

Masters in Business Administration

Thesis Topic: Protecting Depositors in Palestine. Is there a need for the Establishment of Deposit Insurance?

إقرار الاستقرار المالي وحماية المودعين في فلسطين. هل هناك حاجة لإنشاء تأمين على الودائع؟

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Abstract

Deposit insurance has become a popular instrument used by governments in an attempt to ensure bank stability and protect bank depositors in case of bank failure. The purpose of this study was to investigate the need of a deposit insurance scheme in Palestine. This thesis is divided into 6 different chapters. In the first chapter there is a brief introduction of the study. A literature review contains issues related to the implementation of a deposit insurance scheme including the positive and negative aspects associated with deposit insurance. Deposit insurance in the MENA region was discussed and the case of Jordan was explained. Qualitative and Quantitative methods were used for the collection of data. Questionnaires were administered to compliance departments at major commercial banks and interviews were conducted at the Palestinian Monetary Authority and with compliance managers and commercial banks. The findings were discussed and analyzed and a list of recommendations were made. The principal conclusion to be made from this study is that the adoption of a deposit insurance scheme in Palestine is necessary and important.

Table of Contents

Section Titles	Page Number
I. Abstract	
II. Chapter 1 – Introduction	5
a. Statement of the problem	6
b. Definition of terms	6
c. Need for the study	6
d. Limitation of the Study	6
e. Research Questions	7
III. Chapter 2 – Literature Review	
a. Deposit Insurance: When it All Began	9
b. Principles of Deposit Insurance	10
c. Governance	12
d. Deposit Insurance Funding Methods	13
e. Deposit Insurance: The good and the bad	15
f. Deposit insurance and moral hazard	17
g. Deposit Insurance and Adverse Selection	18
h. Making Deposit insurance effective	19
i. Deposit insurance and bank stability	20
j. Deposit insurance and financial development	20
k. Deposit Insurance is not enough!	21
IV. Chapter 3- Deposit Insurance in the MENA region and the Palestinian Context	
a. Deposit insurance in the MENA region	23
b. The case of Jordan	23
c. The Palestinian Context	25
d. Economic and performance indicators	25
e. Palestinian Monetary Authority	25
f. Bank Overview	26
g. Banking Developments	26
h. Performance of the Palestinian Banking Sector	26
i. Legislative and Regulatory Environment	27
V. Chapter 4- Research Methodology	
a. Research Design	30
b. Population and Sample	30
c. Methodology	31
d. Reliability and Validity	32
VI. Chapter 5- Findings and Discussion	33
VII. Chapter 6- Conclusions and recommendations	57
VIII. References	62
IX. Appendix	66

Chapter 1

Introduction

Introduction

There isn't an individual that wouldn't like to know that their savings is protected. Like any other business, banks and other financial institutions can fail. Consequently deposit insurance is needed to provide an effective and necessary way to achieve financial safety. In order for a depositor to trust a bank with confidence with his money, there must be some sort of guarantee that they will get their money back. Deposit insurance is the main way to assure the safekeeping of a depositor's money. The need for deposit insurance emerges from the actuality that banks are in the function of lending money and collecting interest on it. This money comes from the depositor's accounts and the bank only keeps a small percentage of their customer's money on reserves as cash at any given time. The danger exists in the fact that if a banks' customers feel that their bank is having some kind of financial problems, due to borrowers defaulting on loans, and their incentive is to get their money out while they still can. When a banks depositors do this all at once it is said that there is a run on the bank. Because a bank only holds a part of the total funds on reserve, not everyone will be able to get their money. When the bank has no more cash left on hand it has no choice but to go out of business.

In order for there to be economic growth and a developed economic system there must be a properly functioning financial system. The most important part of the financial system are banks. Their significance is derived from their ability to create money and fulfill the intermediation function of accepting liquid deposits and transforming such deposits into illiquid loans for borrowers. This function is termed asset transformation and is said to be welfare enhancing, because it allows funds to be accessed by entrepreneurs for investment purposes, while depositors' liquidity is maintained through demand and other term deposits (Gorton and Pennacchi, 1990).

The critics of deposit insurance emphasize that the proposal of a deposit insurance plan will initiate a moral hazard issue. Depositors and banks would then be motivated to take on more risk. Banks would compete for deposits because depositors would favor safe banks over risky banks to protect their money if there wasn't deposit insurance. If there was deposit insurance, banks would be able to take on extreme risks because depositors would not feel that their savings needed to be protected. Without this need to feel sheltered they would not have to move their money to safer banks.

The establishment of a deposit insurance program can contribute to financial development. The introduction of deposit insurance can stabilize the financial system and reduce the risk of systematic failure. By strengthening depositor's confidence in the stability of the system, deposit insurance may lead to a deeper financial system, which could add to higher economic growth rates.

Statement of the Problem

Is there a need for Deposit Insurance in Palestine? And if a plan for Deposit Insurance were implemented how would this affect the Palestinian financial system and economic situation?

Definitions of Terms

The following are some main concepts that will be used in the study and their brief definitions:

1. **Deposit Insurance:** a measure applied to protect bank depositors from losses caused by a bank's inability to pay its debts when due. Deposit insurance systems are one component of a financial system safety net that promotes financial stability
2. **Banks:** A financial institution in Palestine that collects deposits and gives loans.
3. **Bank run:** when a depositor rushes to withdraw their deposits because they expect the bank to fail. The sudden withdrawals can force the bank to liquidate many of its assets at a loss and fail.

Need for the Study

During the past two decades the world has witnessed an array of banking crises and banks are becoming systematically insolvent. This kind of crisis can occur in both developed and developing economies. Financial safety nets are needed in case of a financial system breakdown and to reduce the costs if one actually does occur.

There is a need for this study to see if there is a need for the establishment of deposit insurance in Palestine. This is important because deposit insurance acts as a part of the safety net in order to eliminate the risk of loss of depositor's funds and prevent bank runs by maintaining depositor's confidence and protecting their savings.

Limitations of the study

This study aims on covering most of the issues related to deposit insurance but unless there are some limitations then this study won't be totally comprehensive. These limitations include:

- Lack of Information on the subject matter of deposit insurance.

- Lack of compliance with Banks and the Palestinian Monetary Authority.

Research Questions

1. What are the benefits of Deposit insurance?
2. Is Deposit Insurance needed in Palestine? What are the challenges facing the deposit insurance practice and how can they be overcome?
3. To what extent would the Palestinian Economy benefit from the implementation of Deposit Insurance?
4. How can Deposit Insurance improve the financial system in Palestine?
5. Does the deposit insurance practice enhance financial stability in Palestine?

Chapter 2

Literature Review

“After all, there is an element in the readjustment of our financial system more important than currency, more important than gold, and that is the confidence of the people.”

President Franklin D. Roosevelt spoke these words in his first speech to the people of the United States on March 12, 1933. President Roosevelt was urging the people to remain calm and avoid the panicked withdrawals that had crippled the nation’s banking system in the first months of 1933. Despite the federal government’s newly adopted plans to restructure many closed but feasible banks, some 4,000 banks that had closed earlier in 1933 or during the bank holiday never reopened.

The adoption of a federal plan to protect depositors was still uncertain, because the confidence of the people was still shaken and public opinion remained uncertain. President Roosevelt, the Secretary of the Treasury and the Chairman of the Senate Banking Committee had voiced an Opposition to such a plan. A system of deposit insurance would be expensive and would unfairly subsidize poorly managed banks, was what they believed. Despite their opposition public opinion went with the Congress, and the Federal Deposit Insurance Corporation was created three months later when the President signed into law the Banking Act of 1933. The final months of 1933 were spent organizing and staffing the FDIC and examining the nearly 8,000 state-chartered banks that were not members of the Federal Reserve System. Federal deposit insurance became effective on January 1, 1934, providing depositors with \$2,500 in coverage, and by any measure it was an immediate success in restoring public confidence and stability to the banking system. Only nine banks failed in 1934, compared to more than 9,000 in the four years before.

Federal deposit insurance remains a fundamental part of the nation’s financial system till this date. The severity of the 1930s banking crisis has not been repeated, but bank deposit insurance was harshly tested in the late 1980s and early 1990s. The system emerged battered but sound and, with some legislative tweaking, better suited to the more volatile, higher-risk financial environment that has evolved in the last quarter of the 20th century.

Principles of Deposit Insurance

Banks are providers of liquidity. As intermediators they ease the transfer of funds between savers and borrowers. If depositors fear that their funds are not readily available, then this could cause a bank run. If a bank run occurs this can turn into a banking crisis because it may spread to sound banks. The result is that access to credit becomes severely restricted, depositors lose access to their funds, and a heavy burden is imposed on the economy (Bernanke, 1983).

Deposit insurance provides depositors with a guarantee that, in the event of a bank failure, their deposits, in part or in full, will be refunded. In many cases the deposit insurance agency is government regulated, administered, and funded, with member banks paying a premium to insure their deposits. The absence of a permanent and credible guarantee can set off persistent occurrences of bank runs.

After a long period of the increase of the prices of houses the US housing bubble burst in 2004. More families were being able to take out mortgages than previously possible. Lending to risky borrowers known as “sub prime lending started. These mortgages started with low interest rates then increased dramatically. Soon new home owners were unable to pay or refinance. The banks and lenders making these loans sold the debt to investors. During 2007 almost 1.3 million housing properties were subject to foreclosure. Banks now were no longer willing to lend each other resulting in a “credit crunch”. By July 2008 major banks and financial institutions around the world reported losses of almost 435 million. Many banks closed or declared bankruptcy. Governments had to rescue these institutions because of the fear of what their collapse would do to the broader economy. These institutions included Freddie Mac and Fannie May in the US, the insurance company AIG, Northern Rock in the UK and Fortis and Dexia in Belgium. The US government prepared a 700 billion bailout package in anticipation of future bankruptcies.

The average insurance amount provided by the FDIC now is \$250,000 per depositor, per insured bank, for each account ownership category. The FDIC insures deposits only. It does not insure securities, mutual funds or similar types of investments that banks and thrift institutions may offer. More than 4900 banks are observed and managed by the FDIC. This make up more than half of the institutions in the US banking system.¹ Banks that are insured by the Federal Deposit Insurance Corporation are also regulated by the FDIC. Both member and nonmember banks have the choice to offer FDIC insurance to their customers.

¹<http://www.fdic.gov/about/learn/symbol/>

As the global financial crisis of 2008 evolved, authorities in the United States and the European Union countries increased the limit and broadened the coverage of their respective deposit insurance schemes. The importance of deposit insurance to the stability of the banking sector is shown through these actions. Although targeted at the banking sector, these measures are designed to restore confidence to the broader financial markets and are consistent with the undeniable belief of some policymakers that deposit insurance positively impacts the overall financial markets.

The main priority of banking institutions is for them to be safe and sound. To enhance public confidence an effective deposit insurance system is expected, which will in turn minimize bank runs. Explicit deposit protection may be designed for consumer protection and macroeconomic stability (Carapella and Di Giorgio, 2004). The design of such a scheme avoids and possibly minimizes the risk of bank failure. In the case of a fear of bank failure depositors are likely to withdraw their funds from solid or safe banks.

Deposit insurance has become a crucial component of the financial safety net of 95 countries around the world, partly due to the financial crises experienced in the 80's and 90's (Carapella and Di Giorgio, 2004).

