Association for the Guarantee of Deposits Luxembourg

Ezekiel Vergara
Yale Program on Financial Stability

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Association for the Guarantee of Deposits Luxembourg

Ezekiel Vergara

Yale Program on Financial Stability Case Study
July 15, 2022

Abstract

During the Global Financial Crisis (GFC), Luxembourgish officials in October 2008 announced plans to raise the country's deposit-insurance cap to EUR 100,000 (USD 134,000) and eliminate co-insurance. Prior to the GFC, Luxembourg's deposit-insurance system covered 90% of deposits in eligible accounts up to EUR 22,222, with depositors responsible for the remaining 10%. On December 19, 2008, the legislature increased the cap to EUR 100,000 and removed the co-insurance, effective January 1, 2009. The Association Pour la Garantie des Dépôts Luxembourg (AGDL), a private deposit-insurance body, administered these changes. All deposit-taking institutions and approved investment firms, except branches of foreign banks, were automatically enrolled with the AGDL. The AGDL covered most types of deposit accounts and select investment instruments. The AGDL was an ex-post deposit-insurance scheme, meaning that the scheme collected no up-front fees. During the GFC, the AGDL paid EUR 310 million to approximately 25,000 depositors. In response to criticism from the International Monetary Fund (IMF) and others, Luxembourg replaced the ex-post scheme with ex-ante funding after the crisis.

Keywords: Association Pour la Garantie des Dépôts, co-insurance, ex-post deposit insurance, Global Financial Crisis, Luxembourg

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1 This case study is part of the Yale Program on Financial Stability (YPFS) selection of New Bagehot Project modules considering account guarantee programs. Cases are available from the Journal of Financial Crises at https://elischolar.library.yale.edu/journal-of-financial-crisis/.

2 Research Associate, YPFS, Yale School of Management.
Overview

In response to the Global Financial Crisis (GFC), on October 7, 2008, the European Union’s (EU) Economic and Financial Council urged member states to increase their deposit-insurance coverage to EUR 50,000, allowing for the possibility that some countries would raise the limit as high as EUR 100,000 (USD 134,000) (EC 2008). On October 10, 2008, the G-7 adopted a statement that emphasized maintaining a sound deposit-insurance scheme (G-7 2008).

The G-7’s statement came a day after Kaupthing Bank Luxembourg, the local subsidiary of an Icelandic bank, failed on October 9, 2008 (Wintersteller 2013). In the wake of this failure and in response to the EU and G-7 statements, Luxembourg’s minister of the treasury and budget Luc Frieden announced on October 17 that the government would propose legislation to increase the deposit-insurance coverage to EUR 100,000 (Grand Duchy of Luxembourg 2008).

Prior to the GFC, Luxembourg’s deposit-insurance system covered a maximum of EUR 20,000 (AGDL 2003). The law allowed for, but did not require, a co-insurance scheme, which covered 90% of an account’s value up to EUR 22,222, with depositors responsible for the remaining 10% (Law of 5 April 1993, Article 62-2). On December 19, 2008, Luxembourg’s Chamber of Deputies, the country’s national legislature, increased the deposit-insurance coverage to EUR 100,000 and eliminated the co-insurance feature (Law of 19 December 2010). These changes to the deposit-insurance scheme came into effect on January 1, 2009.

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3 On October 7, 2008, EUR 1 = USD 1.37, per Yahoo Finance.
The Association Pour la Garantie des Dépôts Luxembourg (AGDL), a private administrator, administered Luxembourg’s deposit-insurance scheme (AGDL 2003; Garcia 2009). The AGDL also insured claims on select investment instruments, either held by the customer or managed on their behalf. All deposit-taking institutions enrolled with Luxembourgish authorities were automatically enrolled with the AGDL. Foreign-bank branches operating in Luxembourg were not automatically insured with the AGDL, though they could receive coverage under certain conditions. The AGDL’s coverage included cash deposits, including foreign-currency deposits, and excluded deposits held by states, insurance companies, and other firms (AGDL 2003; AGDL 2005).

