THE LEGAL AND INSTITUTIONAL FRAMEWORK FOR THE OPERATION OF DEPOSIT INSURANCE SCHEME IN NIGERIA

BY

Lawrence Stephen IJIMDIYA

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DECLARATION

I, Lawrence Stephen Ijimdiya, hereby declare that the information contained in this dissertation is my work and that it has not been presented in any form for any award elsewhere. Information contained from other literary publications have been duly acknowledged.

…….. ……

IJIMDIYA, STEPHEN LAWRENCE DATE

CERTIFICATION

This thesis titled: "The Legal and Institutional Framework for the Operation of Deposit Insurance Scheme in Nigeria" meets the regulation governing the award of the degree of Master of Laws (LL.M) of the Ahmadu Bello University, Zaria and is approved for its contribution to knowledge and literacy presentation.

……. ……

PROF. I. J. G. IROKALIBE **Date**

Chairman, Supervisory Committee

……. ……

DR. A. R. AGOM **Date**

Member, Supervisory Committee

……. ……

DR. A. R. AGOM **Date**

Head, Department of Commercial Law

……. ……

PROF. KABIR BALA **Date**

Dean, School of Postgraduate Studies

ABU, Zaria

DEDICATION

This work is dedicated to the Almighty God who gave me the grace and strength to complete this research work.

To my late father, Engr. Stephen Ayaba Medugu Ijimdiya and my two younger sisters, Justina Stephen Ijimdiya and Magdaline Stephen Ijimdiya, who all passed on to glory during this research work. May your gentle souls continue to rest in the bossom of our Lord Jesus till we meet to part no more at eternity.

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All mistakes and errors that may still be found in this work are mine while due credit has been given to those whose works were consulted.

ABSTRACT

Deposit Insurance System (DIS) has become a key component of most financial systems worldwide because of the important roles it plays in protecting depositors as well as contributing to financial system stability. Since its establishment by the Nigeria Deposit Insurance Corporation (NDIC) Decree No. 22 of 1988, the NDIC, which is charged with deposit protection mandate has remained an active safety-net player in spite of many daunting challenges. The establishment of the corporation was bore out of necessity over two decades ago when the Federal Government conceived the idea of the implementation of the Structural Adjustment Programme (SAP) in which the deregulation of the banking system would constitute an unholden central pillar. The NDIC has been faced with numerous challenges that have hampered the effective and efficient implementation of the Deposit Insurance Scheme (DIS) in Nigeria. Thus, this research work aims at examining these challenges and to proffer sound recommendations. Firstly, the corporation is faced today with the challenge of execution of court judgement against its assets for liability of banks in liquidation. This is because courts normally regard the NDIC as a successor-in-title of failed banks. Secondly, the amount fixed as maximum deposit claim under section 20(1) of the NDIC Act, 2010 to all the classes of depositors and regardless of the amount of deposit lost by a depositor in the event of failure of a deposit-taking financial institution is not reasonable. Thirdly, the penalty provided under section 45 of the NDIC Act, 2010 for non-compliance with its provisions and failure to secure the authenticity of any statement submitted pursuant to the provision of Act is less punitive. Consequently, it is hereby recommended that the NDIC Act, 2010 should further be amended to bar courts from executing judgement against the assets of the Corporation as a result of its statutory mandate as a liquidator of failed banks. Secondly, reimbursement of deposit lost by a depositor in the event of failure of an insured deposit-taking institution should be made full as this will encourage savings. Finally, the penalty provided under section 45 of the NDIC Act, 2010 should be increased by making it more punitive so as to encourage compliance. For the purpose of this research work, the doctrinal method of research will be adopted.

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LIST OF ABBREVIATIONS

AAI	-	African Alliance Insurance
ALL NLR	-	All Nigeria Law Report
AGF	-	Attorney General of the Federation
BOFIA	-	Banks and Other Financial Institution Act
BAS	-	Bank Analysis System
CAC	--	Corporate Affairs Commission
CAMA	-	Companies and Allied Matters Act
Cap	-	Chapter
CBN	-	Central Bank of Nigeria
Co.	-	Company
DIF	-	Deposit Insurance Fund
DIS	-	Deposit Insurance Scheme
DPAS	-	Differential Premium Association System
EDPS	-	Explicit Deposit Protection Scheme
EFASS	-	Electronic Financial Analysis and Surveillance System
FBIR	-	Federal Board of Inland Revenue
FBT	-	Failed Bank Tribunal
FBTLR	-	Failed Banks Tribunal Law Report
FDIC	-	Federal Deposit Insurance Corporation
FHC	-	Federal High Court
FRA	-	Fiscal Responsibility Act
FRN	-	Federal Republic of Nigeria
GNIC	-	Great Nigeria Insurance Company
GPI	-	Gross Premium Income
IADI	-	Independent Association of Deposit Insurance
IDPS	-	Implicit Deposit Protection Scheme
IMF	-	International Monetary Fund

JCA	-	Justice of the Court of Appeal
KB	-	Kings Bench
LFN	-	Laws of the Federation of Nigeria
Ltd	-	Limited
MFB	-	Micro Finance Bank
NAICOM	-	National Insurance Commission
NBLR	-	Nigeria Banking Law Reports
NDIC	-	Nigeria Deposit Insurance Corporation
NICON	-	National Insurance Corporation of Nigeria
NNDC	-	Northern Nigeria Development Company
No.	-	Number
NWLR	-	Nigeria Weekly Law Report
NTB	-	Nigeria Treasury Bills
PLC	-	Public Liability Company
PMS	-	Primary Mortgage Institution
PZ	--	Paterzon Zochonis
QB	-	Queen's Bench
SAP	-	Structural Adjustment Programme
SC	-	Supreme Court
SCNLR	-	Supreme Court of Nigeria Law Report
SIIF	-	Special Insured Institution Fund
USA	-	United States of America
UBA	-	United Bank for Africa
WLR	-	Weekly Law Report

CHAPTER ONE

GENERAL INTRODUCTION

1.9 Background of the Study

In recognition of the strategic importance of a stable banking system to an economy, various institutional arrangements have evolved overtime to foster banking stability; one of such initiatives is the establishment of a deposit protection scheme which is aimed at curtailing the attendant economic disruptions that typically follow bank failures. Among the consequences of these disruptions is the loss of deposits held in the failed bank and the inclination of the depositors of other banks to make panic withdrawal of their deposits in a manner capable of precipitating a run on those otherwise sound banks[1].

Banking business is so important to the economy of any nation that nowhere in the world is that business left to the whims and caprices of the business owners (shareholders) without appropriate regulation and supervision. There are so many reasons for this. Firstly, the bank plays the role of financial intermediation; where surplus fund are mobilized in form of deposits by the depositors and such funds are then channeled to entrepreneurs in the form of loans and advances for business development, giving rise to employment, wealth creation and growth.

That is why banking is often described as the engine room of the economy. Thus, when the banking system collapses, the economy also collapses. The second reason for regulation and supervision is that the share capital brought to the banking business by the shareholders is usually a small fraction when compared to the volume of funds mobilized by the banks from depositors who perhaps are really the

1. Peter, N. U. (1997).*Bank Deposit Insurance in Nigeria*. Page Publishers Services Ltd, p. 32.

most significant stakeholder in banking business. Thus, a bank with share capital of N25 billion in the current dispensation can mobilize up to N1 trillion of depositors funds. The main objectives of regulation and supervision are to promote safe and sound banking system, minimize the risk of failure, provide protection for depositors in the event of failure thereby promoting public confidence in the system and ensuring the stability of the financial system, a necessary ingredient for a vibrant economy[2]. There are several legislations regulating banking business in Nigeria[3]. The banking system is, no doubts, the most regulated industry in most countries.

Given its role in the financial system, deposit insurance scheme aims at ensuring financial guarantee to protect depositors in the event of a bank failure and also to offer a measure of safety for the banking system. However, in a broader sense, deposit insurance serves as one of the complementary measures employed by the monetary authority for effective management and orderly resolution of problems associated with both failed and failing deposit-taking financial institutions. Bank Deposit Insurance Schemes developed out of the need to protect depositors, especially the uninformed from the risk of loss and to also protect the banking system from instability occasioned by runs and loss of confidence.

An efficient Deposit Insurance System (DIS) has been recognized in many jurisdictions as one of the fundamental components of the financial safety-net.

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2. Alheri, B.N. (2012). *Distress Resolution Options and Legal Process Against a Bank in Liquidation: Issues and Challenges.* A Paper Presented at Sensitization Seminar on the Reforms by the Central Bank of Nigeria, held at Abuja, September 24 – 28.

3. Other Statutes that are also relevant for the regulation of different aspects of banking business in Nigeria *inter alia* include: The Economic and Financial Crimes Commission Act, 2002; The Independent Corrupt Practices and other Related Offences Commission Act, 2000, The Money Laundering (Prohibition) Act, 2011; The Investment and Securities Act, 2007, Failed Banks (Recovery of Debts) and Financial Malpractices in Banks Act, 2004; Financial Reporting Council of Nigeria Act, 2011, Fiscal Responsibility Act, 2007. Companies and Allied Matters Act (CAMA), Cap C20, LFN, 2004.

Accordingly**,** many countries all over the world are embracing this concept by the establishment of one form of deposit insurance authority or the other in a bid to insulate their economies against the devastating effects of systemic bank failure.

The Nigeria Deposit Insurance Corporation (NDIC) is the agency of government saddled with the statutory responsibility of administrating the Deposit Insurance System (DIS) in Nigeria. The NDIC has its origin in the report of a committee set up by the Central Bank of Nigeria in 1983. The committee in its report recommended the establishment of a Deposit Protection Fund. Consequently, the NDIC was established through the promulgation of Nigeria Deposit Insurance Corporation (NDIC) Decree 1988[4].

The scheme offers some form of deposit protection to depositors such that their confidence in the banking system is not eroded in situation of failures of depository institutions. It also provides government with a framework for intervention and sterilization of the disruptive effect on the economy in the event of failures of deposit-taking institutions[5].

Two alternative approaches have been adopted in implementing a deposit protection scheme. One is the Implicit Deposit Protection System (IDPS) and the other is the Explicit Deposit Protection Scheme (EDPS). The IDPS is a discretionary approach adopted by the monetary authorities for propping up some failing deposit – taking institutions in the system. There is no explicitly statutory obligation on the part of the government to protect deposits.

4. Nigeria Deposit Insurance Corporation (NDIC) Decree No. 22, 1988.
5. Peter, N. U. *Op. Cit;* pp. 32 - 33.

The government is at liberty to decide whether or not to grant any relief to depositors and the amount of such relief. Government exercises its discretion in this respect, based on its assessment of the consequence as of either intervening or not[6]. Other features of the IDPS include lack of any formal rules and procedures for intervention, absence of any prior funding arrangement and the use of an ad-hoc administrative structures.

This approach is fraught with considerable uncertainties for both the depositors and deposit-taking institutions. But this very weakness ironically provides the greatest justification for its adoption. This justification is premised on the need to maintain market discipline on the part of the depositors and avoid moral hazard on the part of the deposit-taking institutions. Whilst market discipline refers to the depositors taking interest in the financial conditions of the institutions in which they place their deposits and reflecting this in their decisions through withdrawing deposits from the poorly managed ones, moral hazard relates to excessive risk taking by banks knowing that their deposits have been insured[7].

The alternative arrangement is an Explicit Deposit Insurance Scheme (EDIS) created by a legal instrument. The enabling statute usually states the objectives of the scheme and other operational guidelines relating to issues like ownership, funding, extent of deposit protection, membership, resolution options compatible with stated objectives, etc. Thus, EDIS provides a formal framework with clear cut out rules and procedures for providing deposit protection, assessment and management of failed and failing deposit – taking insitutions[8].

6. *Ibid*, p. 33.
7. *Ibid*, p. 33.
8. *Ibid*, pp. 33 - 34.

In Nigeria, we practice the EDPS. Its adoption was necessitated by our experience in bank failure. The law which established the NDIC, that is, the NDIC Decree No. 22 of 15th June, 1988 was repealed due to manifest loopholes which include poor drafting style, rigid provisions that hindered responsiveness to the need of stakeholders. For example, premium payable by banks and insurance coverage could not be varied without amending the law, the appointment of the NDIC as a liquidator of failed insured institutions was not automatic, but was subjected to the Companies and Allied Matters Act (CAMA) tortious court processes, failure to recognise deposit insurance as an exclusive mandate of a deposit insurer, inadequacy of enforcement powers, absence of protection for directors and employees of the NDIC against adverse claims for actions or decisions taken in their official capacity, etc.

In 2006, precisely on the 22nd December, 2006, the Nigeria Deposit Insurance Corporation (NDIC) Act, 2006[9] was passed into law to correct the lacunae and inadequacies of its predecessor. This law, for similar reasons, was further amended as the Nigeria Deposit Insurance Corporation (NDIC) Act, 2010[10] (Hereinafter referred to as the Act), all in an effort to position the Corporation to achieve its statutory mandate.

In spite of these developments, there are still inherent lacunae in the current Act that are serving as clock in the wheel of the Corporation's progress.

9. Nigeria Deposit Insurance Corporation Act, No. 16, 2006.
10. Nigeria Deposit Insurance Corporation Act, Cap. N102, LFN, 2010.

1.10 **Statement of the Problem**

The DIS as a safety-net measure is aimed at protecting banks from failure and depositors from the risk of loss of their hard earned money in the event of bank failure. In Nigeria, the DIS is administered by the NDIC. In the discharge of its statutory responsibilities, the NDIC had in the past two decades been able to take meaningful and significant steps in deposit insurance practice. It has also cooperated with other safety-net players to ensure that the nation's financial system is stable.

In spite of these achievements, there are lingering legal issues and challenges facing the corporation today which are hindering its progress. These include the following lacunae in the NDIC Act; firstly, the most fundamental problem of the Act that requires urgent remedy is the execution of judgement against the assets of the NDIC for liability of banks in liquidation. The corporation had been faced with attachment levied on its assets in execution of judgment obtained against banks in liquidation. That anomalous situation was the result of the corporation's role as liquidator of failed banks in Nigeria. The courts had regarded that role as making the Corporation the successor-in-title of the failed bank, which should not be the case. For example in **Nigeria Deposit Insurance Corporation (Liquidator of All States Trust Bank Plc) v. Tempo Mills Ltd. & Co**[11], the corporation filed an appeal to challenge the judgement of the Federal High Court, Enugu which was really against the closed bank but it was the corporation's head office that was subsequently attached on account of that judgement.

11. Appeal No. CA/E/76/2009 (Unreported).

In **Alhaji Yusuf Ozegya v. NDIC (Receivership of Savannah Bank of Nigeria Plc)**[12] instituted by the Landlord to Savannah Bank, despite the fact that the defendant was sued in official capacity, the High Court of Abuja issued an order to levy execution on the personal assets of the corporation on account of the judgement granted in favour of the Landlord. The corporation had to pay the judgement debt to court to avert removal of the corporation's assets to court by the Sherriff. Interestingly, throughout the duration of the case, the corporation was neither the receiver nor liquidator of Savannah Bank as the bank had gotten its licence restored by the Court of Appeal.

Secondly, the amount fixed as maximum deposit claim under section 20(1) of the Act to all the classes of depositors and regardless of the amount of deposit lost by a depositor in the event of failure of an insured deposit-taking institution is not reasonable.

For example, by the provision of the section, if a man losses N200,000,000.00 in the event of failure of a licence bank, he is only entitled to a maximum reimbursement or claim of N200,000.00 from NDIC. This, to say the least, is not reasonable and can discourage savings which is capable of stifling the economy of investable funds.

Thirdly, the penalty under section 45 for non-compliance with the provisions of the Act is inadequate.

These problems have greatly affected the effective and efficient administration of the DIS in Nigeria and need urgent redress so as to enable the Corporation achieve its statutory mandate.

12. Suit No. NSD/LF/38/2008 (Unreported).

1.11 **Aim and Objectives**

The broad aim of this research work is to examine the inherent lacunae in the present legal framework that regulates the operation of the DIS in Nigeria, that is, the NDIC Act, 2010[13] and to proffer sound recommendations for its amendment.

The researcher believes that effective implementation of the DIS in Nigeria largely depends on adequate framework.

This research work also seeks to provide an in-depth appraisal of the mandates of the NDIC with a view to examining how it has contributed in protecting bank depositors and ensuring sound banking system in the over two decades of its existence in Nigeria.

1.12 **Scope and Limitation of the Research**

The scope of this research work is limited to the stated objectives, consequently, the examination of the inherent lacunae in the present legal framework that regulates the operation of the DIS in Nigeria and to proffer sound recommendations for its amendment.

The research work will also focus on the operation of DIS in Nigeria alone. It also seeks to examine some challenges facing the corporation today that have served as clock in the wheel of its progress as well as the prospect of the corporation.

13. Supra

1.13 **Research Methodology**

For the purpose of this study, the doctrinal method of research will be adopted. By doctrinal method, primary sources such as statutes and case laws and also secondary sources which comprise of journals/articles, text books, magazines, etc will be consulted[14].

The use of statutes and case laws are obviously for the purpose of obtaining the applicable laws and judicial pronouncements on the subject of this study. Whereas the use of the secondary sources is basically to reflect on the way some writers on the subject of the research attempted to analyze the issues at stake.

1.14 **Justification**

A stable and prosperous economy is central to the development of any nation and this cannot ordinarily be achieved without first achieving a very strong and reliable banking system that can earn the confidence of its depositors, customers and the general public at large. This research work will assist in this direction as it will identify the role of the NDIC in enhancing the confidence of the depositors, ensuring sound banking system and also proffer sound recommendations to the lacunae in the present legal framework, that is, the Nigeria Deposit Insurance Corporation Act, 2010[15].

It will also take a critical look at the provision of the Act to see the extent to which it has protected the interest of depositors and customers of such banks in cases of failure, so that adequate recommendation made by the research will assist the government in the formulation of its economic policies that will help in achieving stable and prosperous economy.

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14. Aboki, Y. (2009). Introduction to Legal Research Methodology. Tamaza Publishing Company Ltd, Wusasa, Zaria, p.3
15. Supra

Moreso, the study will essentially assist the government in its current policy and economic reform, more particularly the banking sector reform, as well as the stakeholders in the financial market and the general public.

1.15 **Literature Review**

The Nigeria Deposit Insurance Corporation (NDIC) had in the past 20 years faced numerous legal challenges in the course of performing its statutory functions. In an attempt to address some of these challenges, the corporation successfully pushed for the repeal of the NDIC Decree No. 22 of 15th June 1988 which established it. Similarly, several authors and academicians have written numerous books to proffer solutions and recommendations to some of these challenges.

Ogunleye[16] dealt extensively with the topic of this research. It did not leave any stone unturn on the issue of mandate, powers, governance structure, legal issues in implementing deposit insurance in Nigeria, Deposit insurance funding and fund management. It also discussed the challenges facing the corporation, prospects of the corporation, etc. However, it did not discuss some of the inherent manifest lacunas of the Act which have hampered the effective and efficient operation of the corporation. This research work aims at examining the deficiencies of the Act and to proffer sound recommendations that will aid the government in repositioning the corporation and in its policy formulation.

Ogunleye[17], on his part again articulated brilliantly the concept and relevance of deposit insurance and its role in promoting financial system stability in Nigeria.

16. Ogunleye, G. A. (2009). *20 years of Deposit Insurance in Nigeria*. Kenjul Enterprises.
17. Ogunleye, G. A. (2010). *Perspective on the Nigeria Financial Safety-net*. Adolness Nigeria Limited.

He also examined the Nigerian banking industry and the substantial structural changes it had undergone over the last three decades due to series of reforms in terms of the number of institutions, ownership structure, as well as depth and breadth of operations.

Like the first literature, this literature did not discuss anything relating to the challenges and problems of the NDIC which have immensely affected the implementation of the DIS in Nigeria, let alone the legal inadequacies and lacunae in the previous and present legal framework that regulate the operation of the DIS in Nigeria.

Alheri[18], serves as a veritable literature on the issue of distress resolution options and legal processes against a bank in liquidation. The paper, in its entirety, focused solely on the role of the NDIC in resolving issues relating to distress in the banking system.

Some of the measures the NDIC usually adopts which are discussed in the paper include; Open Bank Assistance, Closed Bank Resolution and the Bridge Bank Resolution. The paper did not also leave any stone unturn in the area of liquidation process. However, rather than using the NDIC Act, 2010 since the paper was written in 2012, the author used the amended NDIC Act, 2006 in presenting her argument. Similarly, the author failed to discuss cases of banks that were bridged by the NDIC and CBN due to liquidity challenges and their failure to meet the CBN capitalization requirement.

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18. Alheri, B. N. *Op. Cit; pp. 1-15.*

Jubril[19], x-rayed the ongoing clash between the CBN and the NDIC over the proposed amendment of its statutes and the need for both agencies to cooperate with each other in order to safe-guard the banking sector and considering their common history. He traced the history of the establishment of the NDIC to CBN in 1983 following the turbulence in the financial industry that made thousands of depositors lost their hard earned life savings.

He also opined that from inception, the core mandate of NDIC is deposit insurance as contained in section 2(1) of the NDIC Act, 2010 hence it should focus on that alone rather than seeking amendment to its Act for powers to make it a parallel /coordinate regulator of banks as CBN.
This move, according to him is fraught with danger and could be a recipe for financial instability.

Though, the author's argument sounds very persuasive, it is wrong to restrict the NDIC's role to only deposit guarantee. To adequately protect depositors, it is pertinent for the NDIC to exercise supervisory powers over banks.
The corporation supervises bank so as to protect depositors, foster monetary stability, promote effective and efficient payment system, promote competition and innovation in the banking system.

Umoh[20], highlighted the contribution of the NDIC to the stability of the financial system which can be examined within the context of its activities in the discharge of its statutory mandate.