Deposit insurance schemes can be either implicit or explicit. Under an implicit deposit insurance scheme there are no stated rules. The only assurance that depositors have is what is implied by the government through its action or stated intention. Under an explicit deposit insurance scheme the terms and conditions are explicitly stated in law. The scheme provides a legally enforceable guarantee on all, or a portion of the principal, and in some cases the interest, on a deposit. The law also states the types of deposits that are enclosed in the incident of bank failures. (Isazade, 2009)

Governance

Every deposit insurance system should have a form of higher authority, which is held accountable from which the system receives authorization. This includes a governing body, and a management team. The deposit insurance system should be structured in a way that the chance for unnecessary political and industry influence, conflicts of interest between members and management is at a minimum. All responsibilities to depositors, member banks, and other relevant stakeholders must be upheld.

According to the Canada Deposit Insurance Corporation (CDIC) International Deposit Insurance Survey, 2003; Demirguc-Kunt, Kane, and Laeven, 2006; and Garcia, 1999, of 79 deposit insurance systems surveyed, 70 were structured as legally separate entities (53 were government agencies or state-owned enterprises, and 17 were privately administered). Nine deposit insurers were structured as departments of a central bank, government department, or other public authority. Separate legal entities are defined as organizations that exist as legal persons in their relevant authority and are governed by a board of directors, a supervisory board, or another type of governing body.

There can be a conflict of interest between the key stake holders and the deposit insurance system. The deposit insurance system must be in full authorization so as to minimize the potential conflicts due to political and other external influence. It is also important for the deposit insurer to communicate and share information with other safety net organizations. This communication can increase the organizations effectiveness and help prevent gaps in responsibilities.

Third party information in a deposit insurance system should be disclosed and protected. Practices should be carried out in an ethical and effective manner. The confidential information that deposit insurance systems receive affects the stability and competitiveness of the member banks and in turn the stability of the financial system as a whole. With this said transparency and disclosure assist with implementing a sound deposit insurance scheme. ²

² Governance of Deposit Insurance Systems, Prepared by the Research and Guidance Committee International Association of Deposit Insurers, 2008

Deposit Insurance Funding methods

To be effective, a deposit insurance system must have access to adequate sources of funding to meet its obligations when they come due.

A. Ex- Ante Funding

When there is an accumulation of a fund to cover deposit insurance claims and related expenses prior to a failure actually occurring, this is known as ex ante funding. Members through contributions, insurance premiums and other means place money in the fund. . This system is more rule-based and offers greater certainty than other. The knowledge that funds have been raised in advance and that the fund is well-managed can reassure depositors that their insured deposits are safe. This helps minimize the risk of sudden withdrawals which could lead to a bank run. An ex ante system also has the advantage of being more reasonable than an ex post system. This is because all member institutions including those that fail will have helped to support the system financially through payments into the fund.

Insurance premiums are collected taking into the account that there will be expected losses in the long run, so the cost of insurance losses is spread over time. Premiums are collected for the fund during times of strong economic conditions which can be used when losses are expected to be higher.

B. Ex Post Funding

In the case of ex post funding, funds are only collected when the institution as failed. There are no explicit responsibilities concerning the sharing of costs for reimbursing depositors. This means that the all costs are placed on the surviving institutions and the failed institution does not reimburse its depositors. The only time an ex post system seems to be beneficial is when there are no failures. Under an *ex-post* system, when the industry and economy are healthy, contributions are minimized and the operating expenses of the deposit insurance system may be low.

C. Hybrid Funding

This type of funding combines both the features of both ex ante and ex post. an ex ante fund financed by premiums and contributions is integrated with a method to obtain funds ex post from member institutions, through special premiums, levies or loans if they are needed.

Table 1: Relative Evaluation of Ex Ante Funding Versus Ex Post Assessments

	Ex ante funding	Ex post assessments
Effectiveness		
Deposit insurer's liquidity	• •	-
Deposit insurer's solvency	• •	-
Transparency and information sharing	• •	-
Conducive to supervision allowing for risk measurement and control	• •	-
Cross sectional risk adjustment of premiums for fairness and correct incentives	• •	-
Smoothing of premiums through time for improved stabilization	• •	-
Potential for government back-up financing (as most funded systems are publicly run)	• •	-
Confidence of depositors	• •	-
Efficiency		
Operating costs	-	• •
Issues related to funds management		
- Optimization of quantity-target level	-	• •
- Optimization of quality-risk-return	-	• •

• † relative advantage, -: relative disadvantage

Source: Roy (2000).

As can be seen from the above table, ex ante funding has numerous advantages. There will be an already available pool of funds. This will allow for the quick disbursement of funds to insured depositors. Also it is fairer to collect premiums from all members before a failure to help cover the costs. The fact that there is a fund that can reimburse depositors helps restore public confidence in the deposit insurance and banking system.³

³ Funding of Deposit Insurance Systems, 2009

Deposit Insurance: The good and the bad

Despite the fact that deposit insurance is said to provide a solution to banking crises, a different view was suggested by Economides, Hubbard and Palia. They stated that federal deposit insurance was placed for the benefit of small banks that were located in areas where large banks wanted less restraining branching legislation. Small banks benefit from deposit insurance because they are able to hold less capital and are better able to attract deposits. There is a conflict of interest between large banks that are well capitalized and are in favor of branching and are in opposition to deposit insurance and small poorly capitalized banks.⁴

A deposit insurance system provides protection to small depositors. Small depositors do not have enough awareness to assess the risk of banks. This is due to the fact that the banking system is complex. (Kraft, 2004). Also major depositors are said to be more informed than small ones. In case of an upcoming crisis they would end up withdrawing their deposits before the small depositors do. An introduction of deposit insurance would reduce risk and ensure financial security of small clients. Everyone will be equally served and there will not be a “first – in line, first- served” rule with the adoption of a deposit insurance scheme. (Momirović, Simonović and Milisavljević)

Diamond and Dybvig (1983) state that even “healthy” banks can fail because bank runs can cause real economic problems. In the event of failure from a healthy bank, loans will be recalled and productive investment will be concluded. Deposit insurance can prevent a banking system from bank runs. A bank run occurs when the banks liquid but risky assets are no longer able to cover fixed liabilities (demand deposits). Depositors then withdraw their money quickly. A study done by Bernanke shows that bank runs give better predictors of economic distress than money supply. Diamond and Dybvig also suggest that a government intervention through deposit insurance is the best way to deal with the liquidity problem of bank runs.

Deposit insurance also is have said to increase competition on the banking sector. When a bank is large it has a more recognizable name. Due to this large banks can collect deposits are a lower interest rate than smaller banks. (Kraft, 2004)

Karekan and Wallace (1978) claim that there is no need for deposit insurance as long as creditors know what the portfolios of banks hold and that bankruptcy will be costly. Knowing this information there will be no bank runs.

⁴ Federal Deposit insurance: economic efficiency or politics?, 1996

If creditors don't have this information about banks then a bank can increase the riskiness of its portfolio. Profits will increase without an increase in costs. A situation of asymmetric information is created between creditors and banks. Information is costly so there will be a cost to remove this asymmetric information. (Yilmazkuday)

Financial stability of the system will put off bank runs through the implementation of deposit insurance despite the conditions of the bank. It is important for the financial system to have certain conditions so as to provide reliability and sustainability. Such conditions include: a sound legal system, an established macroeconomic environment, efficient regulation and supervision, conformity with accounting and regulatory standards, and effective disclosure techniques. (Isazade, 2009)

Bank stability can be improved through an explicit deposit insurance scheme, but some studies have shown otherwise. Deposit insurance is said to have an effect of risk-taking behavior and market disciplines. In the core principles of 1997 the Basel committee did not include deposit insurance as one of its key principles. (Lastra, 2006)

One of the most important benefits of deposit insurance is that all deposits at all insured institutions will be uniformly attractive and always safe. Depositors will not need to differentiate between different institutions. This will create confidence in the banking system as a whole. If one bank fails, depositors at other banking institutions will not need to be concerned about their deposits. This will reduce a threat of a run on the banking system. (Grossman)

Deposit Insurance and Moral Hazard

Concerning the effect of deposit insurance on banks, there are mixed views. It can stabilize the banking system and build confidence from one aspect. On the other hand deposit insurance can be accompanied by the problem of moral hazard. This is because its presence reduces depositors monitoring of the actions of banks. Because deposit insurance conveys a put option on the owners of the bank (Merton, 1977), opportunistic managers may try to maximize the risk of the bank without fear of being subject to depositor discipline. Due to this the banking sector will be subject to an even greater amount of financial instability as a result of the increase in risk taking. With these points deposit insurance has been argued to encourage the very problem it was designed to moderate.

The moral hazard problem is made worse by the presence of large banks, which if become insolvent may induce a financial collapse. Agents in the financial markets know that the government will bail out such banks in the case of a failure (Prescott, 1999). The government therefore will cover all losses to the depositors of a large bank. In this case both depositors and managers are hesitant to the bank's risk exposure, and banks shift funds from less into high-risky assets (Feldman and Rolnick, 1998). Finally the government will be forced to suffer significant losses measured in paid-off deposits and financial disorders (Horvitz, 1975).

Another type of principal agent-problem arises whenever an employee or a contractor, acting as an agent for the principal that he represents, pursues his own interests rather than those of his employer. This problem is related both to the managers of financial institutions and to the representatives of the government (Garcia, 1999). Managers could try to get additional benefits to their own at the expense of increasing risk, shifting possible losses to the depositors and taxpayers.

An essential issue is the setting of the coverage limit. Public confidence is created by having sufficient coverage and it also prevents moral hazard. Moral hazard which is believed to cause extreme risk taking by banks. Banks are then more optimistic to finance high- risk high return projects which in turn may cause more bank failures. (Ng, Lim and Tan, 2010)

A solution to the problem of moral hazard can be solved through the creation of a risk based premium. With a risk based premium bankers will no longer act on their own private incentives. They will no longer maximize the riskiness of their assets. Instead, now if bankers want to consider a risk asset portfolio they must balance the increased cost of insuring deposits against the increased benefits of risk, due to their limited-liability stock holders. (Flood, 1993)

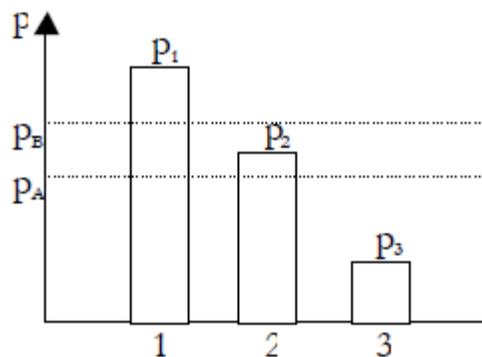
Deposit Insurance and Adverse Selection

Another negative aspect of deposit insurance is an adverse selection problem. Assume that the banking system is represented by three banks ($i=1..3$) with different probabilities of a failure (p_1, p_2, p_3). Let us also assume that an insurance premium is the same for all banks and equals to the average value of

$$p_A = \sum_i p_i$$

individual probabilities of failure

(Mogyl'nyy, 2001)



from this figure we can see that, when an insurance premium equals to p_A , the system proves to be attractive for weaker financial institutions (1,2) and much less attractive to a stronger member of that community (3). A stronger member suffers from adverse selection. It can occur when deposit insurance is voluntary and charges fixed premiums that are not adjusted for the risk peculiar to specific institution (Garcia, 1999). In this situation, the strongest bank is likely to be outside the system. When strong banks withdraw, the premium charged to remaining members has to be raised ($p_A \rightarrow p_B$) to cover the costs of possible bank failures.

