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## Performance of the Nigeria Deposit Insurance Corporation (NDIC)

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### Abstract

*The Nigeria Deposit Insurance Corporation (NDIC) which is more than a decade old has since been battling with the problem of protecting depositors in case of bank failures and promoting sound banking practice and habit. Although it has made much in road with respect to payment for insured bank deposits and liquidation dividends to customers of failed banks, supervision of bank activities and so on. There is still much to be done to satisfy the citizenry. This work therefore tries to look into the corporation's achievements so far as well as its problems with a view to suggesting ways to make it more productive.*

### Introduction

One of the problems that confront the banking sector (both in under-developed and developed countries) is the phenomenon of bank distress. No matter the cause or origin, once a bank starts showing signs of distress, the confidence of the customers of such bank gradually starts being eroded. There might even be a run on such bank (which worsens matters and) which eventually leads to total failure and liquidation. A run on a bank is a situation whereby most of the bank customers who deposited money with such a bank suddenly rush at a time to withdraw very substantial part (if not all) of their deposit. Since the bank operates on the principle that not all who deposited money with it will come to withdraw their deposit at the same time, a run on a bank creates a situation in which the bank will be unable to redeem its obligation

to its customers, At other times, it might be that the fraud in the bank has reached such an alarming rate that the bank becomes insolvent. Even loan default in form of doubtful debt in such an alarming dimension is sufficient to generate "cracks" in the "walls" of the stability of a bank.

There is therefore an acceptable need for an independent body to protect the interest of depositors and promote sound banking habit in which the confidence of depositors in the banking system is not shaky. This is because in the event of any bank failure, the depositors' fund is at stake. The entrepreneurs (in form of the directors and shareholders of the bank) are seriously affected. There is a setback in the economy as productivity is affected.

This is where Deposit Insurance schemes are invaluable in preventing ugly consequences as a result of bank distress and failures in the economy. A 'Deposit Insurance Scheme' (DIS) is an arrangement whereby a designated agency (usually government - owned) guarantees deposits in the insured financial institutions. The guarantee is usually limited to discourage moral hazard, a situation whereby the financiers and depositors would care little about the safety of the deposits because such deposits are fully insured. Also most DIS act as liquidators of failed insured institutions while some, in addition, act as supervisors of insured institutions as well. It is noteworthy that in a DIS, unlike ordinary insurance, the insured institution pays the premium for the benefit of the depositors.

#### **The establishment of Nigeria deposit insurance scheme (NDIC)**

In Nigeria such a scheme is in form of Nigeria Deposit Insurance Scheme (NDIC) Ogunleye (2004) says that "The Nigeria Deposit Insurance Corporation (NDIC) was established in 1988 as an explicit deposit Insurance scheme under the Nigeria Deposit Insurance Corporation Decree No 22 of 1988 now Cap. 301, Laws of the Federation 1990 as amended. Section 1 (I) of the NDIC Act provides for the establishment of the NDIC as a body corporate with perpetual succession and a common seal. The NDIC commenced operations in March 1989. The primary aim of establishing the NDIC is to maintain stability and public confidence in the banking sector by guaranteeing payments to depositors in the event of failure of insured institutions as well as promoting safe and sound banking practices through effective supervision. It is an autonomous regulatory body with powers to examine the books of insured banks and other deposit-taking financial institutions and to restrict the activities of banks found not to be in compliance with regulations. It can also arrange for other banks to assume the deposit liabilities of a failing bank or take over the management of a bank where such action becomes necessary to protect depositors' interest.