19. Jubril, A. (2015). *Why NDIC should Focus on Core Function of Deposit Insurance*. www.sunnewsonline.com, Accessed September 18, 2015, 15.00hrs
20. Umoh, P. N. (2003). *The Role of Deposit Insurance in Financial Sector Stability.* A Paper Delivered at the Fifth CBN Seminar for Finance Correspondents and Business Editors, held at Owerri, Imo State, October 27 – 29.

According to him, some of the activities undertaking by the Corporation with the aim of insulating the financial industry from destructive runs and instability include deposit guarantee, bank supervision, distress resolution and bank liquidation. The author neglected to examine the relevance of adequate legal framework to the corporation in the discharge of its statutory mandate.

Umoh[21] again enumerated the key role the Corporation played upon its establishment in tackling the problem of previous incessant bank failures in Nigeria and the measures which it took.

Similarly, it also examined the legal challenges inherent in the commencement legal framework as well as other challenges which hampered the progress of the Corporation. In the same vein, it also examined the steps which the Corporation took in addressing some of these legal challenges such as the amendment of some Sections of the NDIC Decree No. 22 of 1988 in 1997.

Afolabi[22], discussed the benefits of a consolidated banking system in Nigeria and observed the fundamental problems in the financial industry. He also examined the role of the NDIC as a financial safety-net.

Ologun[23] tried to highlight the several factors that eroded the public confidence reposed in the Nigerian banking system which usually result in bank failure; including bad management of the banking industry and economic recession.

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21. Umoh, P. N. (1999). *A Decade of Deposit Insurance in Nigeria:* Issues and Challenges. Kenjul Enterprise, Abuja, Nigeria.
22. Afolabi, J. A. (2004). *Implications of the Consolidation of Banks for the Nigerian Banking System.*A Paper Presented at the NDIC organised Workshop for FICAN, Enugu.
23. Ologun, S. O. (1995). *Banks Failure in Nigeria: Genesis, Effects and Remedies*, CBN Economic and Financial Review, Vol. 32, No. 3.

While Umoh[24], on his part discussed the concept of deposit insurance and the potential role of the scheme in any financial system, it also examines the relevance of the scheme in Africa drawing on the experiences of African countries that had adopted the explicit type of deposit insurance scheme. He also explain the benefit that African countries would gain from the introduction of deposit insurance scheme most especially, in terms of having efficient and competitive financial system, where he stated thus;

> *"Competition is a vehicle for achieving efficiency since, in a competitive banking system, banks are forced to operate efficiently if they are to keep their customers and remain in business".*

Manu[25] examined the critical issues to be considered before establishing deposit insurance scheme, such as the nature and historical background of the financial system of a given country in order to assess the model of the scheme that could be suitable for the system.

Ogunleye[26] examines the banking consolidation programme being implemented by the Central Bank of Nigeria (CBN) vis-à-vis the challenges posed to the NDIC as a provider of financial safety-net.

Peter[27], traced the evolution of the financial system in Nigeria, establishment and administration of the NDIC, operational activities of the NDIC, prospect and challenges of the NDIC. But did not examine the pivotal role the legal framework plays in the effective operation and implementation of deposit insurance scheme in Nigeria.

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24. Umoh, P. N. (2003). *Deposit Insurance: Concept, Practice and Relebace in Africa*. A Paper presented at International Association of Deposit Insurance (IADI) Regional Conference at Abuja.
25. Manu, B. *Critical issues to consider when establishing Deposit Insurance Scheme*, NDIC Quarterly, Vol. 4 at 16.
26. *Ogunleye, G. A. (2008). Regulatory Challenges in a Consolidated Nigerian System: NDIC Perspective.*
27. Peter, N. U. *Op. Cit; pp. 1 – 15.*

Ademola[28], discussed the importance of the banking industry to the economic prosperity of a country. He opined that considering the role banks play in the mobilization of savings, they impact on every sector of the economy. He also articulated the reasons for the establishment of the NDIC, its functions, the history of bank and the causes of bank failure in Nigeria. In his conclusion, he discussed his findings and made recommendations.

It should be noted that, none of the above literatures examine the legal constraints facing the NDIC such as inadequate legal provisions that have hampered the effective and efficient operation of the NDIC in Nigeria. And the inherent manifest inadequacies of the Act or any other relevant legislation in order to find out the effectiveness of the mechanism put in place by such laws for the implementation of the Deposit Insurance Scheme in Nigeria.

1.16 **Organizational Layout**

Chapter one of the research work contains the general introduction of the research, background of the study, statement of the problem, scope of the research, aim and objectives of the research, research methodology, justification, literature review and organizational layout.

Chapter two will trace the evolution of deposit-taking financial institutions in Nigeria. Although, there are diverse views by authors and academicians as to when modern banking operations started in the territory now known as Nigeria. However, one common denominator expressed by all of them is the fact that it was introduced by British merchants who transacted business on the coast of West Africa during the colonial era.

28. Ademola, G. (2013). *Bank Distress in Nigeria and the Nigeria Deposit Insurance Corporation Intervention*. Global Journal of Management and Business Research, Vol. 13.

The need for the establishment of a deposit taking institution was largely connected to the increase in the volume of trade and commerce in the then Lagos colony. The establishment of the first deposit taking institution in Lagos was the brain child of Mr. George William Neville. This was as a result of the setting up of regular shipping between Liverpool in England and the West African Coast, movement of cargo and the increased importation of British Silver coins in large boxes continued unabated. It was against this background that the initiative for the establishment of a bank was taken in the Lagos office of Elder Dempster & Co. Ltd. Elder Dempster was the first shipping firm, which ran the regular steamship voyage between Liverpool and the West African Coast[29].

This chapter will also discuss the historical development of insurance in Nigeria. In most African countries particularly in Nigeria, modern commercial insurance is less than 100 years old. The British colonial government introduced insurance business into Nigeria in 1910. Traditionally, though some forms of social insurance existed in part of the Nigeria society long before their arrival. This was in a form of mutual and social schemes, which evolved through the extended family system, aged grades and clan union typical of Africa culture.

The chapter will also discuss the formation of insurance contract. In most respect, an insurance contract is the same as any other commercial contract and to that extent, to be valid and enforceable, it must possess all the essential features of a contract.

For example, there must be an agreement base on offer and acceptance, the contract must be legal in all respect, there must be either a valuable consideration or form and there must be an agreement, base upon an equality of knowledge of all the material facts, that is consensus ad idem[30].

29. Goldface – Irokalibe, I. J. (2006). *Law of Banking in Nigeria. Malthouse* Press Limited, Lagos, p. 3.
30. Irukwu, J. O. (2006). *Fundamental of Insurance Law*. Witherbys Printing Ltd, London, p.1.

Lastly, the chapter will also discuss problems and challenges of deposit institutions in Nigeria as well as the distinction between deposit insurance scheme and the conventional insurance system.

Under chapter three the historical development of deposit insurance in Nigeria will be discussed. The Nigeria Deposit Insurance Corporation (NDIC) has its origin in the report of a committee set up in 1983 by the Board of the Central Bank of Nigeria to examine the operations of the banking system in Nigeria. The committee in its report recommended the establishment of a Depositors Protection Fund. Consequently, the Nigeria Deposit Insurance Corporation (NDIC) was established through the promulgation of Decree No. 22 of 15th June 1988.

This was part of the economic reform measures taken by the then government to strengthen the safety net for the banking sector following its liberalization policy and the introduction of the 1986 Structural Adjustment Programme (SAP) in Nigeria. The reasons for the establishment of the Nigeria Deposit Insurance Corporation were also looked into. They include; lessons of prior history: experience of previous bank failures in Nigeria (1947 – 1952), lessons from other countries, anticipated consequence of economic actions on banking supervision, increased competition among banks and change in government bank support policy[31].

It will also examine the governance structure of the Nigeria Deposit Insurance Corporation, powers and authorities of the corporation, the legal framework of the NDIC in Nigeria since its inception, deposit insurance funding and fund management will equally be examined and the issue of failed bank resolution in Nigeria.

31. Peter, N. U. *Op. Cit;* p. 32.

Chapter four will discuss the challenges and prospects of the Nigeria Deposit Insurance Corporation. In the discharge of its mandate, the NDIC had in the past two decades been able to take meaningful and significant steps in deposit insurance practice.

It had also cooperated with other safety-net players to ensure that the nation's financial system was stable. Be it as it may, the prospects for better performance of the NDIC remain very bright. Also, given the experience of the corporation in the last twenty years, there were also several lessons to be learned. Such lessons would be used to improve upon the corporation's efforts at discharging its mandate in the most efficient and effective manner.

Finally, chapter five brings the research to a conclusion with the summary, findings and observations as well as our recommendations and suggestions for effective implementation of the DIS in Nigeria.

CHAPTER TWO

HISTORICAL DEVELOPMENT OF DEPOSIT INSTITUTIONS IN NIGERIA

2.1 Introduction

Banking operations was kicked started in Nigeria as a result of increased commercial activities on the coast of West Africa. At the beginning, the motive was selfish as it was only meant to satisfy the selfish narrow commercial interest of the few British businessmen who operated in the West African coast particularly in Lagos. What was started by a negligible few in probably one room has today grown beyond imagination.

The existence of the first bank in Lagos was the brain child of Mr. George William Neville. This was as a result of the setting up of regular shipping between Liverpool in England and the West Africa Coast, movement of cargo and the increased importation of British silver coins in large boxes continue unabated. It was against this background that the initiative for the establishment of a bank was taken in the Lagos office of Elder Dempster & Co. Ltd. Elder Dempster was the sole shipping firm, which ran the regular steamship voyage between Liverpool and the West African Coast. The Lagos agent of Elder Dempster was Mr. George William Neville. Concern over the increasing number of silver boxes in his Lagos office led him to suggest the establishment of a bank in Lagos to the Chairman of Elder Dempster, Mr. Alfred Lewis Jones. Neither of the two men had any sound knowledge of banking. When Neville thus suggested that banking facilities were urgently required in West Africa, and moreso in Lagos, Alfred Jones told Neville "to approach some existing bank and try to induce them to establish a branch in the country" Neville did[32.]

32. Goldface – Irokalibe, I. J. *Op. Cit;* p. 3.

Following the discussions that took place between Mr. George William Neville and Mr. Alfred Lewis Jones, the Chairman of Elder Dempster, the former swung into action by approaching the African Banking Corporation with the sole aims of persuading them to open a branch in Lagos colony.

2.3 Evolution of Deposit Institutions in Nigeria

2.3.1 The African Banking Corporation (ABC)

The African Banking Corporation was undoubtedly the first bank in Nigeria. Upon the premise of the discussion between Mr. George William Neville and his boss, he approached the African Banking Corporation, which had just about then commenced business in South Africa in the same year, 1891. The London Board of the African Banking Corporation accepted Neville's proposal and on June 4, 1891 "letters were read from Elder Dempster & Co. and from George Neville relating to the opening of a branch in Lagos"[33]. Approval having been given for the founding of a branch of the bank in Lagos, Neville was asked to act as the bank's agent in Lagos.

Alfred Jones was in the meanwhile co-ordinating the important question of colonial office as well as crown agents' approval. The approval became rather imperative as the first task of the Lagos branch was to import and distributes new silver coins. The bank sought and obtained monopoly of this function, hitherto undertaken severally by independent traders, though at a higher cost.

The second fundamental condition for the successful take-off of the Lagos bank was that it should become the banker of the colonial government.

33. Extract from records of the African Banking Corporation, Board meeting held on June 4, 1891 quoted by Fry, R. Bankers in West African (London, Hutchinso Benham (1876), Quoted in Goldface-I*rokalibe, I. J. (2006); Law of Banking in Nigeria, Malthouse Press Limited, Lagos,* p. 1.

Permission on the application for silver import monopoly was granted on January 28, 1892, when the Crown agents finally initialed an agreement. By this agreement, the African Banking Corporation became authorized to import new silver coins from the Royal Mint in London, free of charge for packing freight, and insurance. However, other independent traders in West Africa were still allowed to order new coins from the Mint with the crown agent's approval but only upon payment of one percent premium.

It appears that the actual take off of the Lagos branch took place soon afterward, when Neville return to Lagos. Banking was then born in Nigeria. From the view point of I. J. Goldface-Irokalibe, it is of very striking significance to point out that no formal legislation was enacted by any legislative organ either in England or the colony of Lagos to give effect to the establishment and regulation of banking business in Nigeria.

What happened at that point was, at best a mere administrative approval given by both the colonial office and the crow agents to the African Banking Corporation to commence business. It may well be that the authorities in charge of colonial matters saw the inception of banking in the Lagos colony as nothing other than piece of business venture at that time. It was therefore not until about sixty years later, in 1952, that the first legislation on banking in Nigeria was passed.

After the founding of the Lagos branch of it bank, in August, 1891, the African Banking Corporation decided on October 8, 1891 to send an inspector of the bank, Mr. Mckenzie to Lagos with a mandate to "see that the machinery of the branch is in proper working order and if possible to visit other posts and send full reports to the Directors on the banking possibilities of West African Coast[34]".

34. *Ibid*, p. 4.

While the bank was trying to consolidate itself in Lagos, a trade depression ensued in the area sequel to the outbreak of unrest between the Egba and the Ijebu, two rival Yoruba clans on September 8, 1892, barely a little over a year of banking, Elder Dempster wrote advising that the bank's funds in Lagos might be transferred to London for better use.

In the face of this and other difficulties, including complaints about the bank by some prominent Lagos traders to the colonial office, the Chairman of the African banking Corporation wrote to Alfred Jones. He expressed dissatisfaction with the progress of the bank in Lagos, and wanted to know if Elder Dempster would be prepared to take it over. This almost marked the collapse of banking in Nigeria, but the banks Chairman had a meeting with Mr. Jones about the Lagos branch's affairs.

It was then decided that Africa Banking Corporation should continue for another three months and if it then wished to withdraw, Elder Dempster would take over the branch and refund the money lost by African Banking Corporation.

In October, 1892, the bank's chief inspector, Mr. Herbert was sent to Lagos to report. After investigating the affairs of the bank, on November, 24, he cabled London advising the sale of the Bank to Elder Dempster. In January 1893, Mr. Alfred Jones attended a Board meeting of the African Banking Corporation to discuss terms of the takeover of the Bank in Lagos. The result of the meeting was the sale to Elder Dempster of the Lagos branch of the African Banking Corporation bank for a sum of £1000. The final takeover of the branch was effected on March 31, 1893[35].

35. Fry, R; *Op. Cit;* p. 22.

2.3.2 **The Bank of British West Africa**

The take-over of the Lagos branch of the African Banking Corporation by Elder Dempster was not without problems. The Crown Agent, for instance, refused to transfer the right of importation of Mint silver free of charge from the African Banking Corporation to the new undertaking under Elder Dempster. Furthermore, the Crown Agents insisted on the proper constitution of a new bank and £10,000 worth of securities being deposited in replacement of those to be withdrawn by the African Banking Corporation. To add to these difficulties, the colonial secretary instructed the governor of Lagos to proceed with the closure of official government account with the bank and to withdraw all government funds by March 30, 1893[36].

Following this developments, Elder Demspter, through Mr. George Williams Neville, his Lagos agent, called the then acting governor of Lagos, Captain G. C. Denton, and prevail on how not to press ahead with the withdraw of government funds as it was likely to cause a run. He further offered to deposit £5,000 sterling in specie as security for the account if it was allowed to continue. Captain G. C. Denton reported this offer to London, and Lord Ripon, the colonial secretary gave approval for the fund to remain.

The securities earlier demanded were handed over in May, 1893, and the formation of Bank of British West African was announced. On July 8, 1893 a further £5,000 was deposited by the bank in gold in Lagos treasury Vault. In this way the Bank of British West Africa made its first debut in Lagos. It was however, not until the following year, 1894, that the bank was formally registered in London.

36. *Ibid*, p. 23.

All accounts on the founding of the Bank of British West Africa, agree on the point that Mr. George William Neville was its founder. The records show that the bank was taken over from the African Banking Corporation and given its new name in 1893, and was formally incorporated in London in 1894.

In fact, even the present day successors to the Bank of British West Africa, namely, First Bank of Nigeria, confirm the founding of the bank to have been in 1894. However, research reveals that on Friday, November 10, 1899, Neville appeared before the "Barbour Committee" on West African Currency matters. During the course of his evidence before the committee, Neville was asked about the bank of British West Africa and he straight away acknowledged founding the bank in Lagos in 1892[37.]

It is something of a historical anachronism that the very man who founded the bank should put the founding as 1892, while all other records and accounts speak of 1893 as the year of the take-over by Elder Demspter of the African Banking Corporation and 1894 as the year of eventual incorporation of the Bank of British West Africa under its new name. The likely explanation may be that when the African Bank Incorporation's Chief inspector, Mr. Herbert visited Lagos in late 1892 to investigate the affairs of the bank some kind of take-over arrangement was discussed between him and Neville resulting in his cable advising that the Lagos branch be sold to Elder Dempster.

37. *Ibid*; p. 24

Neville who choose the new name for the bank might have done so in late 1892, and accordingly inform Elder Dempster Chairman, Alfred Jones. The records show that in January 1893, Jones attended a board meeting of the African Banking Corporation to discuss the takeover terms, the final take over being effected on March 31, 1893[38.]

The Bank of British West Africa took off in Lagos in 1893, and was formally incorporated in London in 1894. Notwithstanding this legal oddity, the bank of British West Africa which technically was no more than an offshoot of Elder

Dempster & Co. enjoying its facilities including being managed by Neville, its agent, had come to stay. This fact, however, highlights the legal lacuna in banking law in Nigeria, the bank of British West Africa, already in existence and doing business in Lagos in 1893, was only incorporated in London in 1894. This means that there was no law in Lagos (Nigeria) under which a bank was required to register before commencing business.

The Bank of British West Africa was registered in London as a Limited Liability Company on March 31, 1894. The nominal share capital was £100,000 in shares of £10 each.

The bank's head office was in Liverpool with one branch in Lagos. Four Directors were nominated. These were Alfred Lewis Jones, Chairman of Elder Dempster & Co., F. W. Bond, Chairman of the African Steamship Company, Henry Cole, the Liverpool agent of David Samson and Company, East India Merchants and Bankers, and Edward Lawrence, head of his own Liverpool Merchant firm.

38. Minute of evidence before the Barbour Committee Question No. 189 page 5 on Friday November 10, 1899 National Archives (SNP6 No. 30/1912). Quoted in Goldface-Irokalibe, I. J., Op. Cit; p. 5.

Of the 3,000 shares issued in the first place, Alfred Jones took up 1,733. His partners in Elder Dempster, Alexander Sinclair and W. J. Davy took 433 each. The rest went to the other Directors[39.]

The Directors entered into talks with both the Crown Agents and Elder Dempster & Co, which resulted in the drafting of the Articles of Association and the formal taking over of the Lagos banking business from Elder Dempster & Co. Ltd. It was at the first board meeting in London on May 4, 1894 that William (Sandy) Ross was appointed Secretary. On June 1, 1894, Alfred Jones was appointed Chairman.

The Bank of British West Africa continued to grow and soon became a dominant feature of economic life not only in Lagos but elsewhere, where branches were opened.

Two new branches were opened outside Lagos in quick succession. One in Accra - Gold Coast in 1896 and another in Freetown, Sierra Leone in 1898. In 1900, a branch was opened in Calabar[40]. The various colonial administrations in the British West Africa, soon show their pleasure with the bank's activities. The use of cheques spread rapidly and soon almost the standard mode of paying customs duties and other revenue and for regular remittance of government funds.

Most of the prominent traders in Lagos and elsewhere patronized the bank. By the close of the century this bank was well established throughout British West Africa, and its home based in Lagos was strong and stable. Banking had finally arrived in Nigeria.

39. Ibid, p. 26.
40. The dates of Accra, Freetown tally with Fry's while that of old Calabar was independently established. Quoted in Goldface-Irokalibe, I. J.*Op.Cit*; p. 8.

2.3.3 **The Bank of Nigeria**

Following the Bank of British West Africa, the next bank to be established in Nigeria was the Bank of Nigeria. The bank owned its inception to a number of leading Nigerian merchants who did not quite like the monopoly power of the bank of British West Africa over silver importation and distribution.

There were also allegations of discriminatory premium charged on the supply of silver coins to merchants in favour of some traders.

The new bank was clearly therefore set up to compete with the British Bank of West Africa[41]. The Bank of Nigeria was established in 1899 with the name "Anglo-Africa Bank Limited" for the purpose of meeting the demand for banking facilities in Northern and Southern Nigeria which had been rendered more urgent by the introduction of silver currency.

The name of the bank was subsequently changed to the "Bank of Nigeria Limited". The capital of the bank was £150,000 in £1 shares and of this amount £32,000 was subscribed and issue[42]. The first branches of the bank were located in Calabar, Burutu and Lokoja. They were followed by one in Jabba in the Niger, and another in Grand Bassam in the French Ivory Coast (now Code'Ivoire). The Bank of Nigeria, thus, became in a rather technical sense, the first Bank in Nigeria given the fact that Lagos, where the rival bank of British of West Africa was situate, was then a colony, distinct from the southern protectorate. On this score alone, the claim by the British Bank of West Africa and its present day successor of being the first bank in Nigeria is incorrect.

41. Goldface – Irokalibe, I. J. *Op. Cit*; p. 8.
42. This fact are contained in a letter dated February 5, 1904 written by the Secretary of the Bank of Nigeria Mr. Lich H. Moseley, to the under Secretary of state for the colonies in London National Archives. (SNP49/1906). Quoted in Goldface-Irokalibe, I. J. *Op.Cit*; p. 9.