The next complication is experienced in the banking system the banking system since a higher premium may persuade the second strongest bank (2) to withdraw until only the weakest bank (1) remains in the deposit insurance system. (Mogyl'nyy, 2001)

An Important matter is the setting of the coverage limit. Having an adequate coverage not only instills public confidence but it also prevents moral hazard which is believed to propagate excessive risk taking by banking institutions. Banks are encouraged to finance high- risk high return projects which in turn may cause more bank failures.

Making Deposit Insurance Effective

Economists need to analyze whether the positive effects of deposit insurance schemes are enough to cover the losses, Due to the hazards associated with such a plan. If it is possible to avoid the problems then policy makers need to make the system effective and reliable. The best practices of deposit insurance throughout the world should be looked at. Doing this will provide a set of incentives that encourage economic agents to keep the financial system stable.

There are a set of recommendations that came from long experience of establishing deposit insurance systems (Garcia, 1999, 2000, Working Group on Deposit Insurance, 2000). The deposit insurance system should be publicly announced and there must be trust in it. The precision of deposit insurance system is the ability to reduce moral hazard, agency and political problems. The main objective of deposit insurance is the defense of small depositors who are unable to monitor performance of financial institution on their own. With this being said not all financial institutions should be included in deposit insurance system. Institutions included in deposit guarantee system should be subject to effective supervision and control. It is important for a supervisory system to be submissive with international norms, especially ones stated in the Basel Accord. With respect to the number of deposit accounts and a percentage of the total value of deposits a coverage limit should be set. In order for the fund to be able to meet all of its liabilities a target level for the fund should be place which is usually articulated as a percentage of total of insured deposits. When the deposit insurance agency is unable to meet its liabilities then it will need additional resources. In this case it will need supplementary sources. It could borrow from the central bank. The deposit insurance agency should be composed of people that does not include bankers or people directly related to banking. The government should play a role but its authorities should not try to take control. Finally the best time to create an explicit deposit insurance scheme is during times when the economy is good. When the economy is in a crisis an implicit scheme or a plan that offers a temporary full guarantee would be better since limited coverage does not prevent bank runs.

Deposit Insurance and Bank Stability

According to Demirguc-Kunt and Kane, a reliable deposit insurance scheme adds to financial stability by making bank runs less likely. On the other hand, deposit insurance can cause excess risk-taking and threaten bank stability in the long run. This can be prevented if capital positions and risk-taking of insured institutions are vigilantly managed.

Demirguc-Kunt and Detragiache (2002) used the World Bank's new cross-country database to study the link between financial crises and deposit insurance. Their results indicated that the countries with the highest coverage limits in the sample (61 countries) are five times more fragile than the countries that impose the lowest coverage limits (less than per capita GDP). Also, it was found that banking crises were more likely where a scheme was administered by government officials rather than jointly or in the private sector. Also, it was found that deposit insurance diminishes banking stability in countries that have poorly developed environments. In conclusion, Demirguc-Kunt and Detragiache found that if an explicit deposit insurance scheme is created in a way that has characteristics that increase moral hazard, then a country will most likely acquire a banking crisis.

Deposit Insurance and Financial Development

A general goal in developing countries is to increase the accomplishments of the formal banking system and to increase the flow of bank credit. This can be done by reducing the customer's doubts about the banking system's capability to redeem depositor claims when a financial institution becomes insolvent. If customers possess more confidence in the banking system, then they will mobilize their savings into banks. These savings can be invested in more proficient ways. A substantial amount of research shows that financial development progresses real investment and there will be a higher level of economic growth. (Levine, 1996) Explicit deposit insurance positively affects the level and vitality of financial activity only if there is strong institutional development. This was found out in a study done by Cull, Senbet, and Sorge (2005) using time-series data for 58 countries.

Deposit Insurance is not enough!

Deposit Insurance cannot by itself be expected to prevent a systematic crisis. Because adequate bank capital is thought to reduce a bank's risk, regulators determine the capital ratio. Since regulators are concerned that banks do not hold enough capital they have raised the capital requirements. If banks hold more capital they can more easily absorb potential losses and are more likely to survive. Capital adequacy regulation acts as a very important role in the long-term financing and solvency positions of banks. It helps banks avoid bankruptcies and cause negative effects on the financial system (Dewatripont and Tirole, 1994). It has been shown that in addition to deposit insurance capital adequacy regulations play a very important role in supporting the incentives of bank owners with depositors and other creditors. (Murinde and Yaseen).

The safety and soundness of the banking systems is important not only because it confines economic declines related to financial panics but also because it avoids unfavorable budgetary costs for governments. The government would often have to handle a major part of the bailout. With regulation banks would be forced to invest wisely to protect the banking system. The bank of international settlements standards of the Basle Accord put a regulation on capital requirements. These requirements would put more of banks capital at risk so they can see for themselves the negative consequences of investing in high risk assets. Capital requirements also lessen moral hazard by putting bank equity at risk. It has been argued by Dewatripont and Tirole, 1994, that the introduction of capital adequacy rules will normally strengthen bank capital and this improve the elasticity of banks to negative shocks.

Chapter 3

Deposit Insurance in the MENA region and the Palestinian Context

Deposit Insurance in the MENA region

There are nine explicit deposit insurance systems in the MENA region. Lebanon had the earliest deposit insurance system (1967) after the failure of the Intra Bank. The system was created to carry out the liquidation process while Bahrain, Oman, Morocco, Sudan, Algeria, Jordan, Turkey and Yemen followed after. Lebanon, Sudan, Algeria, Jordan and Yemen have independent systems while Bahrain, Oman, Morocco and Libya have systems managed by the Central Banks. These countries all have the same public policy objectives which is to protect the less financially and knowledgeable depositors and to help contribute to the stability of the financial system.

The coverage limits vary across the countries in the region depending on the income levels and per capita GDP. Funding for the deposit insurance reserves is provided from ex-post funding, except for in Oman and Bahrain. Reserves are also provided with annual contribution from the treasury of Central Bank. There is a compulsory membership to the deposit insurance system, and all banks are subjected to regulation and supervision by their central banks.

The Case of Jordan

In the year 2000 the parliament of Jordan first adopted a deposit insurance scheme by endorsing a special law. The main public policy objectives of the deposit insurance scheme in Jordan is to encourage savings and strengthen confidence in the banking system. Membership is compulsory for all Jordanian banks and branches of foreign banks in the kingdom. It does not include branches of Jordanian banks operating outside the kingdom. Islamic banks in the kingdom have a voluntary membership. The coverage limit is 50,000 JD and covers total deposits excluding government and interbank's deposits and cash collaterals. Funding for the fund consists of 1 million JD paid by the governments and 100,000 JD paid by each member bank. Annual premiums paid by member banks are at a rate of 2.5 per thousand of the total deposits. Funds are invested in bonds issued by the government of Jordan or deposits with the central bank.

The Jordan deposit insurance corporation is managed and supervised by a board of directors chaired by the governor of the central bank. It has a corporate entity status with financial and administrative independence.

It has the power to reimburse depositors if the central bank of Jordan decides to liquidate a member bank. The insured depositor would be paid within 30 days from submitting a deposit claim. It is also the sole legal

representative of any bank whom liquidation has been decided by the central bank of Jordan. The liquidation proceedings must take place within two years. The JODIC may examine banks annual financial statements and examine banks conditions with approval from the central bank.⁵

The central bank of Jordan has the ultimate responsibility for regulation and overseeing all banking and money market activities. The central bank also reviews the adequacy of provisioning. The failure of the Petra Bank in 1989 caused the central bank to be very strict in regards to capital adequacy. After the collapse of the Petra Bank Jordan as not seen another banking or financial crisis. The central bank of Jordan believes that the capital adequacy ratio set at a minimum of 8% by the bank of international settlements should be higher. The current bank of international settlements ratio is set at 12%.

⁵ http://www.dic.gov.jo/index.php?option=com_content&task=view&id=6&Itemid=10

The Palestinian Context

The International Monetary Fund has stated that the Palestinian economy has undergone tremendous growth in the West Bank and Gaza Strip in the first half of 2010. With a population of less than 4 million by the end of 2009, Palestine is a small and open economy. 62 percent of the population lives in the west bank while the remaining 38 percent lives in the Gaza strip. According to the Palestinian Central Bureau of Statistics (2010) the nominal GDP is estimated to be about 6 billion USD.

Economic performance and growth indicators

The Palestinian economy is a distinctive emerging economy. It does not have its own fiscal and monetary policies and there is no national currency. The government depends on foreign aid, which confines its capability to create fiscal policies that will attain the preferred growth rate.

In 2010 there was a growth rate of real GDP of 93%. When compared to surrounding countries in the same year, this growth was much better than Jordan, which had a real GDP growth rate of 3.1%, Egypt 5.1% and Israel 4.6%.

Palestinian Monetary Authority (PMA)

In 1994, The PMA was established to assist with the legal and regulatory environment and to govern domestic banking. The PMA is the emerging Central Bank of Palestine. It has the authorization power in respect to banking, controlling foreign exchange transactions and regulating the capital market.

The PMA is the Palestinian Authority's sole financial agent, the depository of foreign exchange reserves, and the PA's official economic and financial advisor.

In 2009 the PMA issued instructions regulating paid up capital. The instructions made all banks (national and Foreign) raise their capital to a minimum of 50\$ million US, over two phases: completing the payment of paid of capital to US \$35 million by the end of 2009; and completing the payment of capital to US \$50 million by the end of 2010. The long- term goal is to move minimum capital to US \$100 million. Bank merger operations could help achieve capital requirements.

The minimum capital adequacy ratio adopted by the Palestinian monetary authority is 12%, which is the minimum acceptable ratio by the Basel committee. Foreign banks are required to keep with the PMA at least

21% of their capital as a non- withdrawable capital deposit that should not fall below US \$10 million. Other requirement applied to all banks in Palestine include:

- A required reserve ratio of 9% on customers' deposits in shekel and other currencies in 2010.
- Compulsory reserve included annual deduction amounting to 10% of net income before tax in 2009, and was adjusted to 10% of net income after tax in 2010.
- Voluntary reserve, representing 10% of affiliated net profit after tax.
- Reserve for cyclical changes introduced in 2010 amounted to 15% of net profit after tax, according to PMA regulations for 2011. The amount supports the bank's capital and enables it to withstand risks in the banking sector.

Bank Overview

Following the 1994 signing of the Paris Protocol on Economic Relations between the PNA and Israel, the Palestinian Monetary Authority (PMA) was established as an independent institution to implement and regulate monetary policies in Palestine. In recent years the PMA has begun to restructure itself into a modern and effective central bank. By doing this it will be capable to play an important role in the development and growth of the economy. Since the PMA has strengthened its capacity it will be able to achieve both financial and monetary stability.