The AGDL was an ex-post deposit-insurance scheme, meaning that the scheme collected no up-front fees (IMF 2009). Rather, banks only paid fees after the AGDL’s guarantee was triggered. During the GFC, the AGDL paid EUR 310 million to approximately 25,000 depositors before it made any changes to the deposit-insurance system. The collapse of the subsidiaries of three Icelandic banks prompted these payouts (IMF 2010; Wintersteller 2013).

Given criticism of the AGDL’s ex-post funding by the International Monetary Fund (IMF) and Luxembourgish authorities, authorities prepared revisions to the scheme during the GFC (IMF 2009). These revisions put the deposit-insurance scheme under public control and introduced ex-ante fees. By 2011, a draft law had been completed, though Luxembourgish officials awaited the issuance of an EU directive on deposit insurance (IMF 2011). The EU released its Directive in April 2014 (EP/EC 2014).

On December 18, 2015, Luxembourg’s Chamber of Deputies made these changes, creating the Fonds de Garantie des Dépôts Luxembourg (FGDL) to administer Luxembourg’s deposit guarantee (FGDL n.d.; Law of 18 December 2015, Article 154).

As of year-end 2015, the FGDL covered EUR 28.7 billion in deposits, only 6% of total deposits in Luxembourg (IMF MCMCD 2017). With respect to funding, the IMF noted that the FGDL aimed to have an ex-ante fund equivalent to 1.6% of covered deposits. Fees were risk-based, and extraordinary fees could also be levied. As of 2016, the IMF reported that the FGDL would reach a level of 0.8% of covered deposits in 2018 and 1.6% in 2026. As of February 2022, Luxembourg continued to cover EUR 100,000 (FGDL n.d.).

**Summary Evaluation**

The IMF said that the increased deposit-insurance cap, along with the European Central Bank (ECB)’s emergency liquidity provision, served to “restore confidence in [Luxembourg’s] financial sector” (IMF 2010).

Luxembourg’s authorities said that the AGDL had “proven its effectiveness” during the GFC (IMF 2009). They argued that the ex-post funding scheme had been successful because banks had set aside EUR 828 million in provisions to deal with potential bank failures. Those provisions proved more than adequate to cover the EUR 310 million that the AGDL ultimately needed to pay depositors following the failure of three Luxembourgish subsidiaries of Icelandic banks (IMF 2009; Wintersteller 2013).
Nevertheless, Luxembourgish and IMF authorities raised concerns about the AGDL’s ex-post funding scheme and whether it would be sufficient to cover failures, leading to an in-depth revision of the AGDL (IMF 2009; IMF 2010). Officials intended to make the system publicly administered and funded ex-ante. These changes were made in 2015 (FGDL n.d.; Law of 18 December 2015, Article 154).^4^ In 2017, IMF officials evaluated the FGDL and noted that by year-end 2015, it only covered EUR 28.7 billion in deposits out of roughly EUR 490 billion (IMF MCMD 2017). The IMF said that this proportion was low because of the sizable deposits from investment funds and wealth-management clients. The IMF said that while the FGDL aimed for a maximum payout time of seven days, its operational capacity to meet this requirement was still being implemented, especially with respect to the FGDL’s IT platform. Furthermore, despite funding through ex-ante fees, the IMF urged Luxembourgish officials to establish an additional funding backstop for the FGDL, in addition to extraordinary fees.

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^4^ In 1994, Luxembourgish officials strongly opposed an ex-ante scheme, writing that its ex-post scheme was “cost-efficient and effective” (AGDL 2008b).
### Context: Luxembourg 2008–2009

