

SUMMARY¹
of the Experience and Lessons Learnt from the Payout Case of
“Jógazda” Savings Co-operative Bank
(“White Paper”)

The first NDIF payout case in January 2011 of „Jógazda” Savings Co-operative Bank has been the first operation since the 20-working day payout regime was adopted in early 2010 that involved a sizable amount (HUF 9,1 billion, cca. EUR 35 million) and number of depositors (5329 persons).

The NDIF completed the payout within the deadline specified by law, despite the fact that the IT preparations that provided the basis of the reimbursement (processing the saved data file, and customer consolidation) took longer than expected or the given timeframe that has been envisaged for (please, see the attached flowchart).

A key lesson learnt from the case is that the largest risk of feasibility of the payout (*deposit insurance risk*) – particularly in the event of high volumes – lies in the shortcomings of the IT and quality of data. For this reason, a solution is to be found for a more efficient on-site audit of credit institutions. A key consideration for audit activities should be to explore the anomalies hidden in deposit registers (and the resulting deposit insurance risks) and preferably eliminate them prior to closing. Registration risks not only slow down individual indemnification but may also represent an overall hazard to a legislation-based promise of fast-payout. This is why when the authenticity of fast-payout is at stake, deposit insurance is unable to fulfil its high priority role of reinforcing confidence in banks and financial stability in general.

Fast-payout is closely related also to the consumer protection service provided by the NDIF, and, ultimately, to reinforcing depositors’ trust, this is why active communication with the public in cooperation with the partner organisations is necessary is of utmost importance.

The payout implemented on account of “Jógazda” with a market share of tens of per mill, consumed one tenth of the NDIF’s total assets. This amount corresponds to close to 4 years’ deposit insurance premiums paid by the whole banking sector (in 2010, the member institutions paid HUF 2.4 billion in NDIF premiums in total).

The *Post-Payout Customer Satisfaction Survey* administered for the first time in the history of NDIF indemnifications shows that the basic rules of deposit insurance in terms of the coverage limit of 100.000 euro and the payout timeline are both welcome by and acceptable for consumers, and the NDIF was able to conclude the case by reinforcing public confidence.

1) Summary of lessons learnt

Inter-institutional

- It was confirmed by the case that early notification by the Supervision concerning the expected role of the NDIF is of high significance in terms of preparatory works for the payout in order to be able to comply with the 20-working day period.

¹ The English Summary is an extract from the detailed Hungarian version.

- The complexity of the on-site audit carried out by the Supervision makes it hardly possible to draw useful conclusions concerning the condition of the credit institution's deposit source data from the aspect of fast-payout by the NDIF.
- The case of "Jógazda" shed light on the necessity of continuous and close coordination among institutions not only prior to the payout but also under the post-closure phase, in order to avoid the risks resulting from unexpected situations in a sensitive crisis period. An example is the case of an agreement concluded by the failed bank with a neighbouring savings co-operative (Forró és Vidéke Takarékszövetkezet) that rented out the branches of "Jógazda" as early as during the indemnification period, with the approval of the liquidator. This mere fact could have endanger the smooth payout by disruption in servicing the customers of the failed bank under liquidation on behalf of NDIF.
- In cooperation with the Supervision, the NDIF is to strictly require full availability of the documents related to deposit taking business with the credit institution on an on-going basis.

IT

- It may cause significant operating risks, and may even seriously hazard timely payout when a bankrupt bank or a partner thereof fails to deliver to the Fund the compiler (interface) program indispensable for reading the data, or sets an unjustifiably high price for producing it.
- It was proved again that the credit institutions are to pay considerable amount of attention to keeping the deposit and depositor register (Single Customer View record) up to date, and require regular data cleaning – even through prospective supervisory sanctions, if necessary.
- The audit functions incorporated in KIR in 2002 retain their significance, such as checking out ownership structure and logical compliance of deposits.
- A significant number of complaints have been received about funds transfers to account numbers specified by customers, because the credit amount was not received on the specified account. It was mostly caused by mistakes made by the data entry staff hired by the NDIF on keying in account numbers, as
 - the customer's name was not entered with the account number, and
 - a control data entry was omitted.