Banking Developments

The Palestinian Territories indicates a general improvement in performance for 2009. Services provided by the banks increased at a rate of 15.3% from the previous year, with banks providing the greatest volume of services since 1995, approximately US \$2,109 million. The rate of improvement in providing services exceeded the rise in deposits, as reflected in the rate of facilities to deposits which increased from 31.3% to 34.5% during 2009.⁶

Performance of the Palestinian Banking Sector

The Palestinian banking sector has had many significant achievements in the past years. There was been an increase in the net assets/ liabilities of banks by 6.5% in 2009. This increase was due to the enhanced public confidence in the banking system. The consolidated balance sheets of banks showed an increase and this was

⁶ Overview of the Palestinian Economy
Prepared by: The Palestine Economic Policy Research Institute (MAS) April 2010©

due to an increase in the growth of customer deposits by 7.7% to reach 6.3 billion USD. This number represents 103 percent of the GDP, and is high considering the other countries in the region. (PMA Annual Report 2009)

Despite the unstable environment of Palestine the Palestinian banking system has a good reputation and people are confident in it.

An efficient financial system speeds up the rate of economic development. It does this by guaranteeing that the payment system is functioning competently and gathering savings and improving the provision to investment. (Goaied, 2010). The Palestinian banking system has played a very important role in developing and sustaining the economy. It has also helped fuel growth by assisting the distribution of funds to the best users in the financial system.

Legislative and Regulatory Environment

In 2010 there was the issuance of the New banking law number (9), which switched with the former banking law number (2) for the year 2002. This law talks about the gaps that were in the former law and conforms with the banking systems need to deal with banking developments by putting elements of modernity, inclusiveness and effective frameworks for financial and monetary constancy in compliance with international practices. According to the new law, “the PMA has the right to adopt international standards issued by the Basel committee on banking supervision and other international bodies with respect to banks control, in line with the requirements of the local banking environment, as well as international standard to help it achieve effective banking supervisions in order to maintain a sound, effective and safe banking system.”

The PMA law number (2) for the year 1997 still is in effect and acts as a regulator of the PMA’s purpose, objectives and relations with banks. This law will need to be substituted with a new one when the PMA alters into a central bank. The new law would create a legal structure allowing the PMA to carry out monetary policies, distribute currency and serve as a financial advisor to the state of Palestine.

In a report from March 2011, the international monetary fund expresses that the PMA was ready to transform into a modern central bank. The report also talked about all the PMA’s accomplishments since 2007 and how these changes would allow it to perform the functions of a central bank. The report also stated that in 2010 the PMA made qualitative progress in financial markets infrastructure. Also stated in the report was how the PMA used a wide range of prudential ceilings, including required reserve ratios, minimum capital requirements and liquidity ratios.

Since 2008 all banks are in conformity with directions of the Basel committee. The PMA has also reinforced the supervisory and regulatory framework of its own functions. In May 2010 the PMA released instructions in compliance with Basel II. This would control the disclosure of information by financial institutions.

All weak banks were dealt with in 2010. Al Aqsa Islamic bank was willingly liquidated on March 31st 2010. With supervision from the PMA, the banks portfolio was sold to the Palestine Islamic bank. The Palestine international bank was forcibly liquidated in November 2010 with its banking portfolio sold to Al- Quds bank. Due to these liquidations the number of banks operating in Palestine was 18 banks in 2010.

Customer's deposits grew by 12.1% in 2010 to reach 6.0196 billion USD. 90% of total customer deposits came from the private sector with the remaining 10% from the public sector. Time deposits comprised a value of 4.5 million USD, saving deposits had a value of 174.4 million (an increase of 10.4% from 2009) and current deposits had a value of 326.7 million USD (an increase of 13.9% from 2009).

Three different currencies are used in Palestine: shekel, dinar and dollar. The dollar currency is the leading currency in the composition of customer deposits. The amount of customer deposits in US dollars is 156.2 million (an increase of 5.8% from the previous year of 2009). The amount of savings deposits in USD has decreased because of a decline in interest rates. This decrease in interest rates in 2010 was from the consequence of the global financial crisis and the volatility of the dollar exchange rate against other currencies. Deposits in Jordanian Dinars increased by 65.9 million USD in 2010, making up a total of 27.3% of total customer deposits. The amount of deposits in shekel increased by 263.1 million USD in 2010, making a total of 25.4% of customer deposits.⁷

⁷ Palestine Monetary Authority(PMA), Financial Stability Report (FSR) 2010 ,Research and Monetary Policy Department, July 2011

Chapter 4

Research Methodology

Research Design

The research design used in this research topic is the Exploratory Research design. This design was used due to the fact that there was not much known about this subject matter in Palestine. The topic of Deposit Insurance is new to the country. The only information related to the subject was previous studies done in other regions. Extensive preliminary work was done in order to be familiarized with the subject.

Population and Sample

The population to be considered were the 18 banks in Palestine. From that population a sample of 9 banks were chosen, all of them Commercial banks.

A filtering technique was utilized prior to the distribution of quantitative questionnaires. The first question on the questionnaire was “do you have prior knowledge in deposit insurance?” if the respondent answered yes, then they were allowed to complete the questionnaire. If the respondent replied “no” then they did not complete the questionnaire.

The type of sampling technique used was the Purposive sampling. Purposive sampling is a sampling method in which elements are chosen based on purpose of the study. Questionnaires were only given only to those employees with a background in the field of deposit insurance.

Due to the inability to travel throughout the whole region of Palestine, distribution of questionnaires was limited to the Ramallah and Al - Bireh area. A total of (50) questionnaires were distributed among the banks and PMA.

Methodology

Data Collection:

Primary Data

Primary data was collected through questionnaires and Interviews. The questionnaire was considered structured with pre- specified answer choices. It consisted of five multiple choice questions, thirty questions were placed in the form of a Likert scale to be answered on a scale of Strongly disagree, Disagree, Neutral, Agree and Strongly Agree, and one question based on ranking where (1) represents highest importance and (5) represents lowest importance. The Questionnaires were then analyzed using the SPSS software. Questionnaires were distributed to the Major Commercial banks in the Ramallah area. These banks were selected on the basis that they had the largest amount of customer deposits and were most used among the Palestinian population.

The questionnaires were given to the compliance departments and managers at corresponding banks. The banks that were given questionnaires are as follows: Arab Bank, Bank of Palestine, Palestine Investment Bank, Al Quds Bank, Al Rafah Micro Finance Bank, Jordan Ahli Bank, Bank of Jordan, Cairo Amman Bank and Jordan Kuwait Bank. Questionnaires were also distributed at the Palestinian Monetary Authority in the Control and Supervision department.

Primary qualitative data was also collected from extensive interviews. A thorough interview was conducted with Mohammed Monsara (Vice President of Control and Supervision) at the PMA. Also interviews were conducted with compliance managers at the largest banks including: Moammar Shabib from the Arab Bank, Mr. Saker Jundiah from the Bank of Palestine, and Sami Kreitam from the Cairo Amman Bank.

Secondary Data

Secondary data was collected from various sources, although there was a lack of information due to the lack of previous studies done on this subject in the region.

Data was collected from the Internet (articles, reports, and research reports), Financial Journals, Publications and Investment books.

Reliability and Validity

The most popular test for multipoint-scaled items was used, which is Cronbach's coefficient alpha (Cronbach 1946). This coefficient can vary from 0-1; therefore, the higher the coefficients the more reliable the survey is. Generally an alpha coefficient of 0.7 or 0.8 (Bryman & Cramer, 1990) and higher is acceptable.

Reliability Statistics

Cronbach's Alpha	N of Items
.746	30

Table 4-1

We can see from the above table that reliability is considered acceptable since it was 75% and this percentage is considered to be reasonable for such studies.

To achieve content validity the questionnaire was piloted with three managers and two academics, in which they assessed the survey in terms of its content and clarity. Also, variables and measures used in this study were derived from the literature and experts in this field. This can be seen as verification for achieving content validity.

Chapter 5

Findings and Discussion

Frequency Tables

i. Age

Table 5-1		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	18-25 years old	20	38.5	39.2	39.2
	26-40 years old	26	50.0	51.0	90.2
	41-60 years old	5	9.6	9.8	100.0
	Total	51	98.1	100.0	
Missing	System	1	1.9		
Total		52	100.0		

As can be seen from the above table approximately half of the respondents were between the age of 26 and 40.

ii. Your Job Title

Table 5-2		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	CEO	2	3.8	4.0	4.0
	Middle level manager	10	19.2	20.0	24.0
	First-line manager	6	11.5	12.0	36.0
	Employee	32	61.5	64.0	100.0
	Total	50	96.2	100.0	
Missing	System	2	3.8		
Total		52	100.0		

As can be seen from this table more than half of the respondents were employees.

iii. **Years of Work Experience**

Table 5-3		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	less than 1 year	6	11.5	11.8	11.8
	1-3 years	12	23.1	23.5	35.3
	3-5 years	10	19.2	19.6	54.9
	6-10 years	10	19.2	19.6	74.5
	more than 10 years	13	25.0	25.5	100.0
	Total	51	98.1	100.0	
Missing	System	1	1.9		
Total		52	100.0		

Almost all of the respondents had at least one year of working experience.

iv. **The type of industry your organization belongs to**

Table 5-4		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Service	2	3.8	3.9	3.9
	Banking	46	88.5	90.2	94.1
	Other	3	5.8	5.9	100.0
	Total	51	98.1	100.0	
Missing	System	1	1.9		
Total		52	100.0		

Almost all of the respondents belonged to the banking industry.

The main priority of banking institutions is for them to be safe and sound

Table 5-5		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	2	3.8	3.9	3.9
	Neutral	3	5.8	5.9	9.8
	Agree	23	44.2	45.1	54.9
	Strongly agree	23	44.2	45.1	100.0
	Total	51	98.1	100.0	
Missing	System	1	1.9		
Total		52	100.0		

Palestine's banking system is not undercapitalized

Table 5-6		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly disagree	1	1.9	2.0	2.0
	Disagree	15	28.8	29.4	31.4
	Neutral	17	32.7	33.3	64.7
	Agree	15	28.8	29.4	94.1
	Strongly agree	3	5.8	5.9	100.0
	Total	51	98.1	100.0	
Missing	System	1	1.9		
Total		52	100.0		

As can be seen from (Table 5-5), more than 90% of respondents agreed with the fact the main priority of banking institutions is for them to be safe and sound. This assumes that they believe that banks should always be capitalized in order to prevent bank runs. The minimum acceptable capital adequacy ratio adopted by the PMA is 12%. This is also the minimum acceptable ratio by the Basel Committee. It seems as though respondents did not know this fact, which is why only 35% of them agrees that the banking system is not undercapitalized (Table 5-6).

Benefits of Deposit Insurance

Depositor's risk will be reduced with an effective deposit insurance system

Table 5-7		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	1	1.9	1.9	1.9
	neutral	2	3.8	3.8	5.8
	agree	32	61.5	61.5	67.3
	strongly agree	17	32.7	32.7	100.0
	Total	52	100.0	100.0	

Deposit insurance positively impact the overall financial market

Table 5-8		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	disagree	1	1.9	1.9	1.9
	neutral	6	11.5	11.5	13.5
	agree	34	65.4	65.4	78.8
	strongly agree	11	21.2	21.2	100.0
	Total	52	100.0	100.0	

Deposit insurance can help put off bank runs which will improve financial stability

Table 5-9		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	neutral	11	21.2	21.2	21.2
	agree	37	71.2	71.2	92.3
	strongly agree	4	7.7	7.7	100.0
	Total	52	100.0	100.0	

More than 78% of respondents agreed that Deposit insurance can help put off bank runs which would improve financial stability (table 5-9) and more than 86% of respondents believed that deposit insurance can positively impact the overall financial market (table 5-8). More than 94% of respondents agreed that Depositor's risk will be reduced with an effective deposit insurance system (table 5-7).