However, this claims becomes valid to the extent that the Bank of Nigeria later lost its independent identity, following its take-over by the Bank of British West Africa in 1912. In fact, as far back as 1904 in a letter dated February 5, and addressed to under Secretary of State for the colonies, Mr. Lich H. Moseley, Secretary of the Bank of Nigeria categorically described his bank.(Then known as Anglo-African Bank), as "the only bank established in Nigeria[43]".

As at that time, the Bank of British West Africa, in February 1906 was still making enquiries from the colonial under secretary of state for the colonies as to whether it would be welcomed into Nigeria, that is, the territory of the protectorates outside Lagos. In a letter dated February 10, 1906, Mr. J. Couper, the Manager of the bank of British West Africa in Liverpool informed the under secretary to extend the bank's operation into Nigeria. He concluded in the following manner.

"Before going any further, my Board would be glad of an expression of opinion as to whether the advent of this Bank into Nigeria would receive support from the government[44]". From the foregoing account and in a narrow technical sense, the Bank of Nigeria was the first Bank in Nigeria. However, two changes occurred to alter the legal position.

Firstly, the Bank of Nigeria merged with the Bank of British West Africa after it was taken over by it in 1912. Secondly, the erstwhile colony of Lagos merged with the rest of Southern Nigeria to form the Southern Nigeria Protectorate.

The Southern Nigeria Protectorate in turn was amalgamated with the Northern Nigeria Protectorate to form the unified colony of Nigeria. At amalgamation in 1914, the Bank of British West Africa was thus the only bank in Nigeria.

43. Ibid p. 9.
44. Ibid p. 9.

In these circumstances, therefore, the claim of the Bank of British West Africa, and its successors in title (Bank of West Africa, Standard Bank of Nigeria, and First Bank of Nigeria) as indeed the first bank to open business in Nigeria, is to be accepted as correct.

2.3.4 **The Colonial Bank**

Following the amalgamation of the Bank of Nigeria with the Bank of British West Africa, the Bank of British West Africa became once more, the only bank in Nigeria. In 1916, however, a new and more determined competitor emerged. The colonial bank, which hitherto had a charter to operate in the West Indies, announced its intention to open new branches at Accra, Lagos and Zaria, in the Gold Coast (now Ghana), and Nigeria respectively. This was made possible by the revision of the banks charter by the British parliament which granted it permission to work in any of the territories of the British Empire throughout the world.

The colonial bank began operation with capital of £2,000,000 of which £600,000 was paid up; and £150,000 was reserved. Within two years of its debut, the colonial bank established itself in more additional centres in Port Harcourt, Jos and Kano. By 1981, the Bank's reserve fund had grown to a big sum of £325,000 and new shares were issued. Following this issue the bank's paid up capital rose to the sum of £750,000. In 1919 the Governor of Nigeria ordered an equal division of silver coin between the two banks. This triggered another round of rivalry between the Bank of British West Africa and the Colonial Bank similar to the one that existed in the past between the Bank of British West Africa and the Bank of Nigeria. The Bank of British West Africa protested the Governor's action to the colonial office in London. The colonial office approved the Governor's action and before long the colonial bank established itself as a new force to be reckoned with in Nigerian banking business.

In 1925, the bank changed its name to become the Barclay's Bank. It rebuffed overtures for a take-over from the Bank of British West Africa and went on to acquire a dominant status[45].

With the passage of time, more expatriate banks came into the Nigerian Banking arena. Among the new arrivals were the British and French Bank for commerce and industry. The bank later became the British and French Bank.

In October, 1961, its Nigerian branches were re-christened the United Bank for Africa (UBA). The majority shares continued to be held by British and the French interests, but America, Dutch, German, Italian and Swiss banks also acquired shares[46]. Today, the bank is wholly Nigeria owned. Its shares were sold to the general public under the privatization scheme of the Nigerian Federal Government.

The Bank of America is also another expatriate bank that entered the Nigerian banking scene, having ceased to be known as the Bank of America on becoming fully Nigerian owned, it became known as Savannah Bank with its registered Head Office in Lagos. The Bank of India similarly became wholly Nigerian owned under a new name of Allied Bank.

The American chase Manhattan Bank, which also entered the scene later, ceased to do business in Nigeria. The Arab Bank later became known as the Nigerian-Arab Bank. All of these banks progress to varying degrees, and had their shares sold to the public under the Nigerian government privatization and commercialization scheme.

Some of these banks have once again merged with others to form a new banking group or ceased or have ceased to exist under the Nigerian government recapitalization drive of the year 2005 as directed by the Central Bank of Nigeria.

45. Fry, R; *Op. Cit;* pp. 91 – 93.

2.3.5 **Emergence of Indigenous Banks**

Indigenous banks simply means wholly Nigerian owned banks separate and distinct from colonial owned banks. The factors that necessitated the establishment of these banks are not far-fetched.

According to Goldface - Irokalibe I. J., this banks sprang up as a result of the racially discriminatory banking policies on credits and other bank charges levied by British banks against native Nigerians. This can be traced to the slave trade and colonialism which in no small measure lowered the dignity and self-respect of the black man as man. Thus it was not surprising that the urge to set up wholly indigenous bank capable of providing for the economic well-being of natives was felt by many Nigerians at that time. Similarly, displeasure against the colonial banks were likewise expressed in former colonies like India, Cylon (now Sri Lanka), Gold Coast (now Ghana), and Malaya (now Malaysia).

Secondly, it has been established, as a fact of life that the socio-economic milieu of dynamic societies constantly undergo the process of regeneration and development. This was the case with Nigeria in the 1930s; when the first indigenous bank emerged. It completely changed the socio-economic landscape of Nigeria. It brought about political and economic changes which steadily rose the level of awareness. Education and the increased contact with Europe, and the innate propensity of Nigerian to trade, generated such current and pressure which become increasingly incompatible with continued dominance of the banking sector of the economy by British banks.

46. Brown, C. V. (1966). *Nigerian Banking System* (G Allen of Union, London) p. 24.

Thirdly, there was the willingness by Nigerians to hold their savings in the form of bank deposits meant that among individual Nigerian traders and the small but growing body of civil servants, and other professionals, there would be a ready response to any effort at setting up banks which could provide finance at rates lower than those charged by money lenders. It was thus secular change in Nigerian financial habits which further contributed to the emergence of indigenous banks.

In the final analysis the emergence of indigenous banking in Nigerian must be seen as an effort by native Nigerians to break the shackles of economic strangulation by adapting the financial system of the country to meet new demands and challenges[47].

2.3.5.1 **Industrial and Commercial Bank**

The first three indigenous efforts made at establishing indigenous banks, up till 1939 were in chronological orders; the Industrial and Commercial Bank, the Nigerian Merchant Bank and the National Bank of Nigeria.

According to Newlyn and Rowan[48] industrial and Commercial Bank appears to have been originally incorporated in England in May 1914, but by 1929 it was wholly African owned and managed. In 1930, this bank went into compulsory liquidation. However, in the absence of detailed and accurate records, not much is to be said of this bank save that its collapsed generated some reservations and bitterness among the indigenous population.

There were speculations among the Native Africans that the failure of this bank had been deliberately engineered by European business and banking interest. This interest, it was further believed acted in concert with the government whose support and approval was not forth coming.

47. Goldface – Irokalibe I. J. *Op. Cit;* pp. 17 – 18
48. Newlyn, W. T. and Rowan, DC, (1954). *Money and Banking in British Colonial Africa* (Oxford, Clarendon. Quoted in Goldface-Irokalibe, I.J. Op. Cit; p. 19.

The above position of the Native Africans hold Water in the sense that even by the admission of the Europeans, Africans, controlled and managed the bank very briefly. The bank came under African control by 1929, and the very next year, 1930, it went into compulsory liquidation. One would wonder why the bank suddenly ran into trouble within so short a time after it changed hands.

It is submitted that in view of the bitter rivalry which characterized the relationship between the bank of Nigeria, and the bank of British West Africa prior to their amalgamation and the then on-going rivalry between the Bank of British West African, and the Barclay's Bank DCO (formerly colonial Bank), that the Europeans certainly viewed with alarm, African entry into the banking business. The European therefore worked against the new African bank in their own selfish interest.

On the government side, they were not unmindful of the effect African economic success in the banking business will have on nationalistic political agitation. It is therefore submitted that it was the common interest of colonial government and European banking interest to team up and torpedo the industrial and commercial bank.

If after four decades of the attainment of nationhood, former colonial masters still meddle in the national affairs of their former colonies, by giving them financial aids with condition attached, largely in their selfish interest, then it is not unthinkable that in the 1930s, European banking and business interest could team up with government to frustrate the existence of the Industrial and Commercial Bank. This is known as Neo-colonialism.

In the light of the foregoing submission, it is strongly concluded that the failure of the Industrial and Commercial Bank cannot rightly be attributed to mismanagement and incompetence, or any probable speculation. Newlyn and Rowan do not sound

convincing on this point and must therefore have their views rejected as biased in the extreme[49].

2.3.5.2 The Nigerian Mercantile Bank

The Nigerian Mercantile Bank was the second indigenous bank to emerge. At inception, it was registered as Nigerian Industrial Cooperative Society. The name Nigerian Mercantile Bank was adopted in 1931. During its five years of existence, it did not attain any remarkable level of progress. With total paid up capital never reaching £1,700 and total deposits only once exceeding £2,000 in 1933[50].

Its eventual liquidation was therefore only to be expected and this happened in 1936, but not much is recorded about it.

Newlyn and Rowan see the presence, on the board of this bank, of the ex-Managing Director of the Industrial and Commercial bank as "an interesting comment on the credulity of the African public in banking matters". This observation according to Goldface – Irokalibe, I. J. is not correct. If anything, it further illustrates the fact that Nigerians saw the failure of the Industrial and Commercial Bank as the handiwork of Europeans and government collusion. Therefore, it was not surprising, that Nigerians felt that they could still trust their fellow Nigerians who they saw as champion of their struggle against financial and economic emasculation.

49. Goldface – irokalibe, I. J. *Op. Cit;* pp. 19 – 20.
50. Newlyn and Rowan, *Op. Cit;* p.99

The general perception was that indigenous banks emerged to help indigenous businessmen overcome expatriate discrimination.

Furthermore, that expatriate banks, (with the active connivance and support of the colonial administration) were out to stifle the growth and success of this new competitors. It is therefore utterly wrong to suggest as Newlyn and Rowan did that the presence of a former Managing Director of the defunct Industrial and Commercial Bank as a new Managing Director of the Nigerian Mercantile Bank was bad. It is nothing other than a show of indigenous solidarity and support for a worthy cause.

2.3.5.3 The National Bank of Nigeria

The arrival of the National Bank of Nigeria marked the effective starting point of the history of indigenous banking in Nigerian. The bank was incorporated in Lagos as a Limited Liability Company on February 11, 1933, with a nominal share capital of£10,000 out of which £1,000 was paid up. Newlyn and Rowan, however, disputed the amount of the paid up capital. They put it as £505 at June 30, 1934 and £1,023 at June 30, 1935[51]. According to them the source of their information was the bank's annual balance sheets. This information is in conflict with the bank's won information contained in a four-page supplement which ran in the Daily Times newspaper of September 30, 1961.

On the occasion of the opening of its new head office on Broad Street, Lagos, in 1961, the supplement which contained the history of the bank written by its management stated the fact that the company was incorporated with a share capital of £101,000 out of which about £1,000 was paid up.

51. *Ibid*; p. 100

The history of this bank is that of courage and sacrifice in the face of odds coming shortly after the collapse of the other two indigenous banks and given the hostility of established British Banks. Similarly, the circumstances were such that the public could easily have lost faith in the capacity of the indigenous Nigerians entrepreneur to undertake the effective organization of banking business. Expatriate banking houses had also constantly tried to foster the belief that only few Nigerians were credit worthy and even this few must be dealt with caution.

It was against this background that Dr. Akinola Maja, Chief Akintunde Adeshingbin, Chief Theophilus Adebayo Doherty, and Mr. Alfred Olatunde Johnson, took the initiative of forming the National Bank of Nigeria and the Mutual Aid Society. The Mutual Aid Society was founded to carry on the business of money lending. It was registered under the money-lenders ordinance, and became an indigenous device designed to carry out the bank's lending business. By so doing, the bank succeeded in keeping itself out of negative publicity should recourse to court became necessary for recovery of loan granted.

As was expected, the bank faced serious challenges as it had to contend with campaigns and attempts by established expatriate banks to stifle it. All the big foreign merchants, without exception refused to extend their patronage to the bank. In March 1955, the Western region government and the bank entered into an agreement which resulted in that government undertaking to lodge forty five percent of its funds with the bank.

In 1956, the government purchased £1million four percent cumulative preference shares in the bank through the Western Region Marketing Board.

In 1960, these preference shares became converted to ordinary shares with a further £2million in ordinary shares put in by the Marketing Board[52]. The bank, against all odds had come to stay.

It is worthy to note that, the National Bank of Nigeria and its Mutual Aids Society featured three ex-Directors of the defunct Nigerian Mercantile bank. These ex-Directors were named as Dr. A. Maja, Mr. T. A. Doherty, and Mr. H. A. Subair[53]. From the above, it is obvious that the immense experience of these three ex-Directors of the Mercantile Bank contributed in no small measure to the success of the National Bank of Nigeria. The bank, by all accounts, grew into an effective banking institution that offered stiff challenge to expatriate banks. A practical display of the experience of the ex-Directors was manifested in the founding of the Mutual Aids Society.

This service was designed to handle the risky lending business of the bank to ensure that the bank was kept out of negative press coverage and court appearances. The success story of the National Bank of Nigeria was a clear refutation of Newlyn and Rowan's claim that the African public was credulous.

2.3.5.4 The African Continental Bank[54].

In the year following the end of the second World War, more indigenous banks were found in Nigeria. One of such banks is the African Continental Bank. The bank commenced business in 1948.

The bank was originally known as "Tinubu Properties" and was taken over by Dr. Nnamdi Azikiwe for the sum of £250 in 1944. The normal capital of the bank stood at £250,000 in 1949, with only £9,623 paid up as at March 31, 1950.

52. Brown, C. V; *Op Cit;* pp. 21 – 28.
53. Newlyn and Rowan, Op Cit; p. 79.
54. Brown, C. V. Op Cit; pp. 28 – 29 and other sources.

From a modest beginning, the African Continental Bank began to show slow but steady progress and by 1955 its paid-up capital had risen to £28,276 in ordinary shares and £3,370 in eight percent cumulative preference shares.

The bank which has been closely associated with the then Regional Government of the East received a boost in 1955. During that year, the Eastern Region Finance Corporation bought 789,200 worth of cumulative preference shares of the bank. These shares were subsequently taken over by the Eastern Region Finance Corporation. During 1960 – 61, these shares were converted to ordinary shares and additional £1million ordinary shares were purchased by the Eastern Region Marketing Board. In 1962, the Marketing Board increased its shares to £2million ordinary shares. Up to the outbreak of the civil war the African Continental Bank ranked as one of Nigerian's largest commercial banks.

2.3.5.5 Agbonmagbe Banks

The Agbonmagbe Bank was what metamorphosed into Wema Bank. It became the second oldest indigenous bank after the National Bank of Nigeria. The Bank was found in 1945 and became the first indigenous competitor to the National Bank of Nigeria.

Newlyn and Rowan[55] were therefore in error when they submit that the first indigenous competitor to the National Bank of Nigeria did not appear until 1947. The bank had a nominal share capital of £10,000 at inception, out of which £2,300 was paid up.

55. Newlyn and Rowan, *Op. Cit;* p. 104.

The bank passed through a period of slow, but relatively stable growth until 1959 when it received a boost in the form of £200,000 cash deposit from Western Region Marketing Board. Out of this amount, £80,000 was later converted into shares[56].

A host of other indigenous banks commonly referred to as "mushroom banks" also emerged. They were founded between 1933 – 1952, when the first Banking Ordinance regulating banking business in Nigeria was passed, most of these banks collapsed in no time, while a few never even opened for business after their registration. They all ceased operation by 1954 with the exception of Merchants Bank. Various writers and reporters have adduced reasons for their failure.

The consensus, however, appeared to be that these banks failed for two more reasons. Firstly, the banks were grossly under-capitalized.

Secondly, there was a tendency towards too rapid expansion. Majority of the banks seem to be in a hurry to expand.

For instance, the Nigerian Farmers and Commercial Banks with a paid up capital of £13,194 had twenty eight offices. The Nigerian Trust Bank with a paid-up capital of £101,000 had twenty six offices while Standard Bank with paid-up of £13,502 had seven offices[57].

Other factors like bad management and inexperience approach to banking and finance were other factors that led to failures of these mushroom banks. Most of these banks came into existence" as a result of the passage of the banking ordinance in 1952.

56. *Ibid*; p. 107.

57. *Ibid*; p. 108.

2.4 The Historical Development of Insurance in Nigeria

In most African countries particularly in Nigeria, modern commercial insurance is less than 100 years old. The British colonial government introduced insurance business into Nigeria in 1910. Traditionally, though some forms of social insurance existed in part of the Nigerian society long before their arrival.

This was in form of mutual and social schemes, which evolved through, the extended family system, aged grades and clan unions typical of African culture.

This simple form of social insurance was practiced by means of cash donations, organized collective labour of assisting one another and the entire community who suffer mishap. The people in the community especially those of the same age bracket collect funds periodically just in the same manner as the industrial life insurance premiums are collected.

Right from the on set, Nigerian culture and indeed African people have seen the reasons to contribute funds to assist members who may suffer mishap such as illness, important ceremonies as child naming, marriage, funeral and all kinds of obligations[58].

The enactment of the Workmen's Compensation Ordinance, 1942 and the Road Traffic Act, 1945 both contributed to the meaningful take-off of insurance industry at that time. Against the backdrop of the fact that Nigerian economy in the 60s was dependent on agriculture, marine insurance was popular for external traders to produce export. Fire insurance was never popular and the expatriates mainly held mortgage security policies.

58. Usman, O. A. (2009). *Scale Economics and Performance Education of Insurance Market in Nigeria.* Meddel Journal, Vol. 4, p. 1.

However, the parliament in the first Republic set up Obadan Commission (1961) to review the situation in insurance industry and was to come up with recommendations.

The outcome of Obadan Commission gave rise to the establishment of Insurance Companies Act of 1961. Arising from this Act, by 1969, Nigeria had registered close to 50 insurance companies, though with foreign donations.

The foreign donation was so serious that both Great Nigeria Insurance Company (GNIC) owned by Western Region and African Alliance Insurance (AAI) company had a meager share of operation when compared with the overall volume of business in the entire industry. This unfavourable trend persisted for a long time that the Federal Government of Nigeria became skeptical as to what future holds for the then insurance industry that was generally dominated by the foreigners. Nigerians were not allowed to hold sensitive positions, which would have equipped them for managerial or technical responsibilities in the industry.

Out of the 25 insurance companies that existed in 1960, only 7 were indigenous and their total market share was far below 10%, as the bulk of the business went to the foreign owned companies. The Nigerian business and economic life were dominated by the foreigners. The fallout from this was the heavy drain on Nigeria foreign exchange earnings. As a result of these problems, a parliamentary committee was therefore, set up in 1964, under the chairmanship of honourable J. Obadan, for another time, to carry out the following enquiries:

(1) To look into the possibility of introducing governmental control for motor vehicle insurance premium.
(2) To find out about premium charges for the insurance of motor vehicles in Nigeria, for comprehensive covers and the third party so as to know the extent to which rates have increased since, 1950.
(3) To know whether the rights of insurance clients are appropriately covered.

(4) To make recommendation to the state.

In the end, Obadan Committee's recommendation could not go beyond sensitization of government over the danger inherent in the foreign domination of insurance industry.

The Nigerian agents were given Power of Attorney to transact insurance business such as issuance of cover and service on behalf of the London Principals. Throughout this period, insurance focuses more on marine insurance and trade rather than overall development of the economy. The situation was disenchanting to Nigeria as trading companies were being granted license to operate as insurance companies especially to supervise claims and to issue covers on marine insurance. For example, in 1919 the Africa and East Trade Companies were both established as Royal Assurance Agency, which later metamorphosised into a full blown insurance companies branch in 1922. This event then opened up the flood gate for Paterzon Zochonis (PZ), General Insurance, Liverpool London and Law Union and Rock to mention just a few. It is pertinent to say that all of these companies were wholly owned by the Britons and for the major purpose of providing insurance services for their trading activities. However, in 1985 the African Insurance Company Limited emerged as the first wholly indigenous insurance company[59].

Between 1985 and 1990, there was an upsurge and a phenomenal increase in the number of insurance companies operating in Nigeria. This proliferation accounted for over 100 companies operating in the market during this period. The need for control and timely intervention of the government led to the formation of the National Insurance Corporation of Nigeria (NICON), which was later christened NICON Plc.

59. Ibid, pp. 2-4

As at 1969, as an apex company, NICON was further empowered to act as the nation's re-insurance company with other Nigerian insurance firms shedding compulsory shares of their business to the corporation.

In compliance with the provisions of the Nigerian Enterprises Promotion Decree of the Federal Government, in 1979, NICON was chosen to participate in the equity share of 14 foreign owned insurance companies to the tune of 49%. In 1977, the indigenous participation increased to 60% and the control of insurance market by the foreigners began to decline. NICON for a long time assumed the monopoly role of government insurance.

The first remarkable risk business of NICON in the insurance industry came up when an A.D.C. 10 aircraft, newly acquired by the Nigerian Airways and insured by NICON crashed at Iju, Lagos State on 25th November, 1989. The 89 persons on board were reportedly killed in the crash, NICON demonstrated its insurance ability by the settlement of the huge claims. Shortly after this episode, there was a phenomenal increase in the number of insurance companies in Nigerian financial market. This was coupled with the fact that in 1986, Structural Adjustment Programme (SAP) brought about the emergence and proliferation of financial institutions, especially, commercial banks and insurance companies. To streamline insurance business activities and stem the upsurge of the mushroom insurance companies, insurance capital base was raised. Fall-out from this event was that only 57 out of 152 insurance companies qualified for registration. This was coupled with tighter control over the industry that requested for provision for the licensing and control of insurance intermediaries. Generally, sanity was meant for the insurance market through this legislation and control of insurance intermediaries.