Lessons of the payout

- Data submission by customers (bank account number, changes in data) can only be accepted if the respective original copies countersigned by the supervisory commissioner or the liquidator have been received by NDIF. No option should be granted or made available in the future to submit data by fax.
- On auditing, it should be required that the data of uninsured depositors pursuant to section 100 (2) of the Act on Credit Institutions and Financial Enterprises (auditor, senior officials and their respective next of kin living in the same household) are recorded and kept up-to-date in the credit institution's central IT system on on-going basis.
- Complaints are to be filed in all cases, and only subsequently can they be delivered to administrators.
- On indemnification, the attention of administrators in member institutions and customers alike must be called to enter the changes in the system in the event of inherited deposits, and add the heir as the owner. It is also the customer's interest pursuant to the legislation whereby inherited deposits are considered as separate deposits in terms of payout.

- In future cases, special attention must be paid to purchase the customary envelope format, that can store the documents to be posted with the addressee at the appropriate place for the window of envelope.

Lessons in terms of communication

- A primary aspect for customers in terms of obtaining information is the requirement “to get all information from a reliable source without delay, and get everything done at once”. These three expectations can be best met by the NDIF’s home page, by appearances in local press that provide NDIF-related and practical information to consumers, among others – in addition to customer information–, as well as the NDIF’s staff at the other end of the phone.
- From the aspect of a smooth payout process, a key issue is an internally controlled strong activity of giving information to consumers.
- It is evident in the trade that successful payout depends at least to 50% on successful communication. The spokesperson system is necessary not just for efficient media appearances but also for relieving the burdens during the payout and management roles.
- In communication, depositors’ attention must be called to the fact that the NDIF will reimburse customers using their registered addresses in the event of a deposit freeze, and to the potential consequences of a failure to supply the correct up-to-date data.
- As a result of a favourable response rate, for a number of reasons, we plan to use the first post-crisis opinion poll among depositors on a regular basis for our future enhanced payout procedures. On the one hand, it will provide a snapshot of the trends of depositors’ confidence after individual cases, and, particularly, of the suitability of the legal framework, as well as of the stability of the banking system – to NDIF and other safety net players; on the other hand, the evaluation can be utilised in developing our services further. It is worth considering expanding the survey towards cooperation among authorities, and administering it subsequent to a regional case of payment or one generating considerable public attention in the framework of a reputation survey among the population. Such market surveys may represent the basis of trust-building steps of the regulator, the supervisor, the sector itself or individual service providers, in addition to deposit insurance.

2) Action plan

IT actions to be taken

- With the Supervision’s cooperation, it must be organised and required that member institutions incorporate a clause in their contracts with their respective IT service providers to strictly stipulate production of an interface program that complies with the NDIF’s requirements with high urgency (within 24/48 hours) and at financially justifiable service rates not exceeding normal rates.
- For customer data in IT System, an option “Deceased” is to be added to the customer status field, which facilitates a delay in the procedures of payout until the final grant of probate is received.
- For a case of payout by funds transfer, an audit function is to be added to IT System to ensure that the second entering of an account number is to control the first one, and the account number is accepted and the funds are transferred only if the two match. Because it cannot prevent a mistake when one of the data entry personnel enters a bank account number to another person entitled to payout (to one that originally did not specify a bank account number, which means that such a mistake cannot even be found by the other person entering data), this is why a security function would be necessary to signal when a

given account number has been entered to another person entitled to payout. In such cases, a paper-based verification is necessary to see whether both persons have specified bank account numbers for the funds transfer.

- In IT System, it needs to be ensured by linking certain data files that an interface is available to track not only the depositors and the related deposits but also the “indemnification history”: in addition to any linked deposits and indemnified deposits, the settlement document, the payment method and date, including the data of payment by card and any payments returned as undeliverable. In order to facilitate searches in high volumes of data, filter functions need to be added to a number of menu items.

Action to be taken in terms of payout

- Foreign nationals were also found among the depositors of the Savings Cooperative – mostly in case of branches situated along the border with Slovakia. Options of payout methods need to be found whereby foreign customers can be informed and reimbursed cost-efficiently and securely. Separation of depositors living abroad needs to be performed initially in the payout procedure, and, considering that in their case neither the current form of postal payment is adequate (payout through postal voucher), nor can the NDIF Deposit Insurance card be used, the possibility of transferring funds in the future to bank account numbers kept with foreign banks for customers living abroad – and exclusively for them.
- Contact should be established and a standby contract be concluded with a delivery company that efficiently delivers the necessary mail abroad, and can also deliver a notification of settlement. Another solution may be to cooperate with the foreign deposit insurance partner institution.
- Complaints are to be filed in all cases, and only subsequently can they be delivered to administrators.
- Considering the foregoing lessons and experiences of payout, the Payout manual needs to be reviewed, and modified if necessary.