The reason for the establishment of the deposit insurance foundation is to create a fund to pool the financial resources to meet the crisis of any bank. The government would not need to be held responsible to compensate depositors and banks would not be left alone in the face of the crisis itself. This would thus increase the stability of the Palestinian banking system and prevent a panic among depositors in the event of a crisis and its implications for the future. Thus, the Palestinian government decided to establish a fund to cover bank losses and failures of banks.

The ceiling of this fund will be 3% of the value of deposits identified after a study between banks. The number of deposits by value of \$ 5000 or less \$ 10,000 and below \$ 15,000 and below and so on were counted. The value of the deposits as a single value despite the currency was calculated. It was seen that \$10,000 was enough to cover a majority of depositors.

Drawbacks of Deposit Insurance

Deposit insurance will increase banks risk taking behavior

Table 5-10		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	1	1.9	2.0	2.0
	disagree	9	17.3	18.4	20.4
	neutral	13	25.0	26.5	46.9
	agree	23	44.2	46.9	93.9
	strongly agree	3	5.8	6.1	100.0
	Total	49	94.2	100.0	
Missing	System	3	5.8		
Total		52	100.0		

With deposit insurance banks are encourage to finance high - risk, high - return projects

Table 5-11		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	3	5.8	5.8	5.8
	disagree	5	9.6	9.6	15.4
	neutral	15	28.8	28.8	44.2
	agree	25	48.1	48.1	92.3
	strongly agree	4	7.7	7.7	100.0
	Total	52	100.0	100.0	

Deposit insurance can cause moral hazard

Table 5-12		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	2	3.8	3.8	3.8
	disagree	8	15.4	15.4	19.2
	neutral	12	23.1	23.1	42.3
	agree	26	50.0	50.0	92.3
	strongly agree	4	7.7	7.7	100.0
	Total	52	100.0	100.0	

- Around 52% of respondents agreed that deposit insurance would increase banks risk taking behavior (table 5-10). In order to prevent bank risk banks currently perform stress tests. These tests measure the ability of banks to withstand risk in the event of a crisis and speculate the banks' ability to deal with crises that can occur. It is based on experience and previous experience on the measurement of capital to the bank's ability to withstand default. The PMA ordered all banks to in June of 2011 to perform stress testing and send the results for a review. The results of the tests were then sent to the board of directors for recommendations in the probability that a crisis could occur. The most important concern of the PMA is to see what could threaten banks capital and what could increase the possibility of a bank defaulting. 57% of respondents believe that deposit insurance can cause moral hazard (table 5-12) and more than 55% believe that with deposit insurance banks are encouraged to finance high- risk, high – return projects (table 5-11). These risks can be reduced with a risk- based premium; banks that take more risk would have to pay a larger premium, which would be an added cost to them. To lessen the cost banks would have to be aware of the amount of risk they take.
- According to the PMA, each bank is required to pay a subscription fee. The Fee is based on the risks of each financial institution. The Bank who controls its risks well and efficiently will pay less and thus be rewarded for his risk properly. The banks that do not manage their risks well will have to pay higher subscription fees and thereby increasing their expenses. This will allow bank's management to perform better risk management in order to reduce the expenses of a higher subscription fee. This will in turn help to increase security and allow banks to increase their deposits and increase revenues.

Deposit Insurance and the banks Customers

Deposit insurance will increase the confidence of people who have deposits in the bank

Table 5-13		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	disagree	1	1.9	2.0	2.0
	neutral	4	7.7	8.0	10.0
	agree	26	50.0	52.0	62.0
	strongly agree	19	36.5	38.0	100.0
	Total	50	96.2	100.0	
Missing	System	2	3.8		
Total		52	100.0		

Deposit insurance will allow more people to trust the banking system

Table 5-14		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	disagree	1	1.9	1.9	1.9
	neutral	4	7.7	7.7	9.6
	agree	30	57.7	57.7	67.3
	strongly agree	17	32.7	32.7	100.0
	Total	52	100.0	100.0	

Having a deposit insurance scheme would allow banks to attract more deposits

Table 5-15		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	disagree	1	1.9	1.9	1.9
	neutral	10	19.2	19.2	21.2
	agree	32	61.5	61.5	82.7
	strongly agree	9	17.3	17.3	100.0
	Total	52	100.0	100.0	

Deposit insurance will increase the amount of savings put in banks

Table 5-16		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	disagree	2	3.8	3.9	3.9
	neutral	12	23.1	23.5	27.5
	agree	31	59.6	60.8	88.2
	strongly agree	6	11.5	11.8	100.0
	Total	51	98.1	100.0	
Missing	System	1	1.9		
Total		52	100.0		

90% of respondents believed that deposit insurance will increase the confidence of people who have deposits in banks (table 5-13). Mohammed Monsara from the PMA believes that the confidence of the people will increase due to world's experience. He believes the trust of people in the banking system is more than 4 years ago because the value of banks deposits has doubled and this indicates a doubling of confidence in the Palestinian banking system. More than 78% of respondents believe that having a deposit insurance scheme would allow banks to attract more deposits (table 5-15). More than 89% of respondents believe that with deposit insurance more customers would trust the banking system (table 5-14). With more trust in the banking system banks would in turn be able to attract more deposits. In (table 5-16) more than 71% of respondents believed that deposit insurance would increase the amount of savings put into banks.

Moammar Shabib from the Arab bank stated that customers of banks have different amounts of confidence and this confidence varies from bank to bank. Customers of a bank get their confidence from the reputation of the bank itself. Also customers get their confidence from the fact that banks have mandatory reserve requirements from regulators.

The Need for Deposit Insurance

Palestine is in need of a deposit insurance scheme

Table 5-17		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	disagree	3	5.8	5.9	5.9
	neutral	6	11.5	11.8	17.6
	agree	34	65.4	66.7	84.3
	strongly agree	8	15.4	15.7	100.0
	Total	51	98.1	100.0	
Missing	System	1	1.9		
Total		52	100.0		

Deposit insurance would be a fundamental part of the nation`s financial system

Table 5-18		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	disagree	4	7.7	7.7	7.7
	neutral	7	13.5	13.5	21.2
	agree	33	63.5	63.5	84.6
	strongly agree	8	15.4	15.4	100.0
	Total	52	100.0	100.0	

Deposit insurance would provide stability to the banking sector

Table 5-19		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	disagree	2	3.8	3.8	3.8
	neutral	6	11.5	11.5	15.4
	agree	31	59.6	59.6	75.0
	strongly agree	13	25.0	25.0	100.0
	Total	52	100.0	100.0	

During an interview with Mr. Moammar Shabib he believed that Palestine is not ready for Deposit insurance and that the state may not even be ready for it. He believes this because there is still no political and economic stability and the fact that there is a payroll problem. If international donors don't provide the state of Palestine with money then everything in Palestine would stop. Moammar believes that conditions are not just right yet. Despite Mr. Moammar's opinion, 80% of the sample believed that Palestine was indeed ready for a deposit insurance scheme, and the PMA also believes that Palestine is ready too (table 5-17). 78% of the respondents also agree that deposit insurance would be a fundamental part of the nation's financial system (table 5-18). More than 84% of the sample agrees that deposit insurance would provide stability to the banking sector (table 5-19).

A system of deposit insurance would be expensive

Table 5-20		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	disagree	3	5.8	5.8	5.8
	neutral	11	21.2	21.2	26.9
	agree	24	46.2	46.2	73.1
	strongly agree	14	26.9	26.9	100.0
	Total	52	100.0	100.0	

As can be seen from the table above (table 5-20) 72% of respondents agree that deposit insurance would be expensive. It would be expensive for banks that take a lot of risk and are paying a risk – based premium to be part of the deposit insurance scheme. In order to handle the costs of deposit insurance, banks are most likely going to transfer this cost to their customers (depositors). If a depositor was originally getting 3% interest in their deposit, now with a deposit insurance scheme they may only get 2.7% interest on their deposit.

It would be important to make sure that a deposit insurance system is transparent

Table 5-21		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	disagree	1	1.9	2.0	2.0
	neutral	7	13.5	13.7	15.7
	agree	24	46.2	47.1	62.7
	strongly agree	19	36.5	37.3	100.0
	Total	51	98.1	100.0	
Missing	System	1	1.9		
Total		52	100.0		

More than 84% of respondents of the questionnaire agreed that it is important that a deposit insurance system is transparent. This means that a deposit insurance scheme should have a great amount of awareness. At the current time in Palestine there is something known as implicit deposit insurance. It would be up to the government to cover the deficit in the bank deposits in case of the bankruptcy of a bank, as happened with the Palestine International Bank in 2010. This implicit deposit insurance was not publicized, but this is what prevailed until today.

The main objective of deposit insurance would be to protect small depositors who are unable to monitor the financial performance of financial institutions on their own.

Table 5-22		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	1	1.9	2.0	2.0
	disagree	2	3.8	3.9	5.9
	neutral	8	15.4	15.7	21.6
	agree	28	53.8	54.9	76.5
	strongly agree	12	23.1	23.5	100.0
	Total	51	98.1	100.0	
Missing	System	1	1.9		
	Total	52	100.0		

Approximately 85% of respondents believed that deposit insurance’s main objective would be to protect small depositors who are unable to monitor the financial performance of financial institutions on their own (table 5-22). According to the PMA, they would cover the largest proportion of accounts and not the value of the accounts; as it is at the responsibility to cover the largest number of possible depositors, not the value of deposits. A depositor may have a deposit of one million dollars, but it is not necessarily to be from the first reimbursed. The first do be compensated should be small depositors because it is the ultimate responsibility and goal to protect small depositors.

When the number of depositors in banks were counted whose deposit s had a value of \$ 10,000 it was found that these make up 90% of the sum of all depositors. After taking the value for each bank separately, it was found that the biggest bank that could go bankrupt in any day and that a ceiling of \$10,000 is enough to cover the depositors who had deposits of \$ 10,000 or less.

It is possible that the ceiling of the fund of 3% can change. If there is an increase in the fund it is possible for the ceiling to increase, a decrease in the fund would allow the ceiling to decrease. The availability of coverage is calculated using an accurate and clear scientific issued by the Basel Committee. It is also possible for the deposit coverage amount of \$ 10,000 to change based on how much money is collected from fund from year to year and the power of the management in the Deposit insurance institution.

Where money for a deposit insurance fund would be collected from?

Table 5-23		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Palestinian national authority	12	23.1	24.5	24.5
	Premium collected from member banks	17	32.7	34.7	59.2
	Government borrowing	6	11.5	12.2	71.4
	An initial loan from the government for start-up capital	9	17.3	18.4	89.8
	Other	5	9.6	10.2	100.0
	Total	49	94.2	100.0	
Missing	System	3	5.8		
Total		52	100.0		

When asked where money for a deposit insurance fund should be collected from, 24.5% of respondents chose the Palestinian national authority, 34.7 % chose premiums collected from other banks, 12.25 chose government borrowing and 18.4 % chose an initial loan from the government for start- up capital. According to the draft law created by the PMA there will be a contribution from the government and all the rest of the money for the fund will be provided by banks is an annual subscription fee.