In a nutshell, the functions of the NDIC include:- insuring the deposit liabilities of all licensed banks, supervising the activities of all insured institutions through off-site and on-site examinations alongside the Central Bank of Nigeria (CBN). In

conjunction with the CBN, the NDIC also resolves distress in the industry where ever and whenever it occurs and acts as liquidator and receiver of any failed bank. Aguolu (1998) says that "in terms of management and control, the NDIC has the Governor of the Central Bank as chairman. It also has a managing director, two executive directors and three representatives of the Federal Government. The NDIC is owned 60% by the Central Bank and 40% by the Federal Government." With deposit insurance therefore, the failure of one bank becomes an isolated event since it eliminates the danger that unfounded rumours would trigger off courageous bank runs. The corporation tries to ensure safety of depositors' funds and to promote stability in the banking system. The depositor in insured financial institutions does not lose all his deposits in case of bank failure.

Let us briefly look into the achievements of NDIC so far.

#### **The achievements of NDIC so far**

According to Salmon (2004), "Nigeria Deposit Insurance Corporation (NDIC) has paid a total sum of N8.6 billion to the depositors of failed banks in the country. The amount represents total insured deposits of N3.3 billion and N5.3 billion liquidation dividend paid to depositors of the closed banks as at January 2004". According to him, a lot of depositors are yet to come forward to collect their deposits in the closed banks despite series of public campaign embarked upon by the corporation in the mass media to educate the public about NDIC activities. He attributed low response by depositors to the fact that many of them have small deposits balance with the closed banks and apathy or ignorance on the part of many depositors that they could still get their money trapped in the closed banks from NDIC. Umoh (2004), says that "in addition to the payment made to insured depositors of a total sum of N3.3 billion naira (representing 63% of ₦5.2 billion total insured amount) have been collected by the depositors of the 34 failed banks as at December 2003. More and more uninsured depositors have continued to be paid liquidation dividends. As at January 2004, N9.9 billion aggregate dividend had been declared by NDIC for 32 out of the 34 banks in liquidation, and N5.3 billion paid. The balance which is with the agent banks are yet to be collected by the uninsured depositors". Also liquidation dividends were paid to some of the general creditors of some of the banks. The NDIC has therefore done much as far as deposit guarantee and liquidation of dividends are concerned.

With respect to depositors' protection through supervision, the enhancement of supervisory capacity through focused training and acquisition of relevant tools is being vigorously pursued by corporation. In that regard, more staff in the on-site and off-site supervision departments of NDIC have been exposed to new techniques of banking supervision. Similarly, the existing tool for off-site surveillance, "the Bank Analysis System (BAS)," has been enhanced to mitigate some of the problems associated with off-site supervision in our system. Although much has been done in the areas of supervision, it may have been better to have included coordination of

bank activities at interbank level.

This will enable banks which are about to experience distress to identify horizontal competitors and negotiate possibilities of vertical integration or merger. The NDIC will in that capacity be acting as an inter bank linkage and the harbinger of good will messages between banks.

### **Modus operandi of NDIC to protect depositors**

Depositors of insured banks are, by law, allowed to file their claims (which signify that depositors have money in the banks) within 18 months after the bank has been closed. Immediately a bank is closed, and the assets and liabilities of the bank are determined by NDIC and claims filed by depositors, NDIC would pay insured deposits of maximum of N50,000 (there is now a bill before the National Assembly to increase it to N100,000), from the pool of premium paid by the bank when it was alive.

It is pertinent here to note that the premium of the deposits is being paid by the bank and not the depositors themselves.

Later, the corporation would embark upon the sale of the assets of the bank while debts are also recovered from their debtors. The proceed would be used to pay liquidation dividend (excess deposit amount above N50,000) to depositors of the bank. If there is any amount remaining after all depositors have been paid, the money would be used to settle creditors of the bank first and later share holders of the bank. In Nigeria, small depositors with balances between N1. and the proposed maximum coverage of N100,000 constitute about 80% of total depositors. It is therefore quite reasonable to protect this silent majority because in the event of their panicking and bombarding some banks to effect withdrawals, the stability in the financial sector would be shaken, more so because the banking system is very prominent in the financial sectors (Agunleye 2004).