Actions to be taken in terms of customer information and communication

- In communication, the depositors’ attention must be called to the fact that the NDIF will reimburse customers using their registered addresses in the event of a deposit freeze, and to the potential consequences of a failure to report data.
- The general communication must also include a warning to depositors stating that in the event they failed to report their identification data for former anonymous deposits, it is not possible to do so during the payout, and such deposits are not insured.
- In the communication, an attempt needs to be made to form three distinct periods within the reimbursement period in terms of messages and work-flow: the first period (period of data processing, data collection, data cleaning), when the general questions “*What happened?*”, “*How much is paid?*” and “*What is the process of payout?*” are asked; it is the “time of promises”. The settlement period (settlements, posting cards and PIN codes), the “period of first contact and reassurance”, when direct and literally tangible experience of the NDIF’s actual work performance and it is also the period of first complaints. The period of payments (“performance” - obtaining the indemnification amount), associated with the majority of complaints and a second peak of customer inquiries, also resulting from misunderstandings.
- It needs to be initiated that a uniform requirement (standard) for the format of window envelopes needed for electronic enveloping.
- It is to be initiated with partner institutions (authorities) that a reputation survey is administered jointly in the future following any regional case of payment or one

generating considerable public attention. Such market surveys may represent the basis of concentrated trust-building steps of the regulator, the supervisor and the banking sector for financial stability.

Actions to be taken in terms of auditing

- On a continuous basis, the NDIF needs to monitor and be aware of the deposit products offered by its member institutions. The data supply obligation required by HFSA Decree 3/3011. (II. 28.) as of 1 May this year may be good grounds for that, which provides additional avenue to expand cooperation with the Supervision.
- Jointly with the Supervision, a solution should be found for reports on on-site audits to contain information on quality of credit institutions' deposit recording positions – to help preparation of the NDIF for fast-payout.
- On auditing, it should be required that the data of uninsured depositors pursuant to section 100 (2) of the Act on Credit Institutions and Financial Enterprises (auditor, senior officials and their respective next of kin living in the same household) are recorded in the credit institution's central IT system.
- On reimbursement, the attention of administrators in failed member institutions and customers alike must be called to enter the changes in the system in the event of inherited deposits, and add the heir as the owner. It is also the customer's interest pursuant to the legislation whereby inherited deposits are considered as separate deposits in terms of indemnification.
- Credit institutions are to pay considerable attention to keeping the deposit and depositor register up to date, and regular data cleaning is to be required – even through prospective supervisory sanctions, if necessary.
- Full availability of the documents related to deposit taking business with the credit institution needs to be required.
- During audits, credit institutions' attention must be called to the fact that the NDIF will reimburse customers using their registered addresses in the event of a deposit freeze, and to the potential consequences of a failure to supply data.
- Continuous and close coordination among institutions (authorities) should be achieved in a cooperation agreement or in another way, not only prior to the payment period but also during the post-closure phase, in order to avoid the risks resulting from unexpected situations in a sensitive period.

It is reasonable to perform joint evaluation of the experiences of the “Jógazda” case with the business areas of the Supervision (auditing, consumer protection), focusing on shortcomings affecting both the deposit register and consumer protection. Such an event could give rise to formulating universally valid joint recommendations concerning further actions to be taken.

Enclosure

- Annex 1 (Facts of payout)
- Annex 2 (Payout Work-stream)

Details of the payout

Until 8 April, the following reimbursements took place:

Payout obligation	HUF 9 125 801 thousand EUR 35 million
Of which:	
Amount paid by postal voucher until 08.04.2011*	HUF 446 406 thousand EUR 2 million
Reimbursements settled by postal voucher	2314 items
Amount paid by NDIF Deposit Insurance card until 08.04.2011	HUF 1 634 876 thousand EUR 6 million
Reimbursements settled by NDIF Deposit Insurance card	669 items
Amount paid by funds transfer until 08.04.2011	HUF 6 805 638 thousand EUR 26 million
Reimbursements settled by funds transfer	2943 items
Total amount paid	HUF 8 886 921 thousand EUR 34 million
Total number of persons paid out **	5329 persons

* The amount is reduced by returns by post

** The number of persons indemnified and the number of indemnifications differ because a number of persons were involved in a number of deposit items