What currencies would a deposit insurance fund cover?

Table 5-24		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Shekels	4	7.7	7.7	7.7
	Dinars	1	1.9	1.9	9.6
	Dollars	3	5.8	5.8	15.4
	All of the above	38	73.1	73.1	88.5
	a & b	2	3.8	3.8	92.3
	a & c	3	5.8	5.8	98.1
	other	1	1.9	1.9	100.0
	Total	52	100.0	100.0	

More than 78% of the sample agrees that all types of currencies should be covered a deposit insurance scheme (table 5-24). The PMA has studied most systems of deposit insurance around the world and the most important success at the global level in this subject was in Britain, Germany and Italy. Some countries covered deposits in local currencies only, and others in all currencies.

Since that Palestine does not have local currency the PMA is forced to guarantee deposits in all currencies. This will encourage deposits in the local currency and reduce the foreign exchange trading. If in the future Palestine does have its own local currency the deposit insurance will then only cover the Palestinian currency.

In case of bank failure up to how much of depositor`s money should be covered?

Table 5-25		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Up to \$1000	4	7.7	7.8	7.8
	Between \$3001 - \$5000	4	7.7	7.8	15.7
	Between \$5001 - \$7000	5	9.6	9.8	25.5
	Between \$7001 - \$9000	5	9.6	9.8	35.3
	Between \$9001 - \$11000	6	11.5	11.8	47.1
	Between \$11001 - \$13000	3	5.8	5.9	52.9
	Between \$13001 - \$15000	15	28.8	29.4	82.4
	other	9	17.3	17.6	100.0
	Total	51	98.1	100.0	
Missing	System	1	1.9		
Total		52	100.0		

When asked in the questionnaire how much of depositors money should be covered 29.4% of respondents picked from \$ 13,000 – \$15,000 and 11.8% picked between \$9,000- \$11,000. According to the PMA the ceiling coverage as defined in the draft, is \$ 10,000, but this ceiling is in the process of review in order to make sure that the balance of the Fund after it is created is enough or more than this ceiling in the case of coverage.

What do you consider to be the most important preconditions that need to be fulfilled before an implementation of a deposit insurance scheme? (1 is considered to be most important, and 5 is considered least important).

	#
Evaluation of the economy and health of the banking system	1
Macroeconomic stability (long-term stability in the inflation rate, reduction in the interest rates)	2
Sound governance of agencies involving the financial safety net	4
Strong regulation and supervision	3
Sound accounting and disclosure management	5

Table 5-26

As can be seen from the table above (5-26) the respondents believed that the most important precondition for Deposit Insurance was the evaluation and health of the banking system. The next most important precondition was considered to be macroeconomic stability. Strong regulation and supervision was considered the third most important precondition.

Discussion of findings from Interviews:

From my interviews at the PMA and Commercial banks, it was found that The PMA is now working to establish a deposit insurance corporation.

Deposit insurance is one of the three components of the financial safety net. The first component is a strong regulatory authority. The second component is the lender of last resort function and the third component is the existence of an institution to guarantee deposits when needed.

The first thing the PMA did was assess the internal work environment and the banking system. It was found that the environment is now ready and poised for the establishment of a deposit insurance scheme. This scheme would be established with the help of financing from the World Bank. After that, actual procedures were started for the establishment of this Foundation and lists of procedures were made with an internal working draft of the law. A lot of time and effort was put into making this new law and it was looked at from several different directions. When the law was finalized and ready it was sent to the Cabinet for approval and approved by the President.

After the completion of the draft the Internal Audit Department distributed the draft to other departments of the Monetary Authority. It was then reviewed with legal experts to make sure that there is no conflict between the text of the law of deposit insurance and other laws such as the Companies Act and the Banking Act. The PMA then had a new bill which was sent to the banks as they are the key partners in the banking deposit Insurance Corporation.

Banks were given a period of two weeks' time to study the draft and give their feedback. The PMA then organized a meeting with all the banks which are perceived to be a part of the deposit insurance system and discuss all the related issues to make sure it does not conflict with the state of law and matches the basic principles in the designing an effective deposit insurance system. These basic principles came from the Basel Committee – International Banking Supervision-.

The PMA introduced the final observations about the draft and made them part of the law after the draft was assessed by the external and internal legal chancellors. Legal notices of the amendments were made and the final version will be presented to the board of directors and the PMA on April 11th. A certified copy that is approved by management will be presented to the Council of Ministers - on the legislative plan of the government - . A committee composed of 28 legal counsels acting on behalf of the Legislative Council will talk on the compatibility of this new law with all existing laws and try to eliminate any conflict of legal texts. The law will be sent to the Cabinet and then within 6 months it will be sent to the President for his signature.

What are the benefits of deposit insurance?

Table (5-27): The benefits of deposit insurance.

	Mean		Std. Deviation
	Statistic	Std. Error	Statistic
The main priority of banking institutions is for them to be safe and sound	4.3137	.10661	.76132
Depositor's risk will be reduced with an effective deposit insurance system	4.2308	.09754	.70336
Deposit insurance positively impact the overall financial market	4.0577	.08862	.63904
Deposit insurance can help put off bank runs which will improve financial stability	3.8654	.07281	.52502
Deposit insurance makes all insured institutions uniformly attractive and always safe	3.7115	.10398	.74981
Deposit insurance will increase the confidence of people who have deposit in the bank	4.2600	.09819	.69429
Deposit insurance will allow more people to trust the banking system	4.2115	.09246	.66676
Deposit insurance would provide stability to the banking sector	4.0577	.10058	.72527
The main objective of deposit insurance would be to protect small depositors who are unable to monitor the financial performance of financial institutions on their own	3.9412	.12017	.85818
Having a deposit insurance scheme would allow banks to attract more deposits	3.9423	.09278	.66902
Deposit insurance will increase the amount of savings put in banks	3.8039	.09709	.69339
Valid N (list wise)			

As table (5-27) shows, we can imply the benefits of deposit insurance according to respondents. As the mean in all cases is more than 3, (mean >3). So the answers are more agree and strongly agree for the questions for this part. Then we can have the benefits from the deposit insurance as all in the table.

What are the disadvantages from the deposit insurance?

Table (4-29): Disadvantage of deposit insurance.

	Mean		Std. Deviation
	Statistic	Std. Error	Statistic
Deposit insurance can cause moral hazard.	3.4231	.13550	.97711
Deposit insurance can cause an adverse selection problem.	3.3529	.15036	1.07375
A system of deposit insurance would be expensive.	3.9423	.11784	.84976
Deposit insurance will increase banks risk taking behavior.	3.3673	.13265	.92857
With deposit insurance banks are encourage to finance high - risk, high - return projects.	3.4231	.13550	.97711
Valid N (list wise)			

As table (5-28) shows, we can imply the disadvantages of deposit insurance according to respondents. The mean in all cases is more than 3, (mean >3). So the answers are more agree and strongly agree for the questions of this part.

Is deposit insurance needed in Palestine?

Table (5-29): The need for deposit insurance.

	N	Mean		Std. Deviation
	Statistic	Statistic	Std. Error	Statistic
Palestine's banking system is not undercapitalized.	51	3.0784	.13385	.95589
Deposit insurance would be a fundamental part of the nation`s financial system.	52	3.8654	.10646	.76770
There is a need for deposit insurance in Palestine.	52	4.2308	.09359	.67491
Valid N (list wise)	50			

As table (5-29) shows, we can imply the need for deposit insurance according to respondents. As the mean in all cases is more than 3, (mean >3). So the answers are more agree and strongly agree for the questions for this part.

Chapter 6

Conclusions and Recommendations

Conclusions

The purpose of this study was to see if there was a need for the establishment of a deposit insurance scheme in Palestine. Customer's deposits are the main source of external funds. The amount of deposits in Palestinian banks grew by 8% in 2010 to reach 6.8 US billion dollars. This increase in customer deposits shows that there is a high degree of public confidence in the banking system of Palestine. It also shows that there is a constant flow of savings into the banking system.

With the hard work of the Palestinian monetary authority a well functioning banking system has been created. Palestine Monetary Authority Governor Dr. Jihad al Wazeer has created structures that permit banks to work in complicated situations. There is a strong regulatory and supervisory system that helps prevent the banks from external (international financial crises) and internal shocks. The Palestinian monetary authority and the World Bank have a strong partnership, which will help to create a future strong central bank. With the new banking law the confidence of international and regional institutions in the Palestinian banking system will proliferate.

Deposit insurance once adopted in Palestine will be based on the principles issued by the Basel Committee. It will not guarantee people's deposits, except in the case of liquidation of the bank and this means that the deposit insurance institution will only be active and have a role only in case of default or liquidation of the banks. The role of the Palestinian government under a new explicit deposit insurance scheme would not be the addressing of faltering banks but to address the problem of the entire sector. The government would intervene after the banks problems were transferred to the entire banking and financial sector and to prevent the occurrence of a crisis.

Regarding the concerns about deposit insurance and added risk -taking by banks, the PMA now has the right to adopt international standards issued by the Basel committee on banking supervision. This will make sure that banks are in -line with the requirements of the local banking environment.

In conclusion I Believe that Palestine is ready and in need of a Deposit Insurance scheme. The banking sector of Palestine is one of the most important components of the Palestinian financial system. Making sure that the banking sector is stable and secure will affect the financial stability of Palestine as a whole. Despite the fact that a coverage amount of 10,000\$ doesn't seem very much, it sure is better than nothing. It is best that the PMA starts now with something rather than start never. The PMA at this time is more

than ready. It has experienced a modification in the past three years in terms of its institutional structures. It has reinforced the supervisory and regulatory framework of its own operations and advanced towards the execution of Basel II. The changes made in the PMA along with the improved economic conditions in Palestine have played a part to the increasing development of the banking system.

Recommendations

The following are a list of recommendations that can be applied towards the implementation of a deposit insurance scheme in Palestine.

Recommendations for the Palestinian monetary authority and the implementation of the Deposit Insurance scheme itself.

- The deposit insurance scheme should be independent in operations and administration but at the same time a fundamental part of the financial safety net. When the scheme carries out functions it should work with the Palestinian Monetary Authority.
- The ultimate aim of the deposit insurance scheme should be to protect the stability of the system and to protect consumers because they lack the ability to evaluate the risk of banks on their own.
- The main functions of deposit insurance should be: confidence, protection, security, financing and support.
- Membership should be compulsory for all deposit taking institutions. These institutions should be supervised and all applicable and dependable information about them should be shared with the general public through annual reports and publications.
- The deposit insurance scheme should act as a supervisory body by providing controlled liquidation to the financial institutions that have become insolvent.
- The deposit insurance scheme should be designed to reduce moral hazard. This can be done with a risk-based premium. Banks will then not think of acting on behalf of themselves and won't increase the riskiness of their assets. If the banks take on more risk they will be charged a higher premium.
- The coverage levels should be reviewed so that it promotes financial stability. If the coverage level is too high that can cause moral hazard.
- It is significant to ensure that deposit insurance funds are always adequate so that financing requirements can be met immediately. Planning should be done to see the capability of making a punctual payout.
- Benchmarks should be made to monitor the efficiency of the scheme. Any gaps and deficiencies should be quickly brought to attention and handled promptly.
- The PMA should tighten up its control and supervisions to a greater extent over all Banks. Stress tests should be performed regularly and results should be shared not just with the banks but also with the general public in the form of publications. This will boost the people's confidence in the banking system.
- All achievements made by the PMA showing its success should be shared, not just with regional institutions but internationally as well.