Insurance, as a formidable financial sector in Nigeria economy has grown by leaps and bounds in terms of market size and premium income generation. For instance, a

Gross Premium Income (GPI) of 124 million was realized in 1975 but rose to 189 million in 1976 and 290 million in 1977.Although, the gross income increased also to 372 million in 1988, it fell to 314 million in 1979. The performance of Nigerian insurance industry in the last 2 decades has been remarkable, increasing its gross premium income by well over 250% within the first one decade. In 1991, Nigerian insurance market was dominated by 188 companies and 299 insurance brokers. The gross premium for the first ranked insurance company, NICON was closed to 2 billion and the total gross premium income for the entire industry was well above 42 billion (NICON 1969 – 1994), but this amount grossly fall short of enormous risk businesses which insurance companies have undertaken in the economy.

Arising from the above facts, Nigerian insurance market is free but not operating optimally. The new entrants are always ready to float a new business and further deepen the competition. The foregoing therefore, suggests that despite the numerical growth and to some extent, expansion in the insurance industry in Nigeria, the insurance market require a thorough empirical investigation to determine the cost structure and optimal production levels in which an insurance company can efficiently operate. The knowledge of this cost efficiency study serves to help insurance regulators, practitioners and the industry to identify the policies and strategies that could be deployed to salvage the industry and make the insurance sector contribute effectively to financial market development of the Nigerian economy.

In the invent of deregulation policy especially restructioning and recapitalization in the financial sector of the Nigerian economy, most financial institution were hired to operate in an increasing competitive environment. This trend might subsist for long as government policy is geared towards competitive market based on privatization, commercialization, and deregulation. The need to meet up with capitalization requirement of the Central Bank had engendered consolidation

process, which in turn, has brought about mergers, acquisition and raising of more capital through the stock market.

The insurance sub-sector is not exempted from this reform. For instance, the insurance regulatory institution in Nigeria, National Insurance Commission (NAICOM 2005) specified guidelines which insurance firms must meet alongside with the new capital bases. According to the guidelines, insurance firms handling life assurance business will have 2 billion capital bases, while those ones in composite business attract 3 billion. Insurance firms in reinsurance business would have to raise their capital base to 10 billion. Using 2005 as base year, these increments represent 1.233% for life insurance, 1.400% for general insurance and 2.757% for reinsurance business. At various fora, NAICOM has reaffirmed the need for re-capitalization of insurance sector so that they would be financially strong to effectively cover all kinds of risks associated with development efforts in the economy. This need becomes more important in view of recapitalization that has taken place in Nigeria banks[60].

2.4.1 Formation of Insurance Contract

In most respect, an insurance contract is the same as any other commercial contract and to that extent, to be valid and enforceable, it must possess all the essential features of a contract. There are however, certain peculiar characteristics of the insurance contract that makes it different from other contracts.

The first is that insurance contracts, like wagering or betting contracts, are aleatory contracts in the sense that they are based on chance and uncertainty.

60. *Ibid*, pp. 5 – 11.

The main difference however between an insurance contract and setting or wagering contract is that an insurance contract is legally valid because of the element of insurable interest, which distinguishes it from the wagering contract, which is illegal and unenforceable. Other features of insurance contract that distinguishes them from other commercial contracts include such fundamental factors as the utmost good faith principle, and the principles of indemnity and insurable interest, amongst others.

Apart from the special features, insurance contract, like all other contracts are also subject to the general rule that the first step in the making of a contract is the existence of an unqualified offer followed by an unqualified acceptance, supported by all other essential features of a valid contract, such as the element of consensus

ad idem, valuable consideration, legality and an intention to create legal obligations, amongst others[61].

2.4.2 Insurance Contract must Satisfy Essential Features of a Valid Contract[62]

In view of the peculiar nature of insurance contract, it must satisfy all essential features of a valid contract as well as those special requirements of insurance contracts in order to enjoy the protection of the law.

To this end, it has to posses the following characteristic:

(a) **There must be an agreement base on Offer and Acceptance**

There must be an offer made either by the insured or the insurer,

61. Irukwu, J. O. *Op. Cit*; p. 29.
62. *Ibid*, p 29.

(b) **There must be an agreement base on Offer and Acceptance**

There must be an offer made either by the insured or the insurer, followed by an unqualified acceptance of that offer by the other party to the insurance contract. In practice the first offer generally comes from the proposer and to be effective, it must be communicated to the insurer who must be seen to have accepted the offer. Although, the offer may be oral or in writing, the most common method in modern insurance practice is the completion and presentation of a proposal form or a slip. On receipt of the completed proposal form, the insurer may accept the offer or decline or may "accept" the offer with qualification, in which case the "acceptance" may, in law, amount to a counter offer which must be accepted by the proposer before it can be held that there has been a valid offer and acceptance.

Insurers, sometimes make the first offer either by writing to the prospective insured with quotations inviting him to insure with them or by writing to the insured inviting him to renew an expiring cover under an existing insurance contract. When an offer has been made and accepted, there is a binding offer and acceptance and once all the other essential requirements for a valid contract have been met, there is a binding contract of insurance.

For the acceptance to be effective, it must comply with the general rule of the law of contract that acceptance of an offer is effective only when it has been communicated to the offeror. There are three important exceptions to this general rule, especially from an insurance view point. The first is where an offer is unilateral. In such a case, there is a valid acceptance if the person whom the offer is made simply proceeds to perform in accordance with the terms of the offer. The example cited by most of the authorities in this regard are those instances in which newspapers and posters feature advertisements offering accident insurances to travelers. Most of those advertisements are in the form of unilateral offers of coupon insurances against injury or death during air, sea, or land journeys. The

legal position is that the provision of such insurance is a unilateral offer by the insurer, which the proposer is assumed to have accepted just by filling in the relevant details as requested by the form. Claims arising from such insurance after the proposer has responded appropriately to the terms of the unilateral offer must be settle by the insurers in appropriate cases. The second example is where an insurance policy has been issued under seal. The third possible example is where an offer or counter offer is made, and an insured acts relying on the offer.

In such a case, the insured will be regarded as having accepted the offer even in the absence of express communication. Although, the general rule regarding the communication of acceptance does not suggest that silence or delay as such, constitute acceptance, this is the principle that seem to have been established by most of the reported cases on the subject especially by the English courts.

In the English case of **Rust V. Abbey Life Assurance Co**. **Ltd**[63]. the proposer for a linked life policy had retained the life policy for seven months before she decided to dispute the type of life policy that had been issued to her by the insurer. In rejecting the type of policy given to her, she claimed that she had been misled by the insurer's agent.

The court held that even if she had not made an offer to the insurers which they had accepted by issuing the policy, which the court considered was the case, the insurers' issue of the life policy was an offer, which she had in effect, accepted by virtue of the fact that she had done nothing and failed to take any action on the matter for seven months after receiving the policy.

63. (1979) 2 Lloyd's Rep 33.

(c) **The Contract must be Legal in all Respects**

Having settled the issue of offer and acceptance, the next essential requirement for a valid insurance contract is that it must be for a lawful purpose and must be legal in its form. The two contracting parties, the insurer and the insured must have intended to create legally binding obligations.

The parties to the contract must be legally capable of contracting. As a general rule, infants and persons of unsound mind are not capable of contracting. There are however, some exceptions to this rule which also relate to insurance contracts.

(d) **There must be either a Valuable Consideration or Form**

The term valuable consideration, in this context means that each side must give something of value for the promise of the other. In an insurance contract, the consideration on the part of the insured is the premium he pays to the insurers, and the consideration on the part of insurer is his promisee to pay in the event of a loss. A gratuitous promise is not a contract and cannot ordinarily be enforced in a court of law, because the prospective receiver or promisee has given no consideration. But such a promise can be enforced if there is form, that is, if the agreement is under seal and signed, seal and delivered.

(e) **There must be an Agreement base upon an Equality of Knowledge of all the Material Facts.**

There must be consensus ad idem, which means that the minds of the parties must be in one accord. If the insured at the time of negotiation thought he was buying a personal accident insurance, and the insurer though he was selling a motor car insurance, there is no contract between the parties as their minds were not in one accord at the material time.

2.6 Challenges of Deposit Institutions in Nigeria

Banks in Nigeria are today plagued with several problems which have hampered their growth and the development of the economy. The economic development of every nation, no doubt, is premised on having strong banking system. Bank play a key role in the distribution of financial resources to the rest of the economy and act as a repositories for the public's saving. Some of the problems facing banks in Nigeria ranges from banking malpractices to the challenges in the computerised banking environment. According to Goldface – Irokalibe; there are three categories of banking malpractices.

They include malpractice by bank employees, those by outsider i.e. (non-bank employees), and those committed by banks themselves as corporate bodies[64].

(i) Malpractice by Bank Staff

Banking malpractices perpetrated by bank employees consist largely of, but by no means exclusive of the falsification of entries of account of customers with a view to siphoning the excess proceeds or shortfall; forgeries of signatures of accounts, deliberate distortion of records of loans and other transactions, cash theft by bank officials, more especially those in charge of cash, and in some cases even those in the top management levels was not left out. Banks staff also engage in the following malpractices; forged cheques, forged letters of credit, forged mail and telex transfers, suppression of cash, foreign exchange frauds, unauthorized printing of bank stationeries, unauthorised carving of bank rubber stamps, double pledging, wrongful clearing of cheques, issue of cheque books, and some forms of counterfeiting.

64. Goldface – Irokalibe, I. J. *Op. Cit*; p. 175.

Cash malpractices engaged by bank staff take several forms. From outright cash theft from unsuspecting cashiers by their colleagues to suppression of cash by cashiers themselves. Managerial theft may take the form of removing cash from strong rooms or replacing strong rooms money with counterfeit currency notes.

Forgery involves the illegal and unauthorized adjustment of the amount of a cheque, or the signature of the account owner or even the alteration of the date on an otherwise state cheque or other negotiable instrument. These occur mainly on corporate accounts, and are invariably committed by insiders having access to the company's cheque book, in collusion with fraudulent staff of drawee banks[65].

Under sections 70 and 73[66] of the Companies and Allied Matters Act, if an Officer or Agents of a Corporate body commits fraud using forged cheques, while acting or purporting to act in the course of the company's business, the company is bound. This, of course, presupposes that he is authorized, or held out as authorized to transact business on account of his employer or principal. In the circumstances, employer though innocent of the fraud, is liable for the fraud of the Officer or Agent.

In addition, the procedures of granting, recording, and monitoring of loans and advances to customers are plague with fraud and forgeries. Loans and advances granted by banks soon acquire the status of "bad and doubtful debts". This is due to the manipulations of fraudulent bank staff who sometimes, with the active and guided co-operation of borrowers, create and/or exploit procedural loopholes at the detriment of the bank and for their private gains.

65. Ibid, p. 176.
66. Companies and Allied Matters Act, Cap. 59, LFN, 1990 (Now Companies and Allied Matters Act, Cap. C20, LFN, 2004).

Loan frauds may take the form of outright grants to unintended and unqualified borrowers who, aided and abetted by senior bank staff that may be friends, relatives, and even business partners, make false declarations to mislead the bank. These false declarations may be made outright with the intention to defraud. Some other frauds associated with the processing of loans and advances are "legal" difficulties built into the enforcement of bank's rights in relation to perfection, enforcement and realization of securities, such as rights under mortgages. This right may suffer undue delays or other manipulations which eventually frustrate the bank's title to mortgaged property.

Other malpractices engaged by bank staff include suppression of cheques in clearing, interception of telex messages meant for transfer of funds under international commercial, and other transactions with the object of diverting the proceeds into their own foreign accounts. Very senior categories of staff only can engage in this form of malpractice. Finally, there is the ever present case of granting unauthorised overdraft, and fabrication of records to hoodwink inspectors and auditors. In the case of **Akwulev. R** the Appellant, a Manager of the Fagge Ta Kudu Branch of the Bank of West Africa, in Kano, was alleged to have given large sums of bank money to his co-accused. In an effort aimed at defrauding the bank, he caused false entries to be made in the bank's ledgers so as to conceal the truth from the bank inspectors. He was convicted of criminal breach of trust. Although, on appeal, the conviction was set aside on a purely technical ground of his not being a "banker" as provided for under sections 315 of the penal code[67].

67. Goldface – Irokalibe, I. J. *Op. Cit*; pp. 176 – 181.

(ii) **Malpractices by Non-bank Staff**

It is not an easy thing for an outsider to defraud a bank without the active or passive connivance of an insider or insiders within the bank. A majority of malpractices by non-bank staff are aimed at merely using the bank's name as a cover for external frauds. These frauds may not result in direct final losses, but impinge upon the good reputation of Nigerian banks in view of their damaging consequences.

For example, it is a common knowledge that confidence trickers, fake businessmen and women, as well as port agents, produce forge letters of credits and spurious bank drafts purportedly issued by Nigerian banks with the aim of recovering large consignment of goods, and other supplies from overseas manufacturers and traders, which are never paid for. Allied with this, is the practice of printing bank stationeries carving bank rubber stamp and use of fake letter-headed paper of banks.

The effect of this is that when genuine transactions are undertaken, they become suspect. The fear of losing to dupes generates a sense of insecurity in foreign business interest who as a result, are reluctant to do business with Nigeria.

Finally, the element of corruption which has afflicted the larger society is now found in the bank. Corrupt bank customers provide bank staff with inducement. In cash or kind with the aim of procuring loans, advances, or credit facility from the bank. It may also be done with the object of securing a permission to overdraw an account with the bank, without proper authority or compliance with the rules and guidelines for that purpose.

Another reason for engaging in such corrupt practices is the desire to have negotiable instruments discounted or to have any other obligation by the bank temper with, positively or negatively in favour of any person. This may bring about sudden disappearance of documents relating to a loan transaction with a view to having it written off as bad debt[68].

(iii) Malpractice by Banks

Among the principal kinds of malpractices perpetrated by banks, is the breach of Central Bank Policy guidelines. These guidelines may be in relations to credit policy, interest rate policy, foreign exchange, cash reserves, and investment policy among others.

Pursuant to its powers under section 16 – 22 of the Bank and Other Financial Institution Act, as well as under section 28 of the Central Bank of Nigeria Act, the Central Bank of Nigeria exercises various forms of control over other banks within the Nigerian banking system through its policy guidelines.

Central Bank policy guidelines cover such areas like aggregate credit ceiling, sectoral allocation of commercial and merchant banks loans and advances, structure of merchant banks loans and advances, structure of merchant and commercial banks assets, as well as loans to rural borrowers. Other areas include loans to small-scale wholly Nigerian owned enterprises, grace periods on loans for agriculture, loans for residential building, and reserve requirement.

Additional areas that attract guidelines include interest rate policy, capital funds adequacy, banks equity holding in companies, banks obligations, and foreign guarantees and currency deposit as collateral for naira loans.

68. Ibid, p. 182.

In spite of all these guidelines put in place by the Central Bank, Merchant and Commercial Banks more often than not, take steps to evade some of these guidelines with a view to making higher profits. For example, at the maiden official foreign exchange sale of the year 1994, twenty-two banks were found to have applied for far more foreign currency that their customers demanded.

Three banks for instance applied for between ninety-five and one hundred and fifteen million dollars whereas their customers requested for between thirty and forty million dollars. Such excess foreign exchange eventually gets diverted to the parallel market where they are sold at twice the official rates. This is a clear violation of foreign exchange guidelines[69].

These and other malpractices by banks are well known to the Central Bank. Provisions for penalties for default by banks have been put in place by the Central Bank. The Central Bank guidelines equally make provision for fines with respect to banks that default in rendering statutory and other returns.

Violation of the Central Bank policy guidelines by banks is a perennial problem in the Nigerian banking system. It is a well known facts that virtually all banks do not like paying interest on current accounts. Item 9 of the Central Bank credit policy guideline for the 1990 fiscal year dealt with interest rate policy. It provides thus:

> *Consistent with current policy, banks shall pay interest on current accounts deposits. The rate of interest, payable shall be subject to negotiation between banks and their customers*[70].

69. *The African Guardian Magazine*, Vol. 9, No. 9, March 7, 1994. p 1.
70. Central Bank of Nigeria. Credit Policy Guidelines for 1990 Fiscal Year. (CBN Lagos), 1990. pp. 18 – 19. Quoted in Goldface-Irokalibe, I. J. *Op. Cit*; p. 182.

Contrary to the above guidelines, banks did not hold any meetings with their customers to fashion out rates of interest payable on current accounts.

In conclusion, banking malpractices have devastating effects on the national life of any country. They affect the depositors, the other creditors of the banks, the banks themselves, and the national economy at large.
The victims of banking malpractice cut across every segment of society. From the small peasant savings account holder, to the corporate customers, and governments at all levels. Persistent stealing, swindle, and other aggravated frauds result in bank failures, and collapse.

The[71] "multiplier effect" of the bank failures then inevitable manifests itself in the form of ruined businesses, lost of life savings, breach of contractual engagements, loss of valuables, loss of jobs, and the consequential social traumas as well as various concomitant unfulfilled hopes and aspirations they engendered. On the part of the banks, huge losses may occur which threaten the profitability of and the safety of investors capital and business endeavours.

Reduced returns on investment in banking may lead to flight of capital into other sectors, should shareholders and promoters lose confidence in the banking industry. In the final scenario, banks beset with fraud and sundry malpractices simply collapse under the weight of these evils.

71. Central Bank of Nigeria; *Credit Policy Guidelines for 1990 Fiscal year* (CBN Lagos), 1990 pp. 18 –19. In this account of malpractices by banks, the base year of 1990 has been deliberately chosen for two main reasons. First to show that such malpractices have been on for decades and therefore not a new phenomenon. Secondly to illustrate the Central Bank's dynamic approach to this phenomenon as revealed by its review of the guideline as circumstances demand from time to time.

The impact of banking malpractices on the economy at large can be disastrous. The present state of human misery prevalent in Nigeria, which is a direct consequence of our economic failure, can be attributed to bank troubles.

When banking malpractices come to a head, there is a general loss of confidence in the use of negotiable instruments as means of settling contractual and other obligations. The resultant result of loss of faith in the banking system engenders a slow down of the local economy and suspicion abroad in international commercial and economic circles. Letters of credit, bank drafts, bill of exchange, and other instruments of international commerce emanating from local banks would be routinely suspected abroad as being fake.

Banking malpractice also result in negative economic growth when projects have to be abandoned on account of lack of funds which may have been siphoned abroad through collaboration with foreign interests. Poor economic performance result in poverty and misery as the economy is unable to cope with the demand for jobs, production and consumption of goods and services. Nigerians current economic woes, may, without doubt be said to owe in part, to the banking malpractices of a by-gone era, when spurious foreign debts, and inflated import bills were incurred for goods and services that were never rendered to the nation.
Sadly enough, all these unholy spoliation took place with the active connivance, and in some cases, the passive connivance of Nigerian banks[72].

72. Goldface-Irokalibe, I. J. Op. Cit; pp. 187 – 188.

(iv) **Weak Corporate Governance**[73]

Corporate governance provides structure and processes within which shareholders, directors and management conduct the business of a bank with the ultimate objective of realizing long-term shareholder value while taking into account the interests of other stakeholders. Good corporate governance demands not only transparency, accountability and probity, but also a sense of conviction and commitment to ensure that the interests of all parties are protected. Weak governance and/or mismanagement played a major role in bank failure in Nigeria. A number of factors which contributed to mismanagement include the following;

(a) Inexperienced and incompetent personnel were recruited to hold key positions in banks. As a result, most of them lacked the ability to respond to the rapidly changing economic conditions and regulatory framework. The recently issued guidelines by CBN on minimum qualifications for top-management of banks is therefore a welcome development.

(b) Weak internal control systems characterised the operations of many distressed banks. Even where the controls were in place, they were not being complied with. Internal Audit or Inspection functions were weak and sanctions were not imposed on erring officers. The consequences of weak internal controls were clearly reflected in the volume of frauds and forgeries.

(c) Non-compliance with laws and prudential standards. Management of many bank failed to comply with prescribed code of conduct and also failed to keep proper books and accounts in contravention of applicable banking laws, rules and regulations.

73. Ogunleye, G. A. Op. Cit; pp. 61-62.

(v) Weak Risk Assets Management Practices[74]

A number of banks had poor credit policies and in cases where good policies were in place, they were not faithfully implemented. Loans were granted without due regard to ability of borrowers to repay. Several loans were granted without collateral and even where secured, the collaterals were found to be inadequate or non-existent. Credit administration was also found to be weak as credits were not being properly appraised and monitored. Consequently, these weaknesses largely impaired the quality of the loan portfolios of the banks.

(vi) Inadequacy of Capital[75]

The banking industry witnessed a steady and large scale deterioration in capital positions until 1998 when a large number of banks were closed. The capital deficiency is a result of many factors. First, some of the banks were established with inadequate capital and failed to increase their capital base to meet the growth in their risk assets portfolios.

Increased provisions for loan losses as a result of increasing level of non-performing loans further eroded the capital funds of many banks. Some shareholders whose banks were insolvent refused or were unable to recapitalise them. They also made unrealistic offers to new investors who sought to acquire and recapitalise them.

74. Ibid, pp. 62-63.
75. Ibid, p. 65

2.7 Distinction Between Deposit Insurance Scheme and the Conventional Insurance System

The concept and operation modalities of the DIS were still being confused with those of conventional insurance business for protection against fire, marine losses, motor accidents, et cetera which started as far back as early 1920s in Nigeria. In conventional insurance, for example, the premium charged is supposed to be commensurate with the perceived level of risk inherent in the insured person, property or organization.