<table>
<thead>
<tr>
<th></th>
<th>2008</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>GDP</strong></td>
<td>$58.9 billion</td>
<td>$54.5 billion</td>
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<tr>
<td>(SAAR, nominal GDP in LCU</td>
<td></td>
<td></td>
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<tr>
<td>converted to USD)</td>
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<td></td>
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<tr>
<td><strong>GDP per capita</strong></td>
<td>$119,932</td>
<td>$108,988</td>
</tr>
<tr>
<td>(SAAR, nominal GDP in LCU</td>
<td></td>
<td></td>
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<tr>
<td>converted to USD)</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Sovereign credit rating</strong></td>
<td>Data for 2008–2009:</td>
<td></td>
</tr>
<tr>
<td>(five-year senior debt)</td>
<td>Moody’s: Aaa</td>
<td></td>
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<tr>
<td></td>
<td>S&amp;P: AAA</td>
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<tr>
<td></td>
<td>Fitch: AAA</td>
<td></td>
</tr>
<tr>
<td><strong>Size of banking system</strong></td>
<td>$66.7 billion</td>
<td>$62.1 billion</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Size of banking system</strong></td>
<td>113.3%</td>
<td>114.1%</td>
</tr>
<tr>
<td>as a percentage of GDP</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Data not available for 2008</td>
<td>Data not available for 2009</td>
</tr>
<tr>
<td><strong>Five-bank concentration of banking system</strong></td>
<td>39.0%</td>
<td>41.9%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
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<tr>
<td><strong>Foreign involvement in banking system</strong></td>
<td>95%</td>
<td>94%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
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<tr>
<td><strong>Government ownership of banking system</strong></td>
<td>Data not available for 2008</td>
<td>Data not available for 2009</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Existence of deposit insurance</strong></td>
<td>Yes, in 2008</td>
<td>Yes, in 2009</td>
</tr>
</tbody>
</table>

*Sources: Bloomberg; World Bank Global Financial Development Database; World Bank Deposit Insurance Dataset.*
Key Design Decisions

1. **Purpose:** The increase in deposit-insurance coverage provided by the Association Pour la Garantie des Dépôts Luxembourg was meant to reassure depositors and respond to international pressures.

Given the failure of Kaupthing Bank Luxembourg on October 9, 2008, along with increased deposit guarantees in other countries, on October 17, 2008, Luxembourgish authorities announced plans to increase the deposit-guarantee cap to EUR 100,000 (Grand Duchy of Luxembourg 2008; Wintersteller 2013). Luxembourg's Chamber of Deputies adopted this change on December 19, 2008, with the goal of reassuring depositors and competing with international peers (Law of 19 December 2010; Grand Duchy of Luxembourg 2008). The changes to the deposit insurance came into effect on January 1, 2009. The operational date was chosen so as not to cover the failures of three Icelandic subsidiaries, which had occurred in 2008.

2. **Part of a Package:** Luxembourg also announced a guarantee of Dexia, a systemically important institution. Policymakers also adopted recapitalization and liquidity measures.

In addition to the changes to the Association Pour la Garantie des Dépôts (AGDL), on September 30, 2008, the Luxembourgish government also legislated a guarantee of Dexia, in conjunction with Belgian, French, and Dutch authorities (Law of 19 December 2010; Mayer Brown 2009; Wiggins, Tente, and Metrick 2019). The guarantee covered EUR 4.5 billion, including Dexia’s liabilities toward credit and institutional counterparts, its bonds, and its debt securities. For more on Dexia’s guarantee, see Wiggins, Tente, and Metrick 2019. Recapitalizations of Dexia and Fortis Bank also occurred in September and October 2008, in conjunction with France, Belgium, and the Netherlands (Petrovic and Tutsch 2009). The European Central Bank (ECB) and the Luxembourg Central Bank adopted more extensive liquidity measures to help the Luxembourgish economy (Mayer Brown 2009; IMF 2010).

3. **Legal Authority:** Luxembourg’s Chamber of Deputies passed the Law of 19 December 2008, which altered its deposit-insurance scheme.

On October 17, 2008, minister of the treasury and budget Luc Frieden announced that the government would propose legislation to increase Luxembourg’s deposit-insurance coverage to EUR 100,000 (Grand Duchy of Luxembourg 2008). The legislature approved the change with the Law of 19 December 2008. This law became operational on January 1, 2009.