Although NDIC has achieved so much, it can still do better if some of the problems militating against it are tackled.

1. The insurance coverage of N50,000 (maximum) which has been proposed to be N100,000 by the National Assembly is still not appropriate. In view of the fact that inflation has seriously reduced the value of the naira to the extent that many depositors have balances in excess of N200, 000 and in so far as the inflation is continuing, it is not desirable to go and review the maximum premium payable in a matter of few months considering the length of time it takes for bills to be passed in the National Assembly. It may make better sense if the maximum premium is raised to N200,000.
2. The Functions of the NDIC did not include

- A. Coordinating activities between banks so that these banks will early enough discover same level competitors, the things they have in common so as to pave way for mergers or vertical integration in the event of certain stringent regulations (like the N25 billion capital base requirements by the banks). This will help to reduce panic measures by banks in such an event.
  - B. A provision for factoring. According to Umoh (2004) "The major problem facing the corporation now is debt recovery. Post liquidation interest amounting to N5.16 billion were written off from the total loans of N35.37 billion in 2000 leaving the remaining at N30.21 billion." Therefore an arm of the NDIC should be charged with debt factoring, not only to generate more revenue for the corporation but also to seriously prevent frequent distress in banking industry occasioned by bad and doubtful debt.
3. Another problem of NDIC lies in the agent banks as well as where both the insurance guarantee and liquidation dividend are paid.

It has been observed that part of the insurance guarantee payment and liquidation dividend are still uncollected, despite the series of campaigns embarked upon by the corporation in the mass media to educate the public about NDIC activities. Most of the time the payments are made at the State Government headquarters in the agent bank and not at the premises of the failed bank. In such a case, the factor of proximity counts so much. Depositors with small balances may decide to forfeit their pay simply because of the distance and bureaucratic bottle neck involved before receiving their entitlements. It may have made more sense if the agent banks go to the premises of failed banks to effect payment. With this system almost every depositor will go to the premises where he used to bank to collect his entitlement.

Finally, the problem of receiving unreliable returns from banks seriously undermines the off-site supervisory function of NDIC. Through offsite surveillance of the banks, using statutory returns usually enables NDIC to have early warning signals of a bank's distress. Such a warning enables NDIC to propose remedies in time but this is normally sabotaged by presentation of falsified returns by banks in order to hide whatever difficulties the banks might have.

The solution here is to have special representative in each bank being paid by the corporation (but at the same time a staff of the bank concerned).

He will be acting as a sort of 'Intelligence' officer that will be a reliable informant of the bank's actual financial standing. He will be a high caliber educated accountant so as to readily comprehend the books of the bank concerned.

## **Conclusion**

The Nigeria Deposit Insurance Corporation which was established in 1988 has meanwhile performed creditably in insurance guarantee payment, in liquidation dividend payment and in supervisory and advisory capacities, but much still needs to be done.

The current N50,000 maximum insurance coverage (and even the proposed N100,000 to the National Assembly) is grossly inadequate to satisfy the expectations of depositors mainly because of the problem of inflation.

The problem of receiving unreliable returns from banks seriously undermines the off-site supervisory role of NDIC.

The site for the payment of both insurance guarantee and liquidation dividends tends to alienate the depositors of failed banks.

The official function of NDIC does neither include the coordination of interbank activities nor does it have any provision for debt factoring.

## **Recommendations (the way forward for enhanced productivity)**

In the light of the above conclusions, it is here recommended that:- The maximum insurance coverage be raised to N200,000.00 (two hundred thousand naira).

Special intelligence informant paid by the corporation will be a senior employee of each bank.

Payments for insurance guarantee and liquidation dividends will henceforth be at the premises of failed banks in order to stop alienating certain depositors.

The official functions of NDIC should be expanded to include coordination of interbank activities and a provision for debt factoring. If the above recommendations are complied with, there will be enhanced productivity and nation building emanating from the stability of the financial sector.

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