Fact sheet

Protection of bank deposits

When a bank faces insolvency and must file for bankruptcy, clients are bound to become anxious about the security of their savings. In Switzerland, clients' deposits are protected by both the depositor protection scheme and preferential treatment granted in the event of bankruptcy. This reduces the risk of losses suffered.

Protecting depositors has two objectives: on the one hand, they should be protected from suffering losses. Clients must be guaranteed a source of income if 'their' bank goes bankrupt. On the other hand, depositor protection enhances systemic stability by preventing bank runs and reducing contagion during a banking crisis. In Switzerland, deposits totalling CHF 100,000 per client are regarded as preferential deposits. Deposits held by a Swiss branch of a Swiss bank are protected by the depositor protection scheme.

Three-tiered system: bank – depositor protection scheme – bankruptcy assets

Explained simply, depositor protection in Switzerland is based on a three-tiered system. As a first step, preferential deposits are immediately paid out from the remaining liquidity of the failed bank. If the institution's liquidity does not suffice to cover all the preferential bank deposits, the depositor protection scheme is used as a second step to pay out preferential deposits, provided that they were booked in Switzerland. All banks in Switzerland that accept client deposits are obliged to participate in the depositor protection scheme. And as a third step, deposits that belong to the bankruptcy assets are treated preferentially, i.e. in the event of bankruptcy, those deposits are paid out as second creditor class claims.

Unlike cash deposits in bank accounts, assets in custodial accounts such as shares, units in collective investment schemes and other securities are client property, and in the event of bankruptcy, all such assets are immediately ring-fenced and then released to clients.

How depositor protection works

When a bank goes bankrupt, preferential bank deposits are paid out immediately from the remaining liquidity available. In certain cases, FINMA determines the maximum amount; the largest possible number of retail investors has thus been paid out before bankruptcy proceedings are instituted. If the amount of liquidity available to cover the preferential bank deposits does not suffice, the depositor protection scheme comes into play. Once FINMA initiates bankruptcy proceedings, it notifies the depositor protection scheme agency and informs it about the liquidity required to pay out the protected deposits. The funds required are provided collectively (maximum amount CHF 6 billion) to FINMA or the restructuring agent by the other members of the Depositor Protection Association within a period of 20 days. The association members must keep half of the

Level 1	Level 2	Level 3
Preferential deposits (CHF 100,000 per client) are immediately paid out in and outside Switzerland	Depositor protection scheme for preferential deposits (CHF 100,000 per client) in Switzerland	Bankruptcy privilege for bank and retirement savings (CHF 100,000 per client) in and outside Switzerland

amount that they are obliged to contribute as additional liquidity. All preferential deposits that are fully paid out at the latest during bankruptcy proceedings are also secured by underpinning them with domestically held assets which FINMA can easily access.

Other separate privileged arrangements apply to deposits with employee benefits and vested benefits foundations, in particular vested benefits accounts and pillar 3a pension funds, up to a maximum of CHF 100,000 per client. Those deposits are not part of the depositor protection scheme and are only paid out during the bankruptcy proceedings instituted over the pension fund. In the event of bankruptcy, client deposits of over CHF 100,000 per client are regarded as third creditor class claims and are treated equally with the claims of other creditors.

Bankruptcy privilege: In the event of bankruptcy, preferential deposits are allocated to second creditor class claims and are paid out immediately from the bankruptcy assets once first-class claims (employee salary and pension fund claims) have been paid out. Thus, there is a strong likelihood that second creditor class claims will be paid out in full.

The depositor protection system is used only in the event of bankruptcy. The measures described above should not be confused with bank resolution which takes place at an earlier stage. When a bank is being restructured, preferential deposits cannot be compulsorily converted into equity capital, nor is it possible to enforce a waiver of claims as is the case for other debt capital.

Origin and reform of depositor protection

Switzerland has had a depositor protection scheme and preferentially treated deposits in the event of bankruptcy since the 1930s. However, since there were hardly any bank insolvencies in the post-war period up to the beginning of the 1990s, this system has rarely been used.

The lessons learned from the bankruptcy of the Spar- und Leihkasse Thun at the beginning of the 1990s resulted in a substantial revision and strengthening of the protection of Swiss depositors. The definition and scope of preferential deposits were expanded. The depositor protection system is based on self-regulation. In 2005, the Swiss Banks' and Securities Dealers' Depositor Protection Association was formed. Its self-regulatory measures are subject to FINMA's approval.

Information on the depositor protection scheme, e.g. what is meant by preferential and protected deposits, can be found on the Deposit Protection homepage: www.esisuisse.ch.

Some years later the financial crisis demanded further reform. This urgent revision comprises five core elements: firstly, the maximum amount for preferential deposits per client and bank was increased from originally CHF 30,000 to CHF 100,000; secondly, banks are obliged to hold domestic assets of up to 125% of their preferential deposits in order to ensure that there are enough assets in Switzerland to meet clients' claims; thirdly, immediate payment from the funds available is now more generous and flexible; fourthly, the upper limit of the depositor protection scheme was raised from originally four to currently six billion Swiss francs, and, finally, fifthly, deposits at pension fund foundations are separated and, in addition to protected bank deposits which also amount to CHF 100,000, are treated preferentially in the case of bankruptcy. These immediate measures were introduced in 2008 at the height of the most recent financial crisis and are subject to review. In 2011, Parliament adopted these measures practically unchanged in standard law.

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Swiss Financial Market Supervisory Authority FINMA
Einsteinstrasse 2
CH-3003 Bern
Tel. +41 (0)31 327 91 00
Fax +41 (0)31 327 91 01
info@finma.ch
www.finma.ch