Prior to the GFC, Luxembourgish law allowed for, but did not require, a co-insurance scheme, in which 90% or more of deposits were guaranteed, so long as the amount guaranteed summed to EUR 20,000 (Law of 5 April 1993, Article 62-2). The Law of 19 December 2008 did not mention co-insurance, effectively eliminating it as an option. Later, Directive 2009/14/EC required EU member states to eliminate co-insurance, and Luxembourg’s
legislature ultimately repealed it with the Law of 18 December 2015 (Law of 18 December 2015, Article 154; EP/EC 2009).

4. **Administration:** The AGDL, a private legal entity, administered the deposit-insurance scheme. Public authorities determined the extent of the AGDL’s coverage.

Luxembourgish law established the AGDL as an independent legal entity (AGDL 2003). The AGDL was privately administered (Garcia 2009).

Members of the AGDL would meet at least once each year. Each year, members of the AGDL-insured institutions reported the total amount of guaranteed deposits.

5. **Governance:** A board of directors governed the AGDL. The AGDL was subject to public controls.

The board of directors administered the AGDL. The board of directors was comprised of 11 to 15 members, all of whom represented the private sector and served two-year terms (AGDL 2003; Garcia 2009). A chairman and vice-chairman oversaw the AGDL, both selected by the board of directors. The board of directors managed the AGDL, convened meetings, and implemented its decisions. The board of directors’ decisions were taken by a majority vote, according to the AGDL’s procedures and internal rules.

The AGDL was subject to public regulation. Luxembourg’s legislature set its deposit-insurance cap and the Commission for the Supervision of the Financial Sector, Luxembourg’s prudential supervisor, determined which institutions were eligible to operate in Luxembourg (Law of 19 December 2010; AGDL 2003).

6. **Communication:** Luxembourgish officials communicated that the increase in the insured cap was meant to reassure depositors and to respond to international competitors. They also said that guarantees were not retroactive.

On October 17, 2008, following the failure of Kaupthing Bank Luxembourg, Frieden announced that the government would propose legislation to increase the deposit-insurance cap to EUR 100,000. Frieden stressed that this increase was meant to match countries that had increased their deposit guarantees and that such an increase was meant to comply with EU recommendations (Grand Duchy of Luxembourg 2008; EC 2008). Frieden also said that the measure was purely theoretical for most banks in Luxembourg. This was the case, Frieden argued, because Luxembourg had recapitalized its major banks. Furthermore, Frieden stated that the increased coverage would not be retroactively applied to the depositors of Kaupthing Bank Luxembourg.

The AGDL communicated with depositors through various media, including press conferences and the AGDL website, which included information pertinent to depositors who held accounts with failed institutions (AGDL 2008a; AGDL n.d.a; AGDL n.d.b).
7. **Size of Guarantees:** Luxembourg increased its guarantee from EUR 20,000, including co-insurance that imposed losses on depositors, to EUR 100,000 with no co-insurance.

Prior to its modification in 2008, Luxembourg's deposit-insurance system covered a maximum of EUR 20,000 (AGDL 2003). Luxembourgish law allowed for, but did not require, a co-insurance scheme, which covered 90% of an account's value up to EUR 22,222, with depositors responsible for the remaining 10% (Schich 2009; Demirgüç-Kunt, Kane, and Laeven 2014; Law of 5 April 1993, Article 62-2). The legislation adopted on December 19, 2008, increased Luxembourg's deposit-insurance coverage to EUR 100,000 and eliminated co-insurance. These changes came into effect on January 1, 2009.

In 2010, scholars reported that the AGDL covered USD 18.3 billion (Demirgüç-Kunt, Kane, and Laeven 2014). These funds were guaranteed without the presence of a standing deposit-insurance fund.

8. **Source(s) and Size of Funding:** The AGDL had no up-front fees. Eligible institutions would pay fees once the AGDL was activated to pay depositors in a failed bank, using accumulated provisions for such cases.