Recommendations for Commercial Banks in Palestine

- Upon the liquidation of the troubled financial institutions there should be the quick and timely payment of the covered deposits to customers. After a customer files a claim they should receive the insured covered amount within 30 days.
- Contributions by banks to support the Deposit insurance fund should be fair. Any institutions that have higher risk should pay a higher contribution to the fund. There should be a risk -based premium.
- The scheme needs the ability to have a great deal of power to make sure all financial institutions make their contributions and to guarantee the fast and inclusive payout of all covered deposits.
- There should be a great deal of transparency with the implementation of a deposit insurance scheme. It is important to communicate the purpose and the aims of the deposit insurance scheme to the general public. The deposit insurance coverage, limits and types of deposits that are insured should be clearly defined.
- Savings adds to the amount of capital collection in the economy and shows how much of private savings can be used to fund investment. Savings also shows the achievements of the banking system from the perspective of the financial intermediation process. Since savings are a key factor in increasing investment activity, banks should find a way to get people to increase the amount of their savings placed into banks.
- To increase customer's motivation to deposit money, banks should use offerings and promotional campaigns to draw in the deposits of small savers. Banks need to find a way to get customers to place their money in savings deposits instead of shares in the financial markets or buying real property or land so as to preserve the real value of money.
- Since the main purpose of Deposit insurance is to protect customers the deposits that should be covered should include: current, savings and time deposits.

The most important thing to keep in mind is that the state of Palestine is unique. It is not possible to copy and paste a scheme from other countries and adopt it here. The scheme must be structured in a way to match and be appropriate with the countries characteristics and unique circumstances so that it works in the most efficient way.

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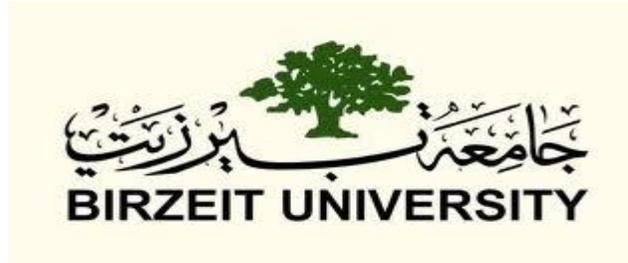
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Appendix

Questionnaire

Complete List of Frequency Tables



Thesis Topic: Protecting Depositors in Palestine. Is there a need for the Establishment of Deposit Insurance?

إقرار الاستقرار المالي وحماية المودعين في فلسطين. هل هناك حاجة لإنشاء تأمين على الودائع؟

Purpose of this Research Study: There isn't an individual that wouldn't like to know that their savings is protected. Like any other business, banks and other financial institutions can fail. Consequently deposit insurance is needed to provide an effective and necessary way to achieve financial safety. Deposit insurance is the main way to assure the safekeeping of a depositor's money. The danger exists in the fact that if banks' customers feel that their bank is having some kind of financial problems, due to borrowers defaulting on loans, and their incentive is to get their money out while they still can. When banks depositors do this all at once it is said that there is a run on the bank. Because a bank only holds a part of the total funds on reserve, not everyone will be able to get their money. When the bank has no more cash left on hand it has no choice but to go out of business. The purpose of this study is to see if there is a need for the establishment of Deposit Insurance in Palestine.

Dear Participants: My name is Shireen Esmail. I am a teacher's assistant in the Finance Department at Birzeit University. As an MBA student and Birzeit University one of my final requirements is to prepare a Final thesis dissertation.

I hope you will take the time to complete this questionnaire and return it. I guarantee that your responses will not be identified with you personally and that your responses are strictly confidential.

If you have any questions or concerns about completing the questionnaire, you may contact me at 0598-90-97-90 or at sesmail@birzeit.edu

Thank you in advance.

Do you have prior knowledge in the Field of Deposit Insurance? Yes no

If you replied “yes” to the above question you may continue filling out the questionnaire. If you replied “no”, then thank you, but your help is no longer needed.

Part 2: Participant Profile

Instructions: Please choose the most suitable answer.

1. Your Age:

- A. 18-25 years old
- B. 26- 40 years old
- C. 41- 60 years old
- D. Over the age of 61

2. Your Job title:

- A. CEO
- B. Middle level manager
- C. First-Line Manager
- D. Employee
- E. Other (Please Specify)

3. Years of Work experience:

- A. Less than 1 year
- B. 1-3 years
- C. 3-5 years
- D. 6-10 years
- E. More than 10 years

4. The type of industry your organization belongs to:

- A. Service
- B. Manufacturing
- C. Investment
- D. Banking
- E. Pharmaceuticals
- F. Telecommunications
- G. Other (please Specify)

Part 3:

Instructions: Please place a (v) in the appropriate space. Choose a number between 1 (strongly agree) and 5 (strongly disagree) to show how strong your belief is.

	Strongly Agree (1)	Agree (2)	Neutral (3)	Disagree (4)	Strongly Disagree (5)
1. The main priority of banking institutions is for them to be safe and sound					
2. Palestine’s banking system is not undercapitalized.					
3. There is Macroeconomic stability in Palestine.					
4. Depositor’s risk will be reduced with an effective deposit insurance system.					
5. Deposit insurance positively impacts the overall financial markets.					
6. Deposit insurance can help put off bank runs which will improve financial stability					
7. Deposit insurance will increase banks risk taking behavior					
8. With deposit insurance banks are encouraged to finance high - risk, high- return projects.					
9. Deposit insurance makes all insured institutions uniformly attractive and always safe.					
10. Deposit Insurance can cause moral hazard.					
11. Deposit insurance can cause an adverse selection problem					
12. Deposit insurance will increase the confidence of the people who have deposits in the bank.					
13. Deposit insurance will allow more people to trust the banking system					
14. A system of deposit insurance would be expensive.					
15. Deposit insurance would be a fundamental part of the nation’s financial system.					
16. Palestine is in need of a deposit insurance scheme.					
17. Deposit insurance would provide stability to the banking sector.					
18. The positive effects of deposit insurance schemes are more than the negative effects.					

19. The main objective of deposit insurance would be to protect small depositors who are unable to monitor the financial performance of financial institutions on their own.					
	Strongly Agree (1)	Agree (2)	Neutral (3)	Disagree (4)	Strongly Disagree (5)
20. Not all financial institutions should be included in a deposit insurance scheme.					
21. Having a deposit insurance scheme would allow banks to attract more deposits.					
22. A deposit insurance system should be a legally separate organization.					
23. A deposit insurance system should be part of the central bank					
24. Coverage included in a deposit insurance scheme should include demand and saving deposits.					
25. Being part of a deposit insurance system should be voluntary for banks.					
26. All types of currencies should be covered a Deposit insurance scheme.					
27. Deposit Insurance will increase the amount of savings put in Banks.					
28. It would be important to make sure that a Deposit Insurance system is transparent .					
29. The joining of banks to a deposit insurance scheme should be Mandatory.					
30. There is a need for Deposit Insurance in Palestine.					

Part 4:

Instructions: Please choose an answer that you most agree with.

1. How confident do you believe people (depositors) are with banks in Palestine?

- A. Very Confident
- B. Somewhat Confident
- C. Not confident

2. Where would money for a deposit insurance fund be collected from?

- A. Palestinian National Authority
- B. Premium collected from member banks
- C. Government borrowing
- D. An Initial loan from the government for start- up capital
- E. Other (Please Specify)_____

3. What currencies would a deposit insurance fund cover?

- A. Shekels
- B. Dinars
- C. Dollars
- D. All of the above
- E. A & B
- F. A & C
- G. Other (Please Specify)_____

4. In case of Bank Failure up to how much of depositor's money should be covered?

- A. Up to \$1000
- B. Between \$1001- \$3000
- C. Between \$3001- \$5000
- D. Between \$5001- \$7000
- E. Between \$7001- \$9000
- F. Between \$9001- \$11,000
- G. Between \$11,001- \$13,000
- H. Between \$13,001- \$15,000
- I. Other (Please Specify)_____

5. In case of a bank failure how long should it take for depositors to be re-imbursed?

- A. Within a few days
- B. Within a month
- C. Within 3 months
- D. Within 6 months
- E. Within 1 year
- F. Other (Please Specify)_____

Part 5

Instructions: Please rate the following points, where **1** is considered to be **most important** and **5** is considered **least important**.

What do you consider to be the most important preconditions that need to be fulfilled before an implementation of a deposit insurance scheme?

_____ Evaluation of the economy and health of the banking system.

_____ Macroeconomic stability (long-term stability in the inflation rate, reduction in the interest rates)

_____ Sound governance of agencies involving the financial safety net.

_____ Strong regulation and supervision.

_____ Sound accounting and disclosure management.

Part 5: Open ended questions

1. In your opinion, is Palestine in need of a Deposit Insurance System? Why or why not?

2. Is Palestine ready for a deposit Insurance system? Why or why not?

3. Do you see Palestine heading towards a financial crisis in the near future?

4. What do you think are some risks associated with Deposit Insurance?

5. What should be the objectives of a Deposit Insurance scheme? _____

Frequency Tables

Age

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	18-25 years old	20	38.5	39.2	39.2
	26-40 years old	26	50.0	51.0	90.2
	41-60 years old	5	9.6	9.8	100.0
	Total	51	98.1	100.0	
Missing	System	1	1.9		
Total		52	100.0		

Your Job Title

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	CEO	2	3.8	4.0	4.0
	Middle level manager	10	19.2	20.0	24.0
	First-line manager	6	11.5	12.0	36.0
	Employee	32	61.5	64.0	100.0
	Total	50	96.2	100.0	
Missing	System	2	3.8		
Total		52	100.0		

Years of Work Experience

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	less than 1 year	6	11.5	11.8	11.8
	1-3 years	12	23.1	23.5	35.3
	3-5 years	10	19.2	19.6	54.9
	6-10 years	10	19.2	19.6	74.5
	more than 10 years	13	25.0	25.5	100.0
	Total	51	98.1	100.0	
Missing	System	1	1.9		
Total		52	100.0		

The type of industry your organization belongs to

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Service	2	3.8	3.9	3.9
	Banking	46	88.5	90.2	94.1
	Other	3	5.8	5.9	100.0
	Total	51	98.1	100.0	
Missing	System	1	1.9		
Total		52	100.0		

1. The main priority of banking institutions is for them to be safe and sound

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Disagree	2	3.8	3.9	3.9
	Neutral	3	5.8	5.9	9.8
	Agree	23	44.2	45.1	54.9
	Strongly agree	23	44.2	45.1	100.0
	Total	51	98.1	100.0	
Missing	System	1	1.9		
Total		52	100.0		

2. Palestine's banking system is not undercapitalized

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Strongly disagree	1	1.9	2.0	2.0
	Disagree	15	28.8	29.4	31.4
	Neutral	17	32.7	33.3	64.7
	Agree	15	28.8	29.4	94.1
	Strongly agree	3	5.8	5.9	100.0
	Total	51	98.1	100.0	
Missing	System	1	1.9		
Total		52	100.0		