Also, participation is usually voluntary. The same are not true for a DIS. Again, the risks associated with debt obligations arising from deposit mobilization by deposit-taking financial institutions are quite different from those associated with contingent nature of conventional insurance contracts. The confusion had in the last twenty years resulted in some of the challenges which the corporation had faced, particularly in the area of coverage, its mandatory nature and even the premium rate charged[76].

The corporation is not a conventional insurance company but a deposit insurance agency with mandate to guarantee deposits of less financially sophisticated depositors, especially the small ones, against the loss of their funds when a deposit-taking financial institution fails. It is also noteworthy that in a DIS unlike in ordinary insurance, the insured institutions pay the premium for the benefit of the depositors[77].

76. Ogunleye, G. A.*Op. Cit;*(2009). pp. 181 – 182.
77. Ademola, G. *Op. Cit*; p. 4.

CHAPTER THREE

LEGAL FRAMEWORK FOR THE REGULATION OF DEPOSIT INSURANCE IN NIGERIA

3.9 Introduction

The period between 1947 and 1952 in Nigeria witnessed rapid growth of indigenous banks in Nigeria. This was before the establishment of CBN in 1959, a year before Nigeria's political independence. The increase in the numbers of indigenous banks was followed also by a high rate of failure of such banks. By 1954, twenty-one (21) out of twenty-five (25) indigenous banks operating in Nigeria had closed doors.

The failure was attributed largely to mismanagement of the banks, lack of adequate capital, and inexperience personnel. The country did not have a central bank at the time to monitor the operations and capitalization of the banks. There were no adequate regulations and/or legislations for the banking industry until the promulgation of the 1952 Banking Ordinance.

3.10 Historical Development of Deposit Insurance in Nigeria

As one of the most strategic financial intermediaries in any economy, government the world over normally takes interest in the stability of the banking system for several macro-economic reasons. These reasons include the need to protect the payment system from complete breakdown and also to avoid a sharp reduction in the saving rate so as not to stifle investible funds.

Repeated cycles of banking instability as experienced in those economies with much older banking history like the United States of America (U.S.A.) and Argentina resulted in great economic losses. This taught the lesson that for as long as certain negatives factors both within and outside the banks' control continue to exist there would continue to be waves of banking instability. The DIS was one of

the institutional arrangements developed to stem such instability by not just taking pre-emptive measures, but by also providing the framework for orderly resolution of the situations whenever they inevitably occur[78].

The evolution of elaborate DIS can be traced to the United States Congress which created the Federal Deposit Insurance Corporation (FDIC) in 1933 following the Great Depression that was experienced worldwide between 1929 and 1933.

Before the establishment of the FDIC in the USA, Deposit insurance was first introduced by some states in the United States of America to protect bank notes. Those States were Vermont**,** Michigan**,** Indiana and New York before 1842, while Lowa and Ohio started theirs 1842. Eight more states later joined the league. The scheme was not uniform across these states as the practices differed with respect to certain operational issues like membership and ways of assessing insured bank. The experiment was a success in some of these states while it failed in others[79].

Finland and the former Czechoslovakia (now Czech and Slovak Republics) established their nationwide DIS in 1924. The Finland's scheme was established for the savings banks and the scheme was extended to co-operative banks in 1931 and commercial banks in 1965.

It was made compulsory for all banks in the system as from 1969. The Czechoslovakia scheme was introduced largely to help revitalize the country's banking sector that was devastated by the First World War and to shore up savings deposits. The scheme was jointly funded by both the participating financial institutions and the government[80].

78. Peter, N. U. Op. Cit; p. 34.
79. Ibid, p. 35
80. Ibid, p. 35.

On the African continent, explicit DIS was only recently embraced, Nigeria took the lead in 1988 with the establishment of the Nigeria Deposit Insurance Corporation (NDIC). The step was informed by five considerations including the lesson of its history of bank failures.

The NDIC has its origin in the report of a Committee set up in 1983 by the Board of Central Bank of Nigeria (CBN), to examine the operations of the banking system in Nigeria.

The Committee in its report recommended the establishment of a Depositors Protection Fund (DPF). Consequently, the Nigeria Deposit Insurance Corporation(NDIC) was established through the promulgation of Decree No. 22 of 15th June 1988. This was part of the economic reform measures taken by the then government to strengthen the safety net for the banking sector following its liberalization policy and the introduction of the 1986 Structural Adjustment Programme (SAP) in Nigeria.

The phenomenal increase in the number of banks from 40 in 1986 to 120 in 1992 led to increased competition amongst banks leading to sharp practices, people of questionable integrity becoming bank owners, managers and inadequate manpower.

All those led to serious breakdown in corporate governance and boardroom squabbles. The unpredictable policy environment, downturn in the economy and political upheavals at the time, also exacerbated the difficult situation. The banking industry was therefore, already in distress by the time the corporation commenced operations in March 1989. NDIC operated under a difficult terrain at the time and was immediately saddled with the management of distress in the banking industry to avert the impending systemic crisis and its resultant consequences. Some of the measures taken by the corporation at the time to manage distress in the interest of Depositors and the system included:

(i) Moral Suasion; continuous interaction with bank managers/owners.

(ii) Imposition of Holding Actions on distressed banks to restrict operations and encourage self-restructuring; about 52 distressed banks had Holding Actions imposed on them.

(iii) Rendering financial assistance to banks; in 1989 alone, NDIC in collaboration with the CBN granted facilities to the tune of N2.3billion to ten banks with serious liquidity problems.

(iv) Take over management and control of 24 distressed banks between 1991 and 1996.

(v) Acquisition and restructuring of seven (7) distressed banks which were handed over to new investors in 1999 and 2000.

(vi) Implementation of the Failed Bank Decree No. 18 of 1994. At the end of 1990, about one out of every two banks in Nigeria was distressed. The Decree was intended to assist distress banks recover their classified assets and punish the malpractices that contributed to the distress. As at June 1996, the corporation had recovered about N3.3billion.

The NDIC is an autonomous body (i.e. an independent agency of government) which acts as an additional supervisory authority over licensed banks and other deposit-taking financial institutions.

The NDIC not only provide financial guarantee to depositors in case of failure but also ensures that banks comply with regulations and practices which foster safety and soundness in the financial market.

The NDIC is empowered to apply sanction and corrective measures when lapses are observed in the operations of insured banks. It is also empowered to undertake the liquidation of failed insured banks when so appointed by the CBN[81].

81. http://www.ndic.org.ng/ndic-history.html, Accessed April 12, 2013, 14.00hrs.

3.11 **Reasons for Establishing the Corporation**

The idea of a deposit insurance scheme in the country was first mooted in the early 1980s when the Federal Government of Nigeria (FGN) was contemplating the implementation of a Structural Adjustment Programme (SAP) in which the deregulation of the banking system would constitute a central pillar. The thought of deregulating the banking system brought memories of the late 1940s and early 1950s when the mushrooming of banks was accompanied by mass bank failure. At the same time, government knew that there were other countries which had successfully implemented deposit protection schemes at various points of their respective economic history which could provide useful lessons for Nigeria. Thus, the decision by the Federal Government of Nigeria to establish insurance scheme in Nigeria was informed by at least four considerations, namely; the bitter experience of prior bank failures in Nigeria in the 1940s and early 1950s, the anticipated consequences of the economic reforms to be introduced by government, the lessons of other countries' experiences with deposit insurance schemes and the need for a strengthened bank supervisory system to complement the efforts of the CBN. Those reasons are briefly examine further.

3.11.1 **Lessons of History:** Experience of prior bank failures in Nigeria

The experience of bank failure in the 40s and 50s in Nigeria was a sad affair for bank officials, depositors and regulators. Consequently, government did not want Nigerians to re-live such experience. Thus, after the establishment of the CBN in 1959, the Federal Government of Nigeria had, since the mid 1960s, ensure through direct support of banks that the Nigerian banking public was no longer exposed to the hazard of bank failures. In this respect, the CBN had deliberately pursue certain measures to prevent bank failures. Those include the requirement that every licensed bank should create and maintain a statutory non-distributable reserve fund from its yearly profits before dividend payments, stipulation of minimum liquidity ratio and capital requirements as well as the rendition of statutory returns in CBN.

In spite of these measures, experience showed that the capital of some banks were seriously eroded by doubt and doubtful debts as a result of inept management and political interference.

With this background of history of bank failure in Nigeria, it was decided that the establishment of a deposit insurance scheme was urgently needed. Such a scheme, it was envisaged, would serve as a means of eliminating the link between the fate of depositors, particularly the small ones, and the fate of their banks so that there could be no reason for insured depositors to panic at the first sign of a banking problem.

3.11.2 **Lessons from Other Countries:** The establishment of the corporation was also informed by the approach which some other countries adopted to ensure banking stability. The lesson from the experience of Czechoslovakia and the United States of America were particularly relevant.

Czechoslovakia was the first country to establish a nationwide deposit insurance scheme in 1924, principally as a measure to revitalize the country's banking system after the ravage of the first World War. In addition, the scheme served to encourage saving by increasing the safety of deposits and ensuring the best possible development of banking practice in that country.

Similarly, the United States of America established the Federal Deposit Insurance Corporation (FDIC) in 1933, over one-third of commercial banks, mostly small, unit banks, failed. Some intrinsically sound banking institutions also failed because of the contagion. The United States of America responded to the problem by establishing the FDIC and by instituting intensive formal regulations for banks which included limitation on the payment of interest, substantial regulations over the portfolio structure of banks, among others. Today, extensive deregulation has taken place in the U.S; but the FDIC, true to its mission, has attempted to make each incident of bank failure an isolated case and to minimize the effects on the

American financial system, thus engendering public confidence in the system. The FDIC has since provided the abiding lessons and model for most countries which subsequently introduced formal deposit insurance scheme in response to anticipated changes in economic and banking conditions. Since Nigeria was at the threshold of fundamental changes in the economy and the banking sub-sector, the authorities reckoned that the country might benefit from the chastening experience of FDIC.

3.11.3 **Anticipated Consequences of Economic Reforms on Banking Supervision.**

The Structural Adjustment Programme (SAP) embarked upon by the government in 1986 was aimed at deregulating the economy on the direction of market-determined pricing. It was envisage that since deregulation would involve the liberalization of the banking licensing process, there would be a substantial increase in the number of licensed banks to be supervised by the CBN. The establishment of an explicit deposit scheme with supervisory power over insured institutions was expected to complement the supervisory effort of the CBN.

Indeed, since the establishment of the Corporation in 1989, it has been possible for both institutions (the CBN and NDIC) to carry out routine and special examinations of licensed banks. The banks are now examined at least once a year as against the two or more years prior to the establishment of the corporation.

3.12 **Mandates of the Corporation**

The International Association of Deposit Insurance (IADI) in 2007 at Basle, Switzerland defined the mandate of an organization as the legal duties it has to undertake in performing the tasks necessary to achieve its public policy objectives. It went further to assert that a mandate defines the roles and responsibilities of the organization and could be used to identify the powers and the authorities confer on the organization to carry out its roles and responsibilities in its attempt to achieve its public objectives. Deposit insurance mandates range from reactive narrow ‘pay

box' mandates (concentrating on reimbursing depositors of failed institutions) to those of 'risk minimizers' with broad mandates that include risk assessment and management, failure resolution and supervision amongst other main ones. From inception, the DIS in Nigeria was established as a risk minimizer with core mandates to guarantee deposits of insured institutions, carry out supervision of insured institutions, partake in failure resolution processes and liquidate failed insured institutions[82].

These core mandates and the ensuring roles and responsibilities of the corporation are as contained in part four of the enabling Act.

3.12.1 **Deposit Guarantee**

Deposit guarantee or deposit insurance is a key and distinct role of the corporation. Under the repealed Nigeria Deposit Insurance Corporation Act, No. 22 of June 1988, the Corporation had the mandate to guarantee the payment of deposit up to a maximum of N50,000 to a depositor in the event of a failure of an insured institution.

That maximum deposit insurance coverage limit lasted till 2005. By 2006, the Nigeria Deposit Insurance Corporation (NDIC) Act, No. 16 of 2006 in section 20(1) increased the coverage level to N200,000 for depositors of failed licenced banks and set N100,000 for depositors of other deposit-taking financial institutions in the event of the revocation of operating licence of the bank or other deposit-taking financial institutions[83]. The Corporation finances the guarantee mainly from the yearly premiums collected from all licenced deposit-taking financial institutions.

82. Ogunleye, G. A. *Op. Cit; pp. 14 – 15.*
83. Op. Cit; S. 20(1), NDIC Act.

Notwithstanding, the provision of Section 20(1) of the enabling Act and subject to the approval of the Board, the Corporation shall have power from time to time, to vary upwards the maximum amount which a depositor shall receive from the Corporation in respect of deposits of failed insured institutions[84]. Where the licence of a failed institution is revoked, payment of the insured deposit in such institution shall be made by the Corporation within 90 days either by cash, negotiable instrument or making available to each depositor a transferred deposit in another insured institution in an amount equal to the insured deposit of such depositor[85].

3.12.2 **Banking Supervision**

Generally, banks are supervised to protect depositors, ensure stability of the banking system, ensure effective and efficient payment system and also to promote competition and innovation in the banking system. Given it broad mandate as risk minimizer, supervision comes naturally as a key mandate of the corporation and this is contained in sections 27-32 of the enabling Act.

The Corporation carries out supervision of insured institutions in order to reduce the potential risk of failure and ensure that unsafe and unsound banking practices do not go unchecked. It also provides oversight required functions to preserve the integrity of and public confidence in the banking system.

The Corporation carries out its supervisory responsibilities through off-site surveillance and on-site examination of insured institutions' books and affairs from which exceptions are reported and recommendations made on how observed lapses should be corrected.

84. Ibid, S. 20(2), NDIC Act.
85. Ibid, S. 21(1), NDIC Act.

Given that the Corporation and the CBN have supervisory powers, the two institutions collaborated in the discharge of their supervisory duties. Over the years, they had developed comprehensive framework which had eliminated role conflict and duplication of effort by the two institutions[86.]

3.12.3 **Bank Failure Resolution**

Bank failure resolution refers to the set of principles, opinions or measures adopted by the bank supervisory authorities to resolve the distressed condition of an insured institution. The distress could be liquidity problem, capital deficiency management weakness, etc.

The main objectives of failure or distress resolution are the maintenance of public confidence and stability in the banking system, by minimizing the risk of loss of depositors fund and achieving minimum disruption in the payment system. There are essentially two broad forms of failure resolution;

(i) Open bank assistance and

(ii) Closed bank resolution[87].

(i) Open Bank Assistance

In Open Bank Assistance, all efforts are geared towards the rehabilitation or resuscitation of a distressed bank, with a view to restoring it to a viable status with adequate capital and sound management. In that regard, the NDIC and the Central Bank of Nigeria either jointly or severally may adopt a number of Open Bank Resolution measures like;

(a) Granting of financial assistance which could be in form of loans, guarantee for loans or the grant of accommodation bill facilities. This type of support is generally appropriate where the bank is suffering from temporary liquidity constraints, but is otherwise solvent.

86. Ibid, see Sections 27-32, NDIC Act.

(b) Imposition of Holding Actions which basically instructs the bank to take or not to take certain actions relating to its operations – usually adopted to avert further dissipation of assets and to increase capital base. In other words, the powers of the Board and Management of the bank are curtailed, and as such, a bank must operate under the general guidance of supervisory authorities.

(c) Changes in Management which entails removal from office of a director, manager or officer and the appointment of replacements. This occurs where specific individuals have been identified to be conducting the affairs of the bank in a manner detrimental to the interest of the bank.

(d) Takeover of control and management which entails the dissolution of Board or removal of the entire Managerial Team and the constitution of a new Board or Management[88].

(ii) Closed Bank Resolution

Where the financial condition of the bank is considered grave, especially where the bank had become insolvent, the resolution option could take a more serious dimension and cold involve the closure of the bank, even if another bank could emerge from the closed bank. These options include:

(a) **Outright Liquidation and Deposit Payout**

The adoption of this option would require the revocation of the licence of the bank by the Central Bank of Nigeria, consequent upon which the Corporation automatically assumes the role of Liquidator pursuant to the provisions of Section 40 of NDIC Act, 2006. The Corporation thereafter, assume control of the bank and prepares the Statement of Affairs which basically determines the total assets and liabilities of the institution as at the closing date.

87. Alheri, B. N. *Op. Cit;* p. 5.
88. Ibid, pp. 5 - 6.

Simultaneously, the Corporation files a petition for Winding-up of the closed bank with a view to obtaining a winding-up order. The Corporation also gives notice to depositors and other creditors, requesting them to file their claims.

As a deposit insurer, the insured deposits of a failed bank are paid by the Corporation from its Deposit Insurance Fund (DIF). As a liquidator, the NDIC proceeds with the realization of the assets of the failed bank, payment of uninsured depositors and other creditors in accordance with the order of priorities established by law. The process is concluded by the termination of liquidation, the dissolution of the bank and discharge of the corporation as a liquidator[89].

It is important to note that liquidation as described above is usually adopted as a last resort and not usually the preferred option because of its effect on cessation of banking service, the traumatic effect on the depositors and ultimately the disruption to the payment system. If it is not well managed, it could destroy depositor's confidence in the banking system.

It is because of the above that the following alternative resolution options are usually considered[90];

(b) **Purchase and Assumption (P &A)**

Purchase and Assumption as a resolution option, ultimately entails the revocation of a distressed bank's licence. However, rather than proceeding to outright liquidation and deposit payoff, a healthy bank is approached, usually through competitive process to bid for the assumption of the liabilities and the purchase of all or some of the assets of the failed bank.

89. See generally, Sections 20 – 26 of the NDIC Act, 2010 on payment of insured deposits and liquidation dividends.
90. Alheri, B. N. Op. Cit; pp. 6 – 7.

Upon the consummation of the transaction, all the depositors of the failed bank would be transferred to the healthy bank where they would continue with banking relationship. The acquiring bank usually acquires the branches of the failed bank together with other assets. This approach would facilitate the continuation of banking business in the same building or as close by as possible. The residual assets and liabilities left over at the failed bank are thereafter, liquidated by the corporation and the failed bank is eventually dissolved as a legal entity. A well consummated P&A would typically result in the closure of a failing bank after banking hours on Friday and the resumption of banking business by Monday in a different name.

The main challenge with the P&A approach is the usual variance between the liabilities to be assumed and the viable assets available for purchase by the acquiring bank. Typically, a deposit insurer can only guarantee the transfer of the insured deposits to the P&A partner, since it cannot fund the entire deposit liabilities.

It is significant to note that the corporation consummated P&A transactions involving eleven (11) banks closed in January, 2006 pursuant to the bank consolidation programme. However, it was a peculiar P&A framework in the sense that the Central Bank of Nigeria had gratuitously guaranteed all Private Sector deposits in the thirteen (13) banks that remain closed pursuant to the consolidation programme. Consequently, in structuring the P&A transaction, the corporation as liquidator transferred not only the insured deposits but also all private sector deposits to the acquiring banks. The acquiring banks selected the assets of the failed banks in which they were interested, at agreed prices, often referred to as 'cherry picking'. The shortfall between the assets acquired and the deposit liabilities assumed by the healthy banks were then funded by the Central Bank of Nigeria through the issue of promissory notes which the banks could discount for cash. However, like typical P&A arrangements, the un-assumed liabilities and leftover

assets remained with the estate of the failed banks and being liquidated by the corporation in its capacity as liquidator and the proceeds used to pay public sector depositors and the subrogation rights of the Central Banks of Nigeria and NDIC.

It is significant to note that contrary to the wrong assumption in some quarters which included a segment of the judiciary, the healthy banks involved in the P&A arrangement did not acquire the failed banks as going concerns and could not therefore be described as successors-in-title to the liabilities of the respective closed banks. Rather, the corporation as liquidator, in the course of realization of assets of failed banks in liquidation, by contract, transferred responsibility for payment of only private sector deposits and insured public sector deposits. They did not step into the shoes of the failed banks and therefore, the joining of the healthy banks as parties in the suits against the closed banks are uncalled for. In fact, the closed banks were not parties to the P&A agreement. In other words there is no privity of contract between the failed banks and the healthy banks[91].

(c) The Bridge Bank Resolution

A bridge bank is a temporary bank organized by the regulators (CBN and NDIC) to administer the deposits and liabilities of a failed bank. Under this arrangement, the NDIC is authorized to operate a failed bank for a period until a bridge can be found for its operations.

The bridge bank option is a veritable tool of enhancing depositor protection and promoting confidence by ensuring ceaseless continuity of banking operation.

Clearly, when in the opinion of CBN, an NDIC – insured bank is in financial trouble, the CBN and NDIC may establish a bridge bank to;

(a) Assume the deposits of the closed bank;

91. Ibid, pp. 6 – 7.

(b) Assume such other liabilities of the closed bank as the Deposit Insurance Corporation may determine to be appropriate;
(c) Purchase such assets of the closed bank as the Deposit Insurance Corporation may determine to be appropriate; and
(d) Performing other temporary function which the Deposit Insurance Corporation may prescribe in accordance with the Act.

Bridge bank must be chartered as national banks. To the extent possible, bridge banks are required to honour the commitment of the failed bank to its customers, and not to interrupt or terminate adequately secured loans. Bridge banks are authorize to seek to liquidate failed banks either by finding buyers for the bank as a going concern, or by liquidating it portfolio of assets within two years, which can be extended by an additional year should the bridge bank failed to wind down its operations within the allotted time, the bridge bank must notify the Governor of the CBN of its intent to dissolve the bridge bank. Under this situation, the NDIC is appointed as the receiver of the bridge bank's assets.