Given that the AGDL was an ex-post deposit-insurance scheme, there were no up-front fees for member institutions (IMF 2009). AGDL-insured institutions only paid fees once the AGDL was activated, covering for the failed institution.

In the GFC, AGDL-institutions were required to pay EUR 310 million in fees, given the failure of three Icelandic subsidiaries (Wintersteller 2013). The IMF, however, reported that AGDL-institutions had amassed EUR 828 million in provisions for such failures (IMF 2010). Luxembourgish law allowed AGDL-insured institutions to set aside up to 10% of their guaranteed deposits as special, tax-exempt provisions (Grand-Ducal Regulation of 21 December 1991). It is unclear, though, whether the Luxembourgish government provided the AGDL with guidance in the GFC.

Following changes to the Luxembourgish deposit-insurance system, the Fonds de Garantie des Dépôts Luxembourg (FGDL) aimed to have a deposit-insurance fund equivalent to 1.6% of covered deposits (IMF MCMD 2017).

9. **Eligible Institutions:** All Luxembourg-registered institutions were automatically enrolled in the AGDL.

All institutions registered with Luxembourg's Commission for the Supervision of the Financial Sector were automatically members of the AGDL (AGDL 2003). This included foreign-bank branches of Luxembourgish institutions. Foreign-bank branches operating in Luxembourg were eligible for supplemental coverage if their coverage was less than that provided by the AGDL.
The AGDL also implemented a separate guarantee on investment instruments, covering all investment firms registered with the Commission for the Supervision on the Financial Sector.

10. Eligible Accounts: The AGDL covered most types of deposits, including those in foreign currencies.

The AGDL covered “all cash deposits” made by depositors in member institutions (AGDL 2003). These included liabilities to credit institutions, savings deposits, time liabilities, and other types of accounts. The AGDL also covered foreign-currency deposits.

Some deposits were not included in the AGDL’s guarantee. These included financial instruments like those held by deposits of insurance companies, states, credit institutions, and investment funds. The AGDL also did not cover the deposits of its board of directors and their families.

The AGDL’s separate guarantee for investment firms covered instruments like securities and money-market instruments. This guarantee excluded several types of investment accounts, such as those held by investment companies, credit institutions, and other entities.

11. Fees: There were no up-front fees associated with the AGDL’s guarantee. In the case of a bank failure, the AGDL would impose levies on registered institutions proportional to the amount of each institution’s guaranteed deposits.

As an ex-post deposit-insurance scheme, the AGDL levied no up-front fees (IMF 2009). Instead, banks only paid fees after the AGDL’s guarantee was triggered by a bank failure. The AGDL’s statutes set out that, in the event of a failure, each member would pay proportionally to the amount of the institution’s AGDL-insured deposits on December 31 of the prior year divided by the total amount of deposits guaranteed by the AGDL on December 31 (AGDL 2003). The AGDL stipulated that ex-post fees could not exceed 5% of an institution’s shareholder equity. The board of directors could instruct institutions to pay these ex-post fees in advance, prior to the exact amount of depositor payouts being determined. When the AGDL was reimbursed, member institutions would be reimbursed on a prorated basis.

In the GFC, Luxembourgish institutions compiled EUR 828 million in provisions for bank failures (IMF 2010). It is unclear whether the Luxembourgish government provided the AGDL with guidance in the GFC. Bank establishments could set aside up to 10% of their guaranteed deposits as special, tax-exempt provisions (Grand-Ducal Regulation of 21 December 1991).

The FGDL, which was established in 2015 and replaced the AGDL, received ex-ante, risk-based fees from banks (IMF MCMD 2017). Banks could also be subject to extraordinary fees.

12. Process for Exercising Guarantee: The AGDL would be activated if the Commission for the Supervision of the Financial Sector determined that an institution was or was soon to be unable to meet its depositor redemptions or if a court suspended
an institution’s ability to pay depositors. The AGDL would then pay claims in no more than three months, subject to extension.