There is macroeconomics stability in Palestine

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid strongly disagree	2	3.8	3.8	3.8
disagree	16	30.8	30.8	34.6
neutral	13	25.0	25.0	59.6
agree	19	36.5	36.5	96.2
strongly agree	2	3.8	3.8	100.0
Total	52	100.0	100.0	

Depositor's risk will be reduced with an effective deposit insurance system

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid strongly disagree	1	1.9	1.9	1.9
neutral	2	3.8	3.8	5.8
agree	32	61.5	61.5	67.3
strongly agree	17	32.7	32.7	100.0
Total	52	100.0	100.0	

Deposit insurance positively impact the overall financial market

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid disagree	1	1.9	1.9	1.9
neutral	6	11.5	11.5	13.5
agree	34	65.4	65.4	78.8
strongly agree	11	21.2	21.2	100.0
Total	52	100.0	100.0	

Deposit insurance can help put off bank runs which will improve financial stability

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	neutral	11	21.2	21.2	21.2
	agree	37	71.2	71.2	92.3
	strongly agree	4	7.7	7.7	100.0
	Total	52	100.0	100.0	

Deposit insurance will increase banks risk taking behavior

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	1	1.9	2.0	2.0
	disagree	9	17.3	18.4	20.4
	neutral	13	25.0	26.5	46.9
	agree	23	44.2	46.9	93.9
	strongly agree	3	5.8	6.1	100.0
	Total	49	94.2	100.0	
Missing	System	3	5.8		
Total		52	100.0		

With deposit insurance banks are encourage to finance high - risk, high - return projects

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	3	5.8	5.8	5.8
	disagree	5	9.6	9.6	15.4
	neutral	15	28.8	28.8	44.2
	agree	25	48.1	48.1	92.3
	strongly agree	4	7.7	7.7	100.0
	Total	52	100.0	100.0	

Deposit insurance makes all insured institutions uniformly attractive and always safe

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid disagree	4	7.7	7.7	7.7
neutral	12	23.1	23.1	30.8
agree	31	59.6	59.6	90.4
strongly agree	5	9.6	9.6	100.0
Total	52	100.0	100.0	

Deposit insurance can cause moral hazard

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid strongly disagree	2	3.8	3.8	3.8
disagree	8	15.4	15.4	19.2
neutral	12	23.1	23.1	42.3
agree	26	50.0	50.0	92.3
strongly agree	4	7.7	7.7	100.0
Total	52	100.0	100.0	

Insurance can cause an adverse selection problem

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid strongly disagree	2	3.8	3.9	3.9
disagree	10	19.2	19.6	23.5
neutral	14	26.9	27.5	51.0
agree	18	34.6	35.3	86.3
strongly agree	7	13.5	13.7	100.0
Total	51	98.1	100.0	
Missing System	1	1.9		
Total	52	100.0		

Deposit insurance will increase the confidence of people who have deposit in the bank

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	disagree	1	1.9	2.0	2.0
	neutral	4	7.7	8.0	10.0
	agree	26	50.0	52.0	62.0
	strongly agree	19	36.5	38.0	100.0
	Total	50	96.2	100.0	
Missing	System	2	3.8		
Total		52	100.0		

Deposit insurance will allow more people to trust the banking system

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	disagree	1	1.9	1.9	1.9
	neutral	4	7.7	7.7	9.6
	agree	30	57.7	57.7	67.3
	strongly agree	17	32.7	32.7	100.0
	Total	52	100.0	100.0	

A system of deposit insurance would be expensive

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	disagree	3	5.8	5.8	5.8
	neutral	11	21.2	21.2	26.9
	agree	24	46.2	46.2	73.1
	strongly agree	14	26.9	26.9	100.0
	Total	52	100.0	100.0	

Deposit insurance would be a fundamental part of the nation`s financial system

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid disagree	4	7.7	7.7	7.7
neutral	7	13.5	13.5	21.2
agree	33	63.5	63.5	84.6
strongly agree	8	15.4	15.4	100.0
Total	52	100.0	100.0	

Palestine is in need of a deposit insurance scheme

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid disagree	3	5.8	5.9	5.9
neutral	6	11.5	11.8	17.6
agree	34	65.4	66.7	84.3
strongly agree	8	15.4	15.7	100.0
Total	51	98.1	100.0	
Missing System	1	1.9		
Total	52	100.0		

Deposit insurance would provide stability to the banking sector

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid disagree	2	3.8	3.8	3.8
neutral	6	11.5	11.5	15.4
agree	31	59.6	59.6	75.0
strongly agree	13	25.0	25.0	100.0
Total	52	100.0	100.0	

The positive effects of deposit insurance schemes are more than the negative effects

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid disagree	1	1.9	1.9	1.9
neutral	13	25.0	25.0	26.9
agree	27	51.9	51.9	78.8
strongly agree	11	21.2	21.2	100.0
Total	52	100.0	100.0	

The main objective of deposit insurance would be to protect small depositors who are unable to monitor the financial performance of financial institutions on their own.

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid strongly disagree	1	1.9	2.0	2.0
disagree	2	3.8	3.9	5.9
neutral	8	15.4	15.7	21.6
agree	28	53.8	54.9	76.5
strongly agree	12	23.1	23.5	100.0
Total	51	98.1	100.0	
Missing System	1	1.9		
Total	52	100.0		

Not all financial institutions should be included in a deposit insurance scheme

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid strongly disagree	5	9.6	9.6	9.6
disagree	18	34.6	34.6	44.2
neutral	9	17.3	17.3	61.5
agree	18	34.6	34.6	96.2
strongly agree	2	3.8	3.8	100.0
Total	52	100.0	100.0	

Having a deposit insurance scheme would allow banks to attract more deposit

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid disagree	1	1.9	1.9	1.9
neutral	10	19.2	19.2	21.2
agree	32	61.5	61.5	82.7
strongly agree	9	17.3	17.3	100.0
Total	52	100.0	100.0	

A deposit insurance system should be a legally separate organization

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid strongly disagree	1	1.9	2.0	2.0
disagree	4	7.7	8.0	10.0
neutral	1	1.9	2.0	12.0
agree	34	65.4	68.0	80.0
strongly agree	10	19.2	20.0	100.0
Total	50	96.2	100.0	
Missing System	2	3.8		
Total	52	100.0		

A deposit insurance system should be a part of the central bank

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid strongly disagree	2	3.8	3.8	3.8
disagree	9	17.3	17.3	21.2
neutral	11	21.2	21.2	42.3
agree	20	38.5	38.5	80.8
strongly agree	10	19.2	19.2	100.0
Total	52	100.0	100.0	

Coverage included in a deposit insurance system should include demand and saving deposit

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	disagree	3	5.8	5.9	5.9
	neutral	8	15.4	15.7	21.6
	agree	32	61.5	62.7	84.3
	strongly agree	8	15.4	15.7	100.0
	Total	51	98.1	100.0	
Missing	System	1	1.9		
Total		52	100.0		

Being part of a deposit insurance system should be voluntary for banks

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	5	9.6	10.0	10.0
	disagree	8	15.4	16.0	26.0
	neutral	9	17.3	18.0	44.0
	agree	23	44.2	46.0	90.0
	strongly agree	5	9.6	10.0	100.0
	Total	50	96.2	100.0	
Missing	System	2	3.8		
Total		52	100.0		

All types of currencies should be covered a deposit insurance scheme

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	strongly disagree	1	1.9	1.9	1.9
	disagree	4	7.7	7.7	9.6
	neutral	6	11.5	11.5	21.2
	agree	31	59.6	59.6	80.8
	strongly agree	10	19.2	19.2	100.0
	Total	52	100.0	100.0	

Deposit insurance will increase the amount of savings put in banks

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	disagree	2	3.8	3.9	3.9
	neutral	12	23.1	23.5	27.5
	agree	31	59.6	60.8	88.2
	strongly agree	6	11.5	11.8	100.0
	Total	51	98.1	100.0	
Missing	System	1	1.9		
Total		52	100.0		

It would be important to make sure that a deposit insurance system is transparent

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	disagree	1	1.9	2.0	2.0
	neutral	7	13.5	13.7	15.7
	agree	24	46.2	47.1	62.7
	strongly agree	19	36.5	37.3	100.0
	Total	51	98.1	100.0	
Missing	System	1	1.9		
Total		52	100.0		

The joining of banks to a deposit insurance scheme should be mandatory

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	disagree	4	7.7	7.7	7.7
	neutral	12	23.1	23.1	30.8
	agree	28	53.8	53.8	84.6
	strongly agree	8	15.4	15.4	100.0
	Total	52	100.0	100.0	

There is a need for deposit insurance in Palestine

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid disagree	1	1.9	1.9	1.9
neutral	4	7.7	7.7	9.6
agree	29	55.8	55.8	65.4
strongly agree	18	34.6	34.6	100.0
Total	52	100.0	100.0	

How confident do you believe people (depositors) are with banks in Palestine?

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid very confident	23	44.2	45.1	45.1
somewhat confident	28	53.8	54.9	100.0
Total	51	98.1	100.0	
Missing System	1	1.9		
Total	52	100.0		

Where money for a deposit insurance fund would be collected from?

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid Palestinian national authority	12	23.1	24.5	24.5
premium collected from member banks	17	32.7	34.7	59.2
government borrowing	6	11.5	12.2	71.4
an initial loan from the government for start-up capital	9	17.3	18.4	89.8
other	5	9.6	10.2	100.0
Total	49	94.2	100.0	
Missing System	3	5.8		
Total	52	100.0		

.What currencies would a deposit insurance fund cover?

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid shekels	4	7.7	7.7	7.7
dinars	1	1.9	1.9	9.6
dollars	3	5.8	5.8	15.4
all of the above	38	73.1	73.1	88.5
a & b	2	3.8	3.8	92.3
a & c	3	5.8	5.8	98.1
other	1	1.9	1.9	100.0
Total	52	100.0	100.0	

4. In case of bank failure up to how much of depositor`s money should be covered?

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid up to 1000\$	4	7.7	7.8	7.8
between 3001\$ - 5000\$	4	7.7	7.8	15.7
between 5001\$ - 7000\$	5	9.6	9.8	25.5
between 7001\$ - 9000\$	5	9.6	9.8	35.3
between 9001\$ - 11000\$	6	11.5	11.8	47.1
between 11001\$ - 13000\$	3	5.8	5.9	52.9
between 13001\$ - 15000\$	15	28.8	29.4	82.4
other	9	17.3	17.6	100.0
Total	51	98.1	100.0	
Missing System	1	1.9		
Total	52	100.0		

In case of a bank failure how long should it take for depositors to be re-imbursed?

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	within a few days	9	17.3	17.6	17.6
	within a month	16	30.8	31.4	49.0
	within 3 months	13	25.0	25.5	74.5
	within 6 months	7	13.5	13.7	88.2
	within a year	4	7.7	7.8	96.1
	other	2	3.8	3.9	100.0
	Total	51	98.1	100.0	
Missing	System	1	1.9		
Total		52	100.0		

**What do you consider to be the most important preconditions that need to be fulfilled before an implementation of a deposit insurance scheme?
(1 is considering to be most important, and 5 is considering least important).**

	#
Evaluation of the economy and health of the banking system	1
Macroeconomic stability (long-term stability in the inflation rate, reduction in the interest rates)	2
Sound governance of agencies involving the financial safety net	4
Strong regulation and supervision	3
Sound accounting and disclosure management	5