In the Nigeria case, the CBN in August 5, 2011, revoked the operating licences of three banks including; Afribank, Spring Bank and Bank PHB, which according to it, did not, show enough capacity and ability for recapitalization. In their place, the CBN through the NDIC established bridge banks and transferred the assets and liabilities of the three affected banks to the bridge banks as follows;

(i) Mainstreet Bank Limited (Afribank),
(ii) Keystone Bank Limited (Bank PHB), and
(iii) Enterprise Bank Limited (Spring Bank)

Under the new management, Mainstreet Bank Limited took over the assets and liabilities of Afribank, Keystone Bank Limited assumed the assets and liabilities of Bank PHB while Enterprise Bank Limited took over that of Spring Bank.

Consequently, the Asset Management Company of Nigeria (AMCON) immediately acquired from the NDIC, the three Bridge Banks. Accordingly, AMCON injected N679 billion into the Bridge Banks to meet the minimum capital base of N25 billion and the minimum capital adequacy ratio of 15 percent.

Mainstreet Bank, which assumed the assets of Afribank received N285 billion, Keystone Bank which assumed the assets of Bank PHB received N283 billion and Enterprise Bank which assumed the assets of Spring Bank, received N111 billion.

The acquisition and transfer of ownership of the Banks were effected through a subscription agreement with each of the three banks. By the subscription agreement, AMCON became the owners of the three banks and provided sufficient capital to restore the banks to the level of capital adequacy stipulated for their operations[92].

3.12.4 **Liquidation Process**

Since the establishment of the NDIC in 1989, the Corporation had been actively engaged in the liquidation process of failed banks in accordance with its statutory mandate. There are currently 45 banks in liquidation exclusive 3 closed banks that are contesting their closure in court. The basic processes are as follows;

(i) **Revocation of Banking Licence**

The first step in the liquidation process is the revocation of the banking licence of the insured financial institution by the Central Bank of Nigeria (CBN). The Banks and Other Financial Institution Act, 1991 as amended empowers the CBN to vary or revoke any condition subject to which a licence was granted. The CBN may also impose fresh or additional conditions to the grant of the bank licence of an insured financial institution[93].

92. Ibid, pp. 8-10.
93. S. 5(1), Banks and Other Financial Institutions Act, Cap. B3, LFN, 2004.

The fact of revocation of the banking licence of any insured institution by the CBN would then be published in the National gazette in accordance with the law.

Whenever the licence of an insured institution is revoked by the Central Bank of Nigeria, the NDIC automatically assumes the function of liquidator to such failed insured institution with powers conferred on a liquidator under the Companies and Allied Matters Act, 1990[94] and the NDIC Act, 2010.

(ii) **Appointment of the NDIC as Provisional Liquidator**

Section 10(1) of the NDIC Act, 2006 empowers the Corporation to act as the liquidator of a failed financial institution whose banking licence is revoked by the CBN. The corporation is statutorily deemed to have been automatically appointed by the Federal High Court as a provincial liquidator[95.]

Accordingly, as a liquidator of a failed insured institution, the NDIC is required to cause a notice to be given by advertisement in National Newspapers or other news media requiring all depositors with the insured institution under liquidation to forward their claims to the NDIC[96.]

Under the NDIC Act, 2006, the NDIC as liquidator is vested with power to;

(a) Realize the assets of the failed insured institution [97]

(b) Enforce the individual liability of the shareholders and directors thereof[98].

(c) Wind-up the affairs of such failed institution as herein otherwise provided[99].

94. See S. 40(1) of the NDIC Act, 2010;See S. 225(1) of the Companies and Allied Matters Act, Cap. C20, LFN, 2004 for the Powers of Liquidators.
95. Note: S. 40(5) of the NDIC Act, 2010 provides that the provisions of the Companies Winding-Up Rules, 1990 and any amendment thereto shall not apply to the Winding Up of Failed Insured Institution by the Corporation as Liquidator. Accordingly, times spent on applying to the Federal High Court to be appointed as a Provisional Liquidator in the first instance as required under the Winding Up Rules, 1990 is saved by the Corporation.
96. S. 41(1), NDIC Act, 2010.
97. S. 41(2) (a), NDIC Act, 2010.
98. S. 41(2) (b), NDIC Act, 2010.
99. S. 41(2) (c), NDIC Act, 2010.

(d) Pay dividends on proved claims at anytime after the expiration of the period of advertisement[100].

It is significant to note that the powers of the NDIC as liquidator in the NDIC Act, 2010 are in addition to the powers of a liquidator as provided under section 425 of the Companies and Allied Matters Act.

(iii) **Application for Winding-up at Federal High Court**

Immediately following the publication in the National gazette of the revocation of the licence of a failed insured institution, the NDIC is required under law to apply to the Federal High Court for an order to wind-up the affairs of the failed insured institution[101]. The Federal High Court was vested with exclusive jurisdiction to entertain matters connected with or pertaining to banking, banks, Other Financial Institutions, including any action between one bank and another, any action by or against the Central Bank of Nigeria arising from banking, foreign exchange coinage, legal tender, bills of exchange, letters of credit, promissory notes and other fiscal measures under section 251(1)(d) of the Constitution of the Federal Republic of Nigeria, 1999 (as amended). Accordingly, winding-up matters are within the exclusive jurisdiction of the Federal High Court.

Once the Federal High Court grants for petition of the NDIC and issues an order for the winding-up of the failed insured financial institution, the said provisional nature of the corporation's status as liquidator is removed[102].

100.S. 41(3) (b), NDIC Act, 2010.
101.S. 40(2), NDIC Act, 2010.
102.Alheri, B. N. Op. Cit; pp.11 -12.

(iv) The Dual Role of NDIC as Insurer and Liquidator

It is significant to note that where NDIC becomes a liquidator of a closed bank, it actually assumes a dual role with respect to the failed bank in liquidation, namely, the role of a deposit insurer and that of a liquidator. As deposit insurer, section 20(1) of the Act authorizes the Corporation to pay up to N500,000.00 to depositors in an insured deposit money bank or N200,000.00 in other deposit-taking insured institutions. In making the payments, the corporation may exercise its discretion to require proof of claim from all depositors with the failed insured bank. The payment of insured claims comes from the DIF contributed by insured institutions and not from the estate of the closed bank. In its role as liquidator, the duties of the NDIC are to;

(i) Settle claims of uninsured depositors and creditors;

(ii) Realize the assets of the failed institution and enforce individual liability of shareholders and debtors;

(iii) Satisfy liabilities of the institution;

(iv) Make dividend payments; and

(v) Wind-up the affairs of the institution.

By the provision of section 22(3), payment of an insured deposit to any person by the corporation whether by cash or by transferred deposit in a new bank or another insured bank, discharges the corporation[103].

(v) Realization of Assets and Collection of Debts

Essential to the NDIC's role as liquidator, is its ability to realize the assets of the bank as required under section 41(2)(a) of the NDIC Act.

103. Ibid, p. 12

In aid to this function; the NDIC may utilize any of the powers of a liquidator under section 425 CAMA including the power to sell the property of a company of a bank before their closure, failed banks typically possess assets which were acquired for use during their period of operation. Upon their closure and NDIC stepping in as the liquidator, NDIC is expected to convert the assets of the failed banks into cash. Other actions taken by the NDIC upon taking possession of the bank include the preparation of the statement of affairs of the bank and taking of inventory of assets and property as at the effective date of the bank's closure. This usually includes known assets and property as at the effective date of the bank's closure, including all known assets of the closed bank, contingent assets as well as those in litigation. Assets are appraised to determine their fair market value which is usually the basis for the disposal price.

In aid of the actual disposal of assets, it must be noted that the vesting of the failed bank's assets in the NDIC is provided for under section 424 CAMA. Therefore, upon the application of the NDIC, the court may direct that all or any part of the property of the bank in liquidation, by whatsoever description, or held by trustees on its behalf, shall vest in the NDIC, and the NDIC may bring or defend in its name any action or legal proceeding which relates to the property of the bank so vested for the purpose of recovering same and winding up the bank. The NDIC may thus dispose of the property vested in it under this section or exercise its power under section 425 of CAMA, 2004 to sell property of the bank to gain funds for satisfaction of the bank's debts. This disposal of bank assets is usually made through public tender. To facilitate speedy liquidation process, the NDIC Act, 2006 suspended the application of the Companies Winding-up Rules and indeed certain provisions of the Companies and Allied Matters Act[104].

104. Ibid, pp. 12 – 13.

3.13 **Governance Structure of the NDIC**

The governing body of the Corporation shall be a Board of Directors which include the Chairman, Managing Director, two none executive Directors, a representative of the Central Bank of Nigeria not below the rank of a Director and the Federal Ministry of Finance not below the rank of a Director and six other members one from each of the six geo-political zones of the country[105]. The Chairman and Board members shall not be persons who own or control significant interests in any insured institution in Nigeria[106].

That provision takes care of any conflict of interest which could hinder effective corporate governance of the Corporation especially the operational independence of the Corporation.

The President appoints the Chairman and members of the Board subject to the confirmation of the Senate[107]. The Chairman and members of the Board shall be part-time members[108].

The part-time members of the Board shall be experienced persons with relevant background thus, capable of improving the potentials for high quality decisions by the Board.

Furthermore, section 6 (2) of the enabling Act bans any Director or employee of any insured institution to be appointed to the Board whilst in office. Section 5 (6) also states that all part-time members must be experienced persons with relevant background[109].

105. Op. Cit; S. 5(1) & (2), NDIC Act.
106. Ibid, S. 5(3), NDIC Act.
107. Ibid, S. 5(4), NDIC Act.
108. Ibid, S. 5(5), NDIC Act.
109. Ibid, S. 5(6), NDIC Act.

A person shall cease to hold office as a member of the Board if he becomes bankrupt, convicted of a felony or any offence involving dishonesty or fraud, becomes of unsound mind, or incapable of carrying out his duties, guilty of a serious misconduct in relation to his duties, guilty of professional misconduct, such that the member is barred from practice of his profession, resigns his appointment by a letter addressed to the President through the Minister of finance or he is found to have failed to disclose to the Board his interest or the significant interest of any member of his family or close associate known to him in any insured institution at the time of his appointment[110].

In order to ensure that Board members do not suffer any personal liability for actions, omission or decision taken in good faith while discharging the mandate of DIS, and therefore compromise their independence, the enabling law provides a protection through section 55. This section makes provision for indemnifying the Directors in respect of anything done or omitted to be done in good faith while executing the powers conferred on the Corporation[111].

Apart from ensuring a competent governing body through appointment of fit and proper person, where the Board is dissolved the Minister of Finance in consultation with CBN is empowered to constitute a management committee which shall comprise the Chairman, Managing Director, Executive Director and representative of the CBN and the Ministry of Finance to perform the function of the Board until a new Board is constituted[112]. The practice can help to sustain oversight of management and preserve institutional memory.

110. Ibid, S. 6(1), NDIC Act.
111. Ibid, S. 55, NDIC Act.
112. Ibid, Section 6(3), NDIC Act.

3.13.1 **Management of the Corporation**

From inception till date, the day-to-day management of the Corporation has been the responsibility of the Managing Director who doubles as the Chief Executive Officer of the Corporation. He is assisted by two Executive Directors. The two Executive Directors perform such duties as may be assigned to them from time to time by the Board and/or the Managing Director. The three executives are the members of the Executive Committee of the Board.

Apart from being responsible for day-to-day management of the Corporation, the committee is also responsible for the implementation of the policy decisions of the Board as well as collaborating and networking with other agencies and organisations within and outside the country on a wide range of issues that could enhance the performance of the Corporation.

In its twenty years of existence, the Corporation had been structured into three divisions: the Managing Director's Office, Operations Division and Corporate Services Division (formerly Finance and Administration). Over the years, these divisions had remained same even though, the number of departments and independent units had changed. Departments and independent unit were created to take care of the expanding roles and responsibilities of the Corporation and also in response to Strategic Plans of the Board. The latest of these plans resulted in the present structure of thirteen (13) departments and four (4) independent unit. Departments are headed by staff of the rank of a Director whilst independent units could be headed by other ranks of executive staff. To ensure proper coordination of the activities of the different departments and independent units, a Management consultative committee comprising all heads of departments/ independent units is put in place to share information and harmonize strategies.

The committee chaired by the Managing Director/Chief Executive Officer, meets every month[113].

3.14 Powers and Authorities of the Corporation

Given the onerous responsibilities that the Corporation is expected to undertake, it is only logical that powers and authorities be bestowed on it in order to effectively discharge its responsibilities. The powers and responsibilities as contained in the enabling Act are as follows;

(i) Authority to Source and Manage Funds of the Corporation

By section 10 of its enabling Act, the fund of the Corporation consist of the following;

(a) Assessed premiums paid by insured institutions.

(b) Income from the investments of the Corporation.

(c) Monies borrowed from any source with the approval of the Board, and

(d) Monies from any other source as may be approved by the Corporation[114].

In addition to the levying of annual premium on deposit taking institutions, the Corporation has the authority to demand for special contribution from insured institutions where the fund of the Corporation is inadequate to give assistance to fail institution.

Such special contribution may not be more than 200% of the annual premium paid by a member institution[115].

113. Ogunleye, G. A.*Op. Cit*; p. 24.
114. Op. Cit; S. 17(5). NDIC Act, 2010.
115. Ibid, S. 10, NDIC Act.

The Corporation is further empowered to invest the premiums and any other fund available to the corporation (that are not immediately required) in Federal Government Securities or other securities as may be determined by the Board of the Corporation.

In addition section 52 gives power to the corporation to borrow from the CBN[116]. Finally, the Corporation is allowed to establish a separate deposit insurance fund for each category of insured institutions into which all assessed and collected premium will be paid[117].

(ii) **Authority to Vary Maximum Deposit Insurance Claim**

By section 20(1) of the enabling Act, the maximum claim by the depositors of a failed bank is N200,000 whilst that of other institutions is pegged at N100,000[118]. Notwithstanding this provision, the Corporation's board is given the authority to only vary upward this maximum claim from time to time[119].

(iii) **Powers to Access Information from, and Examine the Books and Affairs of Member Institution.**

The Corporation has direct access to member institutions' information. It receives direct (hard and soft copies) periodic reports for regular off-site monitoring. It has the authority to request additional information from insured institutions on matters affecting the interest of the depositors and the health of such institutions

116. Ibid, S. 17(5) , NDIC Act.
117. Ibid, S. 17(4) , NDIC Act.
118. Ibid, S. 52, NDIC Act.
119. Ibid, S. 17(4), NDIC Act

The Corporation is also empowered to carry out on-site examination of the books and affairs of insured institutions on regular basis. It also has the authority to conduct special and target examination of insured institutions[120].

(iv) **Power of the Corporation in Failing or Failed Institutions**

The Corporation is empowered to give financial assistance to a failing institution if such an institution requests and meets the conditions specified by the Corporation[121]. For a failed institution whose licence has been withdrawn by the CBN, the Corporation has authority to undertake statutory liquidation. Under the latter condition, the Corporation has the power to realize the assets of the failed insured institution; enforce the individual liability of the shareholders and directors and wind up the affairs of such failed institution[122].

(v) **Enforcement Actions Against Member Institutions**

Given the role and responsibilities of the Corporation as a risk minimizer, it has the authority to take enforcement actions against member institutions in the discharge of its mandates.

For instance, insured institutions and persons representing them could be subject to appropriate sanctions and penalties for violations of or non-compliance with the provisions of the enabling law.

3.14.1 Powers of the Board

The Board of Directors has broad authority which include;

(a) to superintend over the affairs of the Corporation,

120. *Ibid*, S. 20 (1), NDIC Act
121. *Ibid*, Section 20(2), NDIC Act.
122. *Ibid*, section 27(1), (2), (3)& (4), NDIC Act

(b) formulate policy for the administration of the Corporation,

(c) to act in the name of the Corporation,

(d) to acquire offices and other premises for the use of the Corporation,

(e) to make, alter, and revoke rules and regulations for carrying on the business of the Corporation,

(f) to appoint officers who in the opinion of the Board are required for carrying the functions of the Corporation including the examination of insured institutions,

(g) to fix terms and conditions of service including remuneration of employees of the Corporation,

(h) to advise the Central Bank of Nigeria on the need to close a failed insured institution if in the opinion of the Board it continued operation will jeopardize the interest of the depositors,

(i) to serve notice on a failed insured institution of his intention to remove the institution from its record of insured institutions,

(j) to assume with the prior concurrence of the Central Bank of Nigeria, the management of a failing insured institution,

(k) with the concurrence of the Central Bank of Nigeria serve a notice of removal from office on any officer or director who has violated any of the laws, rules or regulations of the corporation or has engaged in an unsound practice that may lead to dissipation of assets or financial loss to his insured institution,

(l) to perform the functions of a liquidator or receiver for all failed insured institutions,

(m) to extend from time to time the period within which a depositor is required under this Act to file his claim for the payment of insured deposit in a failed insured institution,

(n) to prosecute any officer or director of an insured institution who has violated any of the provision of this Act, and to do such other things and enter into such other transactions, which in the opinion of the Boards are reasonably

incidental, supplementary or conducive to the exercise of the powers and performance of the Corporation's functions.

Finally, the Board by the provision of section 56 is empowered to make regulations, rules or orders to give full effect to the provisions of the enabling law – such powers include power to make provisions for such incident and supplementary matters as the Board may consider expedient as well as power to make different provisions for different circumstances guiding the operations of the DIS in Nigeria. It can also alter or revoke such rules and regulations[123].

3.15 **Legal Framework of the NDIC in Nigeria**

A comprehensive and adequate legal framework is crucial for the effective implementation and administration of a DIS in Nigeria.

Depending on the mandate given to the deposit insurer, the statute establishing the DIS should unambiguously specify the powers and authority of the deposit insurer, such as source of funding, the participating deposit-taking financial institutions and the conditions for their participation, etcetera.

The enabling legal framework for the establishment of a DIS in Nigeria was the NDIC Decree No. 22 of 15th June, 1988 now repealed and re-enacted as the Nigeria Deposit Insurance Corporation (NDIC) Act, No. 16, 2006 and the Nigeria Deposit Insurance Act, Cap. N102, 2010.

The NDIC No. 22, 1988 which established the Corporation, was implemented for eighteen (18) years. In those years, it was observed that the legal frame work governing the operations of the NDIC had some inherent inadequacies.

123. Ibid, S. 37 (1) & (2), NDIC Act.

In 1997 and 1998, the legal framework was amended in an effort to clearly define the responsibilities of the Corporation over failing and failed banks. In 1997, the Act was amended (through NDIC (amendment) Decree No. 5 of 1997) to empower the Corporation to take proactive measures where a bank was significantly or critically undercapitalized. The 1998 amendment had only one objective, which was to repeal Sections 23A-D of the NDIC (amendment) Act No. 5 of 1997 which provided for delineation of the respective roles of the CBN and NDIC on distress management and also prescribed clear thresholds as well as the appropriate supervisory action for various levels of distress.

The NDIC Act, 2010 addressed some of the challenges encountered by the Corporation in the discharge of its mandate under the NDIC Decree No. 22 of 15th June, 1988 Act and the NDIC Act, No. 16 of 2006. Although, it may not be possible for law makers to make a perfect law that would address every conceivable development that will occur in the future, the 2010 NDIC Act, had to a great extent removed the challenges the Corporation faced in the course of implementing the repealed 1988 NDIC Decree[124].

The legal framework for the implementation of DIS in Nigeria and its contribution to the development of the Nigeria legal system are as follows;

3.15.1 **Importance of Adequate Framework for NDIC**

A legal framework is the enabling law or legislative provision that enables the establishment of a corporate body, group, commission or organization. In a corporate setting, the legal framework prescribes the structure, grants the relevant powers, assigns roles and responsibilities and regulates business activities, amongst other.

124. Ogunleye, G. A. *Op. Cit;* pp. 27 - 28.

Any deposit insurance system requires the adoption of a legal framework to pilot its affairs and handle emerging issues relating to all the stakeholders particularly, depositors and deposit-taking financial institutions.

For an explicit deposit insurance system, there should be rules governing coverage limit, the types of instruments covered, the methods of calculating depositors' claims, funding arrangement and other related matters. Legal framework will no doubt, help clarify the authorities' obligations to depositors as well as limit the scope of discretionary decisions that may result in arbitrary actions. Also, there is need for a legal framework to support early intervention and prompt corrective action, the ability to close failed banks promptly and provisions for the clear and orderly liquidation of assets.

Generally, for an effective implementation of a DIS, an appropriate legal framework that addresses some pertinent emerging issues and challenges of a DIS should be in place. Such framework should state the objectives of the scheme and other operational guidelines relating to such issues as ownership; administrative structure, participation in the system (mandatory or voluntary); funding of the Scheme; types of claims/liabilities covered; extent of coverage, supervisory responsibilities, failure resolution options compatible with stated objectives, and enforcement powers. For example, formally specifying the mandate of a deposit insurer by law clarifies the role of deposit insurance within the financial safety-net. Clarity of the mandate contributes to sound governance as well as greater accountability[125].

125. Ibid, p. 28

3.15.2 An Overview of the NDIC Decree No. 22 of 1988 and Rationale for its Repeal

The repealed NDIC Decree No. 22 of June, 1988 which established the Corporation at inception, provided the mandate for the operating policies and procedures of the NDIC. The core functions of the Corporation under the 1988 Decree could be broadly classified into deposit guarantee, bank supervision, distress resolution and bank liquidation.