Pursuant to Luxembourg law, the AGDL could be activated for two reasons. First, if the Commission for the Supervision of the Financial Sector determined that a member institution would be unable to repay its cash deposits at that time or in the near future (AGDL 2003). Second, if a Luxembourgish court suspended an institution’s ability to take and redeem deposits. The AGDL would then pay out depositors, which could take up to three months. In exceptional circumstances, the AGDL could request up to three extensions, none exceeding three months. The AGDL required liquidators or legal representatives to verify depositor claims. The AGDL was granted subrogation against a failed institution.

13. Other Restrictions on Eligible Institutions/Accounts: There were no additional conditions.

There were no additional conditions associated with the changes to the Luxembourgish scheme.

14. Duration: The changes to the Luxembourgish deposit-insurance scheme were permanent changes.

The 2008 changes to the deposit-insurance system were adopted as permanent changes, without a sunset date (Law of 19 December 2010). As of February 2022, Luxembourg continued to cover EUR 100,000 (FGDL n.d.).

During the GFC, Luxembourgish authorities prepared revisions to the scheme, including altering the scheme to an ex-ante funding method and making the scheme publicly owned (IMF 2009). By 2011, a draft law had been completed, though Luxembourgish officials awaited the issuance of an EU directive on deposit insurance (IMF 2011). The EU released its directive in April 2014, and Luxembourgish officials made the aforementioned changes on December 18, 2015 (EP/EC 2014). This created the FGDL to administer Luxembourg’s deposit guarantee (FGDL n.d.; Law of 18 December 2015, Article 154).
References and Key Program Documents

Documents cited in the text are introduced with a parenthetical author-date citation. Documents that are relevant to this case but have not been cited in text do not include this parenthetical reference.

Program Summaries

Web page highlighting the FGDL and its purpose.  
https://ypfs.som.yale.edu/library/document/about-fgdl

Summary of Luxembourg’s financial interventions in the GFC.  

Implementation Documents

Document containing frequently asked questions and their responses.  
https://ypfs.som.yale.edu/library/document/frequently-asked-questions-0

Legal/Regulatory Guidance

Brochure discussing Luxembourg’s deposit-insurance scheme.  
https://ypfs.som.yale.edu/library/document/agdl-brochure

Directive requiring EU member states to update their deposit-guarantee systems, in accordance with principles established by the ministers of finance.  

EU Directive on deposit-insurance schemes.

Regulation allowing AGDL members to set aside tax-exempt provisions.


Law establishing the AGDL’s coverage requirements.


Law overhauling Luxembourg’s deposit-insurance system.

Press Releases/Announcements


AGDL web page regarding the failure of Glitnir.
https://ypfs.som.yale.edu/library/document/agdl-glitnir


AGDL web page discussing the failure of Landsbanki.
https://ypfs.som.yale.edu/library/document/agdl-landsbanki


AGDL web page regarding the failure of Kaupthing.
https://ypfs.som.yale.edu/library/document/agdl-kaupthing


Press release summarizing the Council’s coordinated response to the GFC.


Statement by the Group of Seven countries outlining their response to the GFC.
https://ypfs.som.yale.edu/library/g-7-finance-ministers-and-central-bank-governors-plan-action


Announcement in which Luxembourg pledges to increase its deposit-insurance coverage.

Reports/Assessments

AGDL responses to an EU Directive.


Review of Luxembourg’s economy.


Review of Luxembourg’s economy and its response to the GFC.

Evaluation of Luxembourg’s economy in 2011.

IMF FSAP discussing the FGDL. 

Key Academic Papers

World Bank policy-research working paper providing a comprehensive, global database of deposit-insurance arrangements as of 2013. 
https://ypfs.som.yale.edu/library/document/deposit-insurance-database

Book chapter examining deposit-insurance systems across EU member states. 

Piece detailing financial responses to the GFC by country. 
https://ypfs.som.yale.edu/node/4151

Examines deposit insurance in relation to topics in economics. 

Case study of the EU intervention of Dexia. 
https://ypfs.som.yale.edu/node/3065
Examines Luxembourg and its deposit-insurance system. 

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