continue to be illiquid without adequate international investment funds. Similarly for Thailand, efforts to build a deeper, more liquid and less volatile debt market could prove to be futile.

And that is only a story half-told. What has just been described can be categorized as the indirect effect of Basel III implementation in other countries. Now that we have that covered, let's talk about the direct impact of the Bank of Thailand's plan to adopt Basel III as soon as next year.

First of all, simultaneous adoption is aggressive. Even the US has decided to delay implementation. In the past, the Bank of Thailand was careful not to adopt the first two Basel rules right away. This time it may seem to the Thai regulator that the status quo will weather the harsher regulatory reforms. And it is true; it may have taken a painful lesson from the 1997 Asian Financial Crisis but Thai banks are now fundamentally stronger, overcapitalized and underleveraged. The impact of Basel III on the Thai banking operations is likely small, especially compared to the true economic cost that will travel beyond the banking sector in the long run.

Indeed, because bank loans in Thailand still make up the majority of corporate financing, **banks' limited capital will certainly hurt business expansions.** On the back of harsher capital rules, banks will begin to brace themselves. Customer profiles will be subject to scrutiny for risk-return balance. With capital becoming scarce, expect the rise in cost of financing to be pre-emptively passed through to bank customers. Infrastructure projects will be under added pressure; not only are foreign funds withdrawing due to deleveraging as mentioned before, but loans from domestic banks will also be a bit harder to come by if Basel III is adopted in Thailand. Under this scenario, it is difficult to imagine how the banking system could reach the required rate of credit growth to support economic development.

Trade finance is another area of concern. Among bank financing products, SMEs who are involved in trading business prefer a type of working capital financing called "letter of credit" or L/C. With this L/C document, small businesses will be assured to pursue overseas trades because risks in international payments are shifted to the issuing banks who will guarantee payments. The risks on banks are small, too. On average, the chance of L/C going default is lesser than normal loans because it is short term in nature and the source of funds to be settled on the due date is known, or "self-liquidating".

The bad news is: Basel does not think so. In the context of leverage level, the rules ask that banks apply the full guaranteed amount on L/C, instead of only its risk-adjusted amount as was the norm in the past rules. This could force smaller banks to put a wrap on trade financing business altogether, as it is already low-margin. So how can SMEs finance its trade cheaply? **This is discouraging for an economy like Thailand which depends on the well-being of its international trade and SMEs. As a side effect, we could see renewed popularity of shadow banking system that offers similar guarantee for SMEs to satisfy trading needs but is otherwise unregulated.**

Perhaps we must ask ourselves this: by fully and hastily adopting Basel III are we unnecessarily importing problems from the West, while in the process putting the good health of the economy at risk? We cannot escape the indirect impact of Basel III adoption in other countries, but we can certainly choose the right regulatory path and timeframe that do not interfere with national efforts for growth. Indeed, there is an effort from banks across Asia to call for delay in implementation until nation-specific rules can be established to match the distinct national circumstances and requirements. For Thailand, infrastructure development is still imperative; while international trade and SMEs are still Thai economy's lifeline that needs support, not control. We could do without these new liquidity and leverage rules that discourage those that are vital to us, particularly when the Thai version of capital rules have been a bit tougher than required since Basel I.