In implementing the provisions of the repealed Decree No. 22 of 1988, there were a number of constraints and challenges faced by the Corporation due to the inadequacies of some provisions of the repealed Decree. Some of the issues which necessitated the repeal of the 1988 Decree were as follows;

(i) Poor drafting style;

(ii) Transfer of responsibility for bank supervision from the Federal Ministry of Finance to CBN not reflected in the Decree;

(iii) Rigid provisions that hindered responsiveness to the needs of stakeholders. For example, premium payable by banks and insurance coverage could not be varied without amending the law;

(iv) The appointment of NDIC as liquidator of failed insured institutions was not automatic, but was subjected to the Companies & Allied Matter Act tortuous court processes;

(v) Failure to recognize deposit insurance as an exclusive mandate of a deposit insurer;

(vi) Inadequacy of enforcement powers;

(vii) Absence of protection for Directors and Employees of NDIC against adverse claims for actions or decisions taken in the official capacity;

(viii) Lack of provision to ensure payment of insured deposits in litigious situations.

Most of the provisions of the repealed Decree No. 22 of 1988 were very rigid and gave no room for timely and appropriate responsiveness to stakeholders' needs. Consequently, the major thrust of its amendments was to make room for flexibility such that the Corporation's Board of Directors would have the discretion to make policy decision that would enable the Corporation to respond promptly to the dynamics of the financial services industry. For example, the increase in the deposit insurance coverage from N50,000 to N100,000 proposed in 2001 and later to N200,000 in 2004 would have long been effected if the Corporation's Board had the power to vary deposit insurance coverage from time to time in response to development in the financial services industry and the economy.

Apart from the rigidity of provisions in the repealed Decree, some observed inadequacies made its amendment imperative. Such inadequacies included explicit power to serve as liquidator, power to present winding up petition to the Federal High Court, power to p\incorporate bridge bank(s) as vehicle(s) for distress resolution, and the indemnity for the Corporation's officers and directors in respect of action taken in good faith.

As a result of the above deficiencies and other gaps in the 1988 Decree, the Corporation had over the years doggedly pursued the amendment of the principal Decree with vigor and the National Assembly passed the re-enacted NDIC Bill which was signed into law by the President on 22nd December, 2006. The drafting errors in the old Decree were rectified to facilitate effective understanding and implementation. The 2010 NDIC Act contains 60 sections grouped into 12 parts[126].

126. Ibid, p. 29.

3.15.3 **Highlight of the 2010 NDIC Act and Implications**

For many years, the corporation was able to make giant strides in the area of banking supervision and distress resolution, but it faced a lot of challenges in those years before the repeal of the 1988 Decree. Some of the major provisions introduced into the 2010 Act and their implications for the operations of the Corporation are highlighted below;

(i) **Harmonization with the Banks and Other Financial Institutions Act (BOFIA), 1991 as amended**

Although, the Corporation remains an autonomous agency under the supervisory purview of Federal Ministry of Finance (FMF), its operations, particularly with regard to banking issues were harmonized with the BOFIA. The 1988 Decree was enacted when the CBN was under the supervision of the FMF, hence the Corporation's supervisory duties relating to banks was subject to Hon. Minister of Finance (HMF) oversight.

However, following the enactment of the BOFIA in 1991 which conferred autonomy on CBN on banking matters, some of the powers of the HMF in the 1988 Decree become ineffectual.

The new Act has therefore, regularized the anomaly by subsisting references to the FMF with references to the CBN in areas of banking supervision. The implication of that development was that the Corporation would be able to collaborate effectively with the CBN on issues relating to banking supervision.

(ii) **Sole Mandate as Deposit Insurer**

The new Act has recognized the Corporation as the sole deposit insurer in Nigeria, hence it provided that no person other than the Corporation shall insure deposit liabilities or guarantee payment to depositors of insured institutions in Nigeria. This

provision had clearly barred insurance companies from deposit insurance. Hitherto, it had been observed that some insurance companies had attempted to insure bank deposits by placing adverts in the media soliciting for depositors to insure their deposits with them.

(iii) **Premium Rate (section 17)**

Although, the subsisting rate of premium payable was retained, the Corporation had been empowered to vary the rate or introduce new basis of premium assessment. Consequently, unlike under the old law where the rate was static and the Corporation had no power to vary it, the Corporation can now reduce the premium or change the basis of assessment whenever it is considered desirable to do so. The Corporation exercised its power in that regard and introduced the differential premium assessment system in year 2007.

Furthermore, the Corporation had been empowered to establish separate Insurance Funds for each category of insured institutions. This new provision had enable the Corporation to set up a separate Deposit Insurance Fund for Primary Mortgage Institutions and Micro-Finance Banks, while maintaining a separate fund for the universal banks in order to reflect the different orientation and focus on the two (2) categories of insured institutions. Similarly, different premium rates could now be prescribed for PMIs/Micro-finance Banks and universal banks.

(iv) **Maximum Insurance Claim (Section 20)**

The new Act increased the maximum insurance claim payable to depositors from N50,000.00 to N200,000.00 for universal banks, while a minimum claim of N100,000.00 was prescribed for depositors of Primary Mortgage Institutions and Micro-finance banks. Furthermore, unlike in the old Decree which did not empower the Corporation to vary the maximum claim, no matter how desirable, the new Act has empowered the Corporation to increase the maximum claim whenever

considered appropriate. It is significant to note that only an upward review was allowed by the new Act.

The Act also stated clearly that the insured claim was without prejudice to the additional payments which would be made to depositors by way of liquidation dividend as assets of the closed banks were being realized by the Corporation. The new amendment should put to rest the wrong notion that it was only the insured claim that a depositor could receive in respect of its deposit in a failed.

(v) **Power to Freeze Deposit Account (Section 22)**

The new Act empowered the Corporation to freeze a deposit account in a failed bank where it was suspected that such account was connected with any criminal activity until after final determination by a Court or Tribunal. That provision was part of the anti-money laundering measures being implemented by Government.

(vi) **Termination of Insured Status (Section 23 – 26)**

Although, there were provisions on termination of insured status of banks in the old Act, they were ambiguous. In the new Act, elaborate provisions on the power of the Corporation to de-insure a member institution were made. The Act also stated quite clearly the implications of the termination of insured status which could be a ground for the revocation of the licence of a bank.

(vii) **Prompt Corrective Action (Section 32)**

The new Act had made specific provisions in section 32 empowering the Corporation to take prompt corrective actions deemed necessary to address incidences of unsafe and unsound practice or violation of law or regulations by an insured institution.

(viii) **Power to Manage and restructure Failing Bank(Section 28 – 39)**

The Act had streamlined the provisions on the take-over of Management of failing banks and had made provisions which would enable the Corporation to restructure such distressed banks, especially through Mergers/Acquisitions as well as purchase and Assumption transactions. Furthermore, the new Act had empowered the Corporation to establish a Bridge Bank in consultation with CBN (Section 39).

(ix) **Power to Act as Liquidator (Section 40)**

The new Act had made it very clear that upon the revocation of the licence of a bank by the CBN, the Corporation shall act as provisional liquidator, pending the making of a winding-up order by the Federal High Court. With that development, there would no longer be any need for the Corporation to apply to a Federal High Court for appointment as a Provisional Liquidator of a bank whose licence has been revoked, which indeed had frustrated the efforts of the Corporate in the payment of insured deposits promptly.

Furthermore, some provisions were made to address the hindrance which the Companies winding-up rules had caused for the liquidation of banks. It is also significant to note that the new Act had reduced opportunities for litigants to obtain frivolous injunctions against the Corporation, while performing its role as liquidator, particularly with regard to the payment of insured claims. Thus, whenever a litigant challenging the Corporation as liquidator files for injunction, the trial court is required to refer such motion to the Court of Appeal for determination. The Court of Appeal is required to take a decision on the issue within a time frame of 60 days.

(x) **Right to Appear in Court (Section 47)**

In-house lawyers of the Corporation had been empowered to represent the Corporation in litigations involving insured banks. The provision is very important,

because many debt recovery cases which external solicitors are reluctant to take due to the difficulties associated with debt recovery as well as the nature of the cases, could be handled by in-house lawyers. Debt recovery is based on no recovery, no commission.

(xi) **Higher Responsibilities on External Auditors (Section 54)**

The new Act had placed higher responsibilities on external auditors of banks with regard to their auditing assignment, while a higher penalty was also provided for non-compliance.

(xii) **Indemnity for Directors and Employees (Section 55)**

In line with what obtains in most statutes establishing public institutions and consistent with best practice in deposit insurance, the new Act had provided protection to Directors and employees against personal liability for actions taken in good faith in the ordinary course of business.

Furthermore, in order to prevent suits filed in Court against the Corporation in respect of liquidated banks without notice, the Act requires any party intending to file a suit against the Corporation to first give one (1) month notice of the intention to file an action in Court. Such pre-action notice would enable the Corporation to resolve the issues where feasible and avoid unnecessary litigation.

(xiii) **Increase in Quantum of Penalties**

The penalties prescribed by the old Act for contravention of the Act by insured institutions were enhanced in the new Act. The enhancement was intended to encourage compliance.

(xiv) **Other Legislations that Impacted on the Corporation**

Aside from the Corporation's enabling Act and the Fiscal Responsibility Act, there were some other legislations in Nigeria that also guided the operations of the Corporation since its establishment. Some of the legislations included the Central Bank of Nigeria (CBN) Act of 1991 (as amended); the Banks and Other Financial Institutions Act (BOFIA) of 1991 (as amended); the Companies and Allied Matters Act (CAMA) of 1990 (as amended); and the Failed Banks Act of 1994.

The CBN Act provides for the establishment of the apex banking regulatory authority. The CBN directly regulates the activities of licenced banks and other financial institutions. The Bank and Other Financial Institution Act (BOFIA) 1991 conferred on the central Bank of Nigeria the power to regulate banks and other financial institutions operating in the country. The BOFIA provides the legal framework governing the licensing, operations, regulation and supervision of banks.

The Failed Banks (Recovery of Debt and Other Financial Malpractices) Act No. 18 of 1994, established the Failed Banks' Tribunal with powers to recover debts owed to failed banks, try offences specified in the BOFIA and the NDIC Act as well as other tribunal established pursuant to the Act had been transferred to the Federal High Court.

The Companies& Allied Matters Act (CAMA) 1990 regulates incorporation and operation of companies in Nigeria. The Act is relevant to the operations of the DIS to the extent that banks are required to register first as companies before applying for banking license. The CAMA provides the framework for the baking institutions to be incorporated and operated as Public Liability Companies (Plc).

Another legislation that impacted on the operations of the Corporation was the Fiscal Responsibility Act (FRA) which was enacted in 2007. The Act was aimed at redirecting government at all levels to imbibe fiscal behavior that would promote

prudence and sound financial management. Under Section 21 and the schedule of the FRA, the Nigeria Deposit Insurance Corporation (NDIC) was listed as one of the government agencies required under Section 22 to establish a general reserve fund to which one fifth of their operating surplus would be allocated at the end of each financial year while the balance of the operating surplus (i.e. 80%) would be paid to the consolidated Revenue Fund of the Federal Government. Under Section 23, the surpluses of the Corporation were classified as a Federal treasury Revenue while the deficits were classified as the Corporations' losses for the fiscal year.

The Fiscal Responsibility Act has serious implications for the Corporation. For instance, deposit insurance system is a component of the financial safety-net which most governments all over the world establish to promote financial system stability. The macro-economic stability which the Acts seeks to promote cannot be realized without financial system stability. The establishment of NDIC relieved the Federal Government of the contingent liability of having to bail our distressed banks. Therefore, the Corporation's operating surpluses should be utilized to build up the Deposit Insurance Fund.

Deposit Insurance is a financial guarantee (i.e. upfront promise to pay guaranteed sum) to depositors in the event of bank failure. It is a legal obligation imposed under the deposit insurance contract. No institution listed under Section 21 of the FRA except the Corporation was under such a legal obligation. That no doubt, illustrates the peculiar position of the Corporation. While the treatment of deficit as a loss for the fiscal year under Section 23 may not have devastating effect on agencies funded by the Federal Budget, any deficit incurred by the Corporation will no doubt, erode its general reserve fund since it is self-financing and does not receive budgetary allocation from the Federal Government. For the Corporation, the general reserve fund is the first line of defence against any deficit (or loss) sustained.

The inclusion of the Corporation under Section 21 would also severely impair its ability to build up its general reserve fund and thus the deposit insurance fund. The significant reduction in general reserves would impair the Corporation's ability to generate investment income to meet its operational expenses. Such impairment could affect the credibility of the deposit insurance system in Nigeria.

Inadequate funding can lead to delays in resolving failed institutions and loss of credibility by the deposit insurer. The Corporation had increased deposit insurance coverage from N50,000.00 to N200,000.00 through its new Act. That signified a huge increase of its liability to bank depositors. Also, the Corporation had indirectly reduced the premium rate through the adoption of the Differential Premium Assessment System (DPAS). Hence, the removal of 80% of NDIC's surplus through the application of the Fiscal Responsibility Act would compound NDIC's predicament of balancing increased liability (i.e. increased insurance coverage) against reduced income (through premium rate reduction).

Above all, it is best practice in a DIS to plough reserves to the premium fund. Such plough-back allows the DIF to be built up to meet contingencies, particularly in our case where government had maintained a policy of not using public funds to bail our banks[127].

3.16 **Deposit Insurance Funding and Fund Management**

Adequate funding is crucial to the effective implementation of a DIS regardless of the type of mandate. DIS must have access to adequate sources of funding to meet its obligations when they fall due, for it to be effective. Funding for a DIS influences, to a large extent: the credibility of the scheme and the confidence it elicits from its participants and the banking public at large; its stabilizing capacity; the way the cost of providing insurance is finally allocated among depository

127. *Ibid*, pp. 28-38.

institutions, users of financial services and taxpayers; and the balance or risks among the financial institutions themselves as well as the insurer's exposure vis-à-vis different insured depository institutions.

A well-designed deposit insurance system should have in place mechanisms necessary to ensure that adequate funds are available to reimburse depositors promptly in the event of an insured institution's failure and to cover the operating expenses of the system. As the experiences of several countries have shown, inadequate funding could lead to delay in resolving failed institutions as well as significant increase in costs, with attendant consequences on the credibility and confidence in the system. The design of a deposit insurance system's funding could affect when and by whom the costs of deposit insurance would be borne.

In Nigeria, the explicit deposit insurance system being administered by the NDIC**,** necessitated the adoption of an ex ante funding arrangement for the Corporation, to enable it discharge its mandates as well as sustain its operations effectively. This chapter discusses the funding arrangement, including the growth in the Deposit Insurance Funds as well as deposit insurance pricing in Nigeria and how the Fund had been managed in the last twenty years[128].

3.16.1 **Sources of Fund for DIS**

The sources of fund for a deposit insurance system, especially the Deposit Insurance Fund (DIF), which is used for depositor reimbursements, resolution costs and running expenses of the insurance agency could come from the private sector, the public sector or both.

128. Ibid, p. 67.

(i) **Private Sources**

Participating institutions are the main source of funding under this arrangement. Institutions usually pay mandatory annual premium as one of the conditions for membership of a DIS**.**

Premium amounts are typically determined relative to either the insured deposit base or the total deposit base. Policymakers in countries which use insured deposits as a basis for determining premium are of the view that institutions with a higher percentage of insured deposits tend to enjoy more protection than those that have low percentage of insured deposits.

On the other hand, using total deposit has the advantage of ease of assessment and can prevent speculative switches by banks between insured and uninsured deposits and can help the deposit insurer to build its DIF more rapidly. It may also be necessary, sometimes, to introduce special premiums or levies on the participating institutions, when the DIF is not sufficient to resolve some failures.

(ii) **Public Sources**

In addition to premiums collected from participating institutions, most deposit insurance systems have arrangements to access public sector funds if the need arises. These could take the form of initial contributions when the system is established, government or central bank loans to cover special circumstances and grants to cover losses. In most countries where the DIS is publically-owned, government provides initial capital to establish the system. Since the promotion of financial system stability and the efficiency of a financial safety net are important government policy objectives which benefit the country as a whole, it can be argued that it is appropriated for the public sector to give the system some financial support by providing initial capital to establish a fund and/or provide supplementary funding in crisis situations. In some jurisdictions, the central bank or government directly grants the deposit insurer line of credit.

Generally, it is less expensive for the insurer to obtain funds from the public sector than from the private sector, since the public sector can usually raise funds at lower cost, given its credit rating. Also, during crisis, it may be difficult to raise funds directly through the private sector.

(iii) **Access to Contingent Financing**

A deposit insurer by itself may not be able to contend with a large-scale financial crisis as no DIS is designed to resolve systemic crisis. Even in a non-systemic crisis, the DIS may find itself with inadequate funds in reserve to meet its commitments. The funding gap can be covered by giving the insurer access to contingent or back-up financing either from the government or the market. The backup funding would allow the prompt reimbursement of insured deposits and could be required through special contribution by the surviving institutions. If a contingent funding mechanism is in place, it is important to have clearly defined rules on its use so that public funds will not be excessively relied on or otherwise used inappropriately.

There are a number of potential sources from which to obtain contingency funding. These include the private sector (loans or bonds, with or without government guarantee), the government treasury and the central banks. International organizations such as the International Monetary Fund (IMF) and the World Bank may be helpful in some cases, particularly where government is unable to mobilize financial resources quickly enough, because of legal or other constraints.

In rare cases, the deposit insurer could consider private sources such as obtaining one or several lines of credit from insured banks. The issuance of bonds or debentures if needed may be other possibilities. Although the deposit insurer is typically a government agency, a government guarantee may nevertheless lower the cost of borrowing from the private sector since it can enhance the credit rating of

the financial instrument used. In some cases, the lack of government guarantee may even block access to private sector credit[129].

3.16.2 **Other Funding Sources for the DIS in Nigeria**

The Nigerian DIS was established as an explicit deposit insurance system, with specific funding arrangements clearly spelt-out in its enabling Act. Section 10 (1) of the NDIC Act, 2010 identified four sources of funds for the DIS in Nigeria. The sources are: capital contributions and periodic recapitalization provided by government through the shareholders (CBN and the Federal Ministry of Finance); premium contribution by participating institutions; borrowing from the CBN; and special contribution by the participating institutions.

On initial capitalization, at inception in 1989, the authorized capital was fixed at N100 million, out of which N50 million was paid-up. It remained so until 1992 when the authorized capital was reviewed to N1 billion, with N500 million paid-up.

The situation lasted up to 1996 when both the authorized capital and the amount paid-up were raised to N2.3 billion and N1 billion respectively. In the subsequent years, both the authorized and paid-up capital remained constant at N23 billion and N2.1 billion respectively.

The NDIC Act, 2010 put the authorized capital of the Corporation at N5 billion with the paid-up capital rising to N2.3 billion. That was done to adequately cater for the rising capital expenditure requirements of the Corporation.

The premium contribution by insured institutions is derived through the application of an assessment rate.

129. *Ibid*, pp. 46-48.

From inception in 1989 up till 2007, the Corporation charged a flat rate of 15/16 of 1% per annum (which is about 0.94 per cent or 94 basis points) against the total deposits (less exemptions) of a deposit money bank for its premium as provided in section 16 of the NDIC Act, 2010. Under that provision, it also charged other deposit-taking financial institutions a flat rate of 18/16 of 1% per annum (which is 0.5 per cent or 50 basis point) of the total deposit liabilities of the institutions as at 31st December of the preceding year. With effect from January 2008, the Corporation implemented a Differential Premium Assessment System **(**DPAS**)** on the deposit money banks.

The Corporation was empowered to borrow from the Central Bank of Nigeria in times of need, as clearly specified in the NDIC Act, where the DIF was not sufficient to settle depositors' claims as a result of multiple bank failures or the failure of a systemic bank, post consolidation. Although the NDIC once applied for support from the CBN in anticipation of the multiple liquidation of 1998, it never had cause to use that source of funding.

With regard to Special Contribution by the participating institutions as a source of funding of the DIS, the Corporation also never had cause to explore that opportunity. Section 17 (5) of the NDIC Act, 2010 states as follows:

> *"where the funds of the Corporation are not sufficient for giving assistance to insured institutions within the meaning of section 2(1)(b) of this Act or otherwise insufficient for implementation of the objects of the Corporation, every participating insured institution or category of insured institution may be obliged, without prejudice to subsection (1) and (2) of this section, to pay as Special Contribution out of its profit before tax, a sum equal to its annual premium or such other sum as the Board may require not exceeding 200% of its annual premium on such terms and conditions as the Board may from time to time determine"*

.

3.16.3 **Trends in the Growth of Deposit Insurance Fund (DIF) in Nigeria**

The size of the fund vis-à-vis the risk exposure of an insurance agency determines the extent to which a deposit insurer could exercise its obligations in crisis situations.

It is therefore imperative for the deposit insurer to not only ensure that the DIF grows over time but that it is adequate to sustain its operations. Basic approaches to building a DIF include a steady premium assessed over an extended period as well as a premium system designed to achieve and maintain a target reserve ratio or range.

In Nigeria, the DIF is obtained through assessed premium paid by insured banks and other financial institutions. The task of generating a DIF for the deposit insurance system in the country started with the first premium assessment carried out in 1989 when a total of 82 insured banks were assessed for premium on their deposit liabilities for 1988 and 1989. Table 4.1 shows at a glance the trend in the growth of DIF in the last twenty years. As evidence in Table 4.1, a total of N382.5 million was realized as premium contribution, when the scheme started in 1989.

Since then the DIF has continued to grow as more banks were established in the country and as banks deposit grew. However, it is pertinent to note that there were instances where the DIF experienced decline, which was as a result of deposit reimbursement arising from the failure of a sizeable number of banks in 1998, for example.

The DIF, as shown in Table 4.1 grew from N382.5 million in 1989 to N10.2 billion in 1997. It declined to N8.3 billion in 1998 as a result of the failure of 26 banks, whose insured depositors had to be settled by the NDIC. From that period, the DIF rose steadily from N12.3 billion in 1999 to N57.5 billion in 2004. Another decrease in the size of DIF was witnessed in 2005, which was as a result of the provision

made in respect of a possible reimbursement of the claims of the depositors of Peak Merchant Bank and Savannah Bank, whose cases were in court as well as the 14 banks that could not meet the CBN recapitalization requirement and whose licenses were to be revoked (NDIC, 2005). By 2008, the DIF had grown to N175.6 billion, despite the introduction of the Differential Premium Assessment System **(**DPAS**),** which caused a reduction in the amount of premium paid by the banks, owing to the reduction of the premium rate. Table 4.1 also reveals the ratio of DIF to total deposits of insured banks in the system. The ratio rose from 0.12 percent in 1989 to 3.27 percent in 1997. It then fell to 2.14 percent and 2.45 percent in 1998 and 2002 respectively. This could be explained by the depletion of the DIF as a result of the multiple liquidation of 1998 and other ones undertaken between 2000 and 2002. The ratio also rose to 3.17 percent in2004 and then declined to 2.02 percent in 2008 owing to the liquidation of the banks closed under the Purchase and Assumption transaction adopted since 2010[130].

130.*Ibid*, pp. 56 – 57.

Table 3.8.3

Trend in the growth of deposit insurance fund in Nigeria

YEAR	DEPOSIT INSURANCE FUND (DIF) (N Million)	TOTAL DEPOSIT OF INSURED BANK (N Million)	RATIO OF DIF TO TOTAL DEPOSITS (%)*
1988	39.5	33,949.2	0.12
1989	382,5	30,802.9	1.24
1990	706.7	43,856.9	1.61
1991	1,205.5	59,477.1	2.03
1992	1,890.9	87,737.1	2.16
1993	2,829.5	144,971.6	1.95
1994	4,229.5	177,373.8	2.38
1995	5,909.1	210,945.6	2.80
1996	7,811.01	258,968.1	3.02
1997	10,265.4	314.185.5	3.27
1998	8,384.8	392,478.24	2.14
1999	12,338.01	569,798.52	2.17
2000	19,416.3	838,592.56	2.32
2001	26,337.4	1,017,195.72	2.59
2002	30,049.6	1,226,624.12	2.45
2003	42,773.4	1,415,785.86	3.02
2004	57,595.1	1,814,745.44	3.17
2005	54,726.6	2,469,069.71	2.22
2006	90,179.09	3,412,273.3	2.64
2007	124,423.4	5,337,174.33	2.33
2008	175,629.6	8,702,996.20	2.02

3.16.4 Deposit Insurance Pricing

(i) Deposit Insurance Assessments

The most common method for a deposit insurer to raise funds, whether ex ante or ex post, is through premiums levied on member institutions. The mechanism for the assessment and collection of premiums should be clearly defined. The premium rate is determined taking into account the funding needs of the insurer and the ability of the members to fund the system. Policymakers must determine the assessment base as well as the premium assessment rate and method.

(ii) Premium Assessment Base

Premium assessment base is the foundation used to determine the contributions made by member institutions to the fund. The extent of the assessment base is determined by taking into account the maximum exposure of the deposit insurance system. The most common assessment bases are insured and total deposits. However, some systems could have a broader base and include domestic liabilities or all liabilities and obligations or take into account considerations such as non-performing loans. In a survey covering 87 countries practicing deposit insurance conducted by LADI in 2008, the statistics revealed that 43 countries including Brazil, Canada, Taiwan, Korea, Japan, used Philippines, Nigeria, Kenya and Argentina, used total deposit and the remaining 15 countries used other indices such as risk weighted assets (e.g. Norway and Poland), credit portfolio (e.g. Lebanon) et cetera, as bases for premium assessment. From the survey, it was obvious that insured deposit was the most widely used base for premium assessment. It is often argued that the use of insured deposit as assessment base does not fetch more premiums to the Deposit Insurance Fund (DIF) and could be more complex to administer. However, charging premiums on insured deposits would seem more equitable, as the premium payable is equated to the perceived level of protection offered by the deposit insurance system (NDIC, 1999).

Total deposits adjusted for some exemptions are mostly popular amongst newly established systems that need to build their DIF as rapidly as possible. It was argued that the use of total deposits for premium assessment fetches more money to the DIF that the insured deposits (NDIC, 1999). It is also easier to administer than assessing premium using insured deposit. However, it appears less equitable, when compared with insured deposit as basis for assessment.

In Nigeria, section 16 of the NDIC Act, 2010 clearly specifies the assessment base to be total deposits less exemptions such as:

a) Insider deposits, that is, deposits of staff including directors of the licensed bank or financial institution;
b) Counter-claims from one person who maintains both a deposit and loan accounts, the former serving as a collateral for the loan; or
c) Such other deposits as may be specified from time to time by the Board".

At inception, the choice of total deposit as assessment base by the NDIC was informed by the need to rapidly build the DIF considering distressed situation of seven banks. Also, total deposit liabilities was chosen as assessment base because of its ease of administration as against the complexities associated with the use of insured deposits.

(iii) Premium Assessment Rate and Approach

The Premium assessment approach could be either flat rate or differential (risk-adjusted).

(a) Flat Rate Premium Approach

Under flat-rate premium approach, all member institutions are assessed at the same rate given the assessment base. This approach is relatively easy to implement. It provides the opportunity for the deposit insurer to rapidly build the deposit insurance fund. That is the reason many newly established or transitional systems

prefer this method of assessment (Hoelscher, et al, 2006). The major shortcomings, however, are that it is inequitable since more prudently managed low-risk institutions subsidize higher-risk institutions and the exposure to moral hazard is higher than under risk-adjusted system.

The Corporation started and continued with the application of a flat rate to all the participating institutions up till 2007. The application of the flat rate for premium charged was found to be administratively convenient and easy to understand even by the insured institutions. It was also found to have assisted the Corporation in the rapid build-up of its DIF. However, the use of the flat rate approach for premium assessment had been criticized by some participating institutions. Those that perceived themselves as less risky saw no reason why they should be made to pay the same proportion as those that were adjudged to be more risky. There was also the argument that the rate charged by the NDIC was one of the highest in the world and that it was higher than the net profit of some banks (NDIC, 1997). Even when the objectives for adopting the flat-rate premium assessment system appeared to have been achieved, the Corporation could not alter the rate without amending the enabling Decree No. 22 of 1988. Hence, the Corporation only adopted a differential system when a new enabling Act was enacted in 2010.

(b) **Differential Premium Approach**

Under the risk- adjusted or differential premium system, the risk posed by a member institution to the deposit insurer is incorporated into the premium structure. This attenuates the moral hazard issue by providing member institutions with an incentive for better risk management. Differential premium assessment is more equitable, since cross-subsidization among institutions is reduced. In a risk-related system of insurance premium, banks pay premium based on their relative risk of failure, that is, banks that engage in riskier behavior would be subject to higher premiums. If the risk of the failure were price properly, the benefits of increased

risk-taking would be taxed away, limiting banks' incentives to engage in overly risky acidities. This should in turn lead banks to limit their risk exposure and therefore act as a mitigant to the erosion of market discipline resulting from the introduction of deposit insurance (Hoelscher, et al, 2010). An important advantage of risk-adjusted systems is that it can lead to pressure by the member institution's board of directors on management to address risk-related issues when premiums are raised. A drawback of differential premium systems is that they are more complex to develop and administer. Also, for a country transitioning from a flat rate system to a differential premium systems the amount of premium collection could reduce, which has implications for the deposit insurance fund. In terms of the applicability of the risk-adjusted premium system, there has been increase in the number of countries using it. As at 2003, there were a total of 25 countries using risk-adjusted premium assessment system (Demirguc-Kunt, et al, 2005, Hoelscher, et al, 2006, IADI, 2008).

There are wide variations in the practice of risk-adjusted premium system. Most countries use a variant of the CAMELS rating system to sort banks into different risk groups, often with emphasis on capital adequacy (e.g. Canada, Colombia, French and Hong Kong. Other countries (e.g. Finland, Hungary, Portugal and Sweden, use solvency or capital adequacy ratios to categorize banks into different risk groups. It should be noted that although risk-adjusted premiums may be attractive in principle, they are administratively demanding and are unlikely to work well unless supported by complementary policies such as prompt bank intervention and effective supervision and regulation.

(c) Development and Application of Differential Premium Assessment System (DPAS)

The NDIC Act, 2010 gave the board of the Corporation the powers to alter the pricing method, and that facilitated the adoption of the Differential Premium

Assessment system (DPAS) effective January 2008. The need to adopt the DPAS became more compelling partly because of the emergence of bigger banks sequel to the bank consolidation policy of the Federal Government, which made sound risk management a critical factor in ensuring the safety and soundness of the banking system. Other reasons for the adoption of the DPAS include the on-going initiative to adopt a risk-based supervisory framework as well as the emphasis placed on sound risk management by the Basle II Capital Accord (NDIC, 2008).

The adoption of DPAS by the Corporation had the multiple objectives of ensuring fairness in deposit insurance pricing and a reduction in the overall premium burden on banks as well as promotion of sound risk management in the participating institutions without jeopardizing the Deposit Insurance Fund (NDIC, 2007).

In designing the DPAS, the experiences of the NDIC in implementing DIS for close to two decades and the lessons learnt from the experiences of other jurisdictions, particularly Turkey and Canada were used. The Nigeria DPAS, which considered both quantitative and qualitative factors, had two primary stages:

i) The determination of a base premium Rate(Ro) for all the banks; and
ii) The determination of add-ons based on individual bank's risk profile using both quantitative and qualitative factors.

It is pertinent to note that in determining the Ro, several scenarios were used, while taking into account the sustainability of the DIS. The sustainability of the system was measured by the operating surplus/deficit (and this was dependent on the available investible funds) at various levels of the feasible Ro. Given several assumptions and projections, 50 basis points emerged as the base rate that would ensure the sustainability of the system and which must be paid by all the participating institutions. The add-ons were calculated on individual bank's risk profile up to a maximum of 30 basis points. Table 4.2 contains these add-ons were

put together, a maximum of 80 basis point was arrived at, which the riskiest bank in the system would pay as premium. Also, when this was compared with the 94 basis points paid under the flat-rate system, it showed a significant reduction, which was one of the objectives for adopting the DPAS. It was noteworthy that the implementation of DPAS in 2008 reduced premium burden of the banking industry by about 35 percent[131].

3.16.5 **Management of Deposit Insurance Fund in Nigeria**

When a deposit insurance system is funded on an ex-ante basis, there is the need to consider policies associated with the management of the DIF. In this regard, it is imperative to consider the trade-off between liquidity and return. The fund must have adequate level of liquid assets on hand to enable it readily compensate insured depositor should an institution fail. Depending on the mandate of the insurer, funds may also be required to support other forms of failure resolution such as provision of Open Bank Assistance to troubled banks. Funds would also be required to day-to-day operations and to attract quality staff and acquire the operational resources necessary for the functioning of the deposit insurer.

In many systems, funds are held in Low-risk, highly liquid assets, typically short-term government securities. In other systems, policy makers may pursue an investment strategy that places more emphasis on achieving higher rates of return. Both of these strategies have their advantages and disadvantages.

If a conservative approach is adopted, the opportunity cost is the foregone return to the deposit insurance fund.

131. *Ibid*, pp. 59 – 65.

The pursuit of a higher-return policy may result in funds not being available for meeting insurance obligations when they are needed and/or the loss of principal, if securities become unrealizable. This could induce erosion of public confidence in the deposit insurance system. A preferred approach would be an investment strategy that balances higher rates of return against the certainty that funds will be available when needed and guards against loss of principal.

Other considerations include whether a deposit insurer should invest in its own members. The advantage of this approach is that it effectively places the funds withdrawn from the banking system by the deposit insurer back into the system. However, a drawback is that the insurer runs the risk of investing in members, which could subsequently fail, with the result that the invested fund would be lost. To some extent, the risk could be mitigated by only placing funds with low-risk members. Another problem with this approach is that it can place the insurer in a dilemma should an institution in which it has placed the funds begin to experience difficulties. Withdrawing its funds from such institution could worsen the institution's liquidity situation, but not to do so would be unfair to the other members and inconsistent with the rationale for the fund. At a minimum, the insurer should refrain from placing funds with high risk or troubled institutions. It is also advisable to invest funds in financial assets denominated in the currency in which potential claims are most likely to occur.

(i) Separate Deposit Insurance Funds

Many DIS, which rely on exante funding, maintain only one deposit insurance fund for all their member institutions. However, certain factors or circumstance had necessitated the establishment of separate DIF for different types of member institutions. For instance, in situations where there are major differences in the risk profiles of different types of institutions, there can be benefits to having separate different funds and help segregate institutions with significantly different risk

profiles and reduce the scope of cross subsidies between the categories of institutions. While common costs can be shared, sector specific costs can be isolated and premiums can vary among sectors.

Nevertheless, the separate fund approach does have some disadvantages. Having more than one fund can result in risk being overly concentrated (particularly if there is small number of institutions in each fund). Thus, the advantages and disadvantages of separate funds must be weighed carefully when deciding to establish how best to proceed. If separate funds approach is adopted it is important to ensure that the distinctions among the institutions and their funds are real and do not contribute to competitive distortions.

In Nigeria, following the extension of deposit insurance coverage to Microfinance Banks (MFBs) and Primary Mortgage Institutions (PMIs) in 2008, a separate fund called Special Insured Institutions. Insurance Fund (SIIF) was created for such deposit insurance window. The decision to separate the funds was informed by the deposit profile as well as the risk profile of the special insured institutions, the premium rate charged and their coverage level. The separation of the fund entailed the maintenance of separate accounts for both the deposit money banks and the special insured institutions. In the event of failure, only money meant for a category of insured institutions would be used to resolve the failure.

Section 10(2) of the NDIC Act 2010 states as follows:

> *"The Corporation shall have power to establish a separate Deposit Insurance Fund (DIF) for each category of insured institution in which all assessed premium paid shall be deposited and which fund the Corporation shall utilize for the respective insured institutions".*

At the take-off stage of SIIF in 2007, some seed money had to be provided for the SIIF from the operating surplus of the Corporation pending the time the SIIF was

able to grow, as a contingency arrangement against the possible failure of any of the institutions. This became necessary considering the large number of licensed MFBs and PMIs, deposit profiles and their mode of operation, which posed significant risk to the meager premium they were likely to generate in the short-run.

(ii) DIF Investment Policy in Nigeria

Where the funding arrangement is ex ante, policy makers need to consider which investment policy would effectively utilize the funds available for deposit insurance purposes. Such policy should emphasize safety, liquidity and minimum distortions whenever such investments have to be realised to meet obligations under the scheme.

The availability of instruments for meeting these criteria depends on the depth of the financial system. However, the preferred option had mostly been in government securities. Regardless of the investment approach selected, policy makers should ensure that the funds are protected from fraud and defalcation.

The DIF investment policy in Nigeria was guided by the provisions of the NDIC Act, 2010. Section 13(1) states as follows:

> *The Corporation shall have powers to invest money not immediately required in Federal Government Securities or in such other securities as the Board may from time to time determine".*

The broad objective of the policy was to make a positive return (after adjusting for inflation) without compromising safety and liquidity of funds.

The specific objectives of the investment policy were to:

(a) Provide liquidity for its deposit insurance responsibilities and to meet normal operating needs. The provision fo an adequate liquidity profile will be informed by potential, anticipated or contingent insurance payouts and

conditions operating in the financial markets. To this end, all investments held by the Corporation should be readily realizable or convertible to cash;

(b) Preserve capital and maximum investment returns by adopting a conservative investment policy. This requires that all investments be of very high quality, in terms of the ability of the investee to meet its obligations to the Corporation and the arrangements which are in place to protect the Corporation as investor.

(c) Minimize overall risk by portfolio diversification;

(d) Ensure expeditious investment of all residual fund without threatening the safety and liquidity objectives. In that regard, the investment policy aims at ensuring that no residual fund meant for investment remains idle for more than 24 hours; and

(e) Periodically measure its investment performance against acceptable benchmarks.

To achieve the above objectives, the Corporation's investment policy provided for the establishment of levels of responsibility and reporting requirements. That was done to ensure senior management oversight and proper implementation of investment management and control processes. The structure comprised Senior Management Investment Advisory Committee and Finance Department. Each of these levels was expected to play roles that would ensure prudent management of the DIF, while taking into account safety and liquidity of the funds.

Also, guidelines in terms of portfolio composition, target rates and investment limits were provided for in the investment policy. The investment portfolio of the Corporation consisted of three segments, namely; short-term, medium-term and long-term investments in eligible debt instruments. The short-term investment instruments included, but not limited to;

(a) Treasury bills;

(b) Treasury Certificates;
(c) CBN Debt Instruments specially issued for liquidity management;
(d) Medium and long-term investments having a remaining maturity of one year or less sourced from the secondary market; and
(e) Such other short-term debt instruments that are in the same class with Federal Government securities.

The medium and long-term investment instruments included, but are not limited to the following:

(a) FGN Bonds and Notes of over 1 year to 10 years tenor;
(b) Specially issued Bonds by the Federal Government of over 1 year to 10 years tenor such as Pension Arrears Bond, Local Contractor Liability Bond;
(c) Investment indebtedness issued by the Federal Government; and
(d) Treasury Bonds and Notes issued by the Central Bank of Nigeria.

Investment Target rates were usually set and as much as possible the target rates set were realistic and determined by the available government securities, their rates and potential as well as contingent obligations of the Corporation as deposit insurer and the general economic outlook, among others.

Investment limits were set in order to achieve the target rates and in doing that tenor and the amount in each maturity cycle were taken into account to ensure that the Corporation did not suffer undue risks arising from inflation or inability to reinvest matured investments. Also, efforts were always made to ensure that the maturity profiles of investment were aligned with the DIF cash flow projections. Based on the above considerations, the maximum tenor for Bonds was set at 7 years. Other investment limits (which could either be from the primary or secondary segment of government securities market) for the Deposit Insurance fund were as follows:

(a) FGN Bonds and other eligible medium/long term securities: 60% maximum

(b) Nigeria Treasury Bills (NTBs) and other eligible short-term securities: 40% minimum.

The above limits were usually subjected to reviews from time to time to reflect changing economic and market conditions as well as developments in the financial condition of the insured institutions.

(iii) Management of General Reserve Funds

In addition to the above-mentioned sources of funds to the DIF, General Reserve Fund is yet another veritable source of funds to the deposit insurer. This is usually derived from the operating surplus of the deposit insurer at the end of a financial year. It forms part of the funds not only available for use but which can be re-invested by the deposit insurer.

Section 12(1) of the NDIC Act, 2010 provides for the establishment of a General Reserve Fund. The Act states as follows:

> *"The Corporation shall establish a General Reserve Fund to which shall be transferred the Corporation's net operating surplus before tax if the reserve fund is less than ten times the authorised capital".*

In compliance with the above provision of the Act, the NDIC established the General Reserve Fund from the inception of the scheme in 1989. Since then, the whole of the operating surplus at the end of each financial year had always been remitted to the reserve fund because it was less than ten times the authorised capital. However, following the enactment of the Fiscal Responsibility Act in 2007, the remittances of the operating surplus to the General Reserve Fund became impaired. This was because the Fiscal Responsibility Act provided that 80% of the operating surplus of certain government agencies including the NDIC at the end of each financial year should be remitted to the federation account regardless of the

requirements of their enabling laws. It also stated that the Fiscal Responsibility Act superseded any law that is in conflict with its provisions.

Furthermore, where the operating surplus of the Corporation at the end of the year turned out to be more than ten times the authorised capital, section 12(2) of the NDIC Act 2010 provides for how the surplus would be appropriated as follows:

> *"Where the reserve fund is more than ten times the authorised capital at the end of the year, 75 percent of the net operating surplus before tax shall be transferred to the reserve fund, 50 percent of the remaining amount after tax shall be applied to reduce the annual premium payable by the insured institutions while the remaining 50 percent shall be paid to the shareholders".*

The implications of the Fiscal Responsibility Act is that the reserve funds may not grow to attain the level specified in the NDIC Act where it could be appropriated to reduce premium payment by the insured institutions and for payment of dividend to the shareholders as provided for in the NDIC Act.

It is also noteworthy that in other jurisdictions such as Malaysia, Canada, United States of America, operating surpluses are added to the DIF so as to enable the DIF grow as quickly as possible[132].

132. Ibid, Pp. 59 – 65

CHAPTER FOUR
CHALLENGES AND PROSPECTS OF DEPOSIT INSURANCE IN NIGERIA

4.4 Introduction

In the discharge of its mandate, the NDIC had in the past two decades been able to take meaningful and significant steps in deposit insurance practice. It had also cooperated with other safety-net players to ensure that the nation's financial system was stable. In spite of the huge success made in the areas of depositor protection, banking supervision, failure resolution and bank liquidation, there were still several lingering issues and challenges that required furthers attention.

On the other hand, prospects for better performance of the NDIC remain very bright. Also, given the experience of the Corporation in the last twenty years, there were also several lessons to be learned. Such lessons would be used to improve upon the Corporation's efforts at discharging its mandate in the most efficient and effective manner.

The challenges of the Corporation ranges from legal challenges, challenges to funding, supervisory challenges, challenges of failure resolution, and challenges of managing stakeholders' expectation.

4.5 Challenges of the Nigeria Deposit Insurance Corporation[133]

The corporation had in the last 20 years faced numerous legal challenges in the course of performing its statutory functions. In an attempt to address some of the challenges, the corporation successfully pushed for the repeal of Decree No. 22 of 1988 and the passage of the NDIC Act, 2006, now NDIC 2010. While the 2010 Act addressed some of the legal challenges, there are still some lingering ones which include:

133. *Ibid*, pp. 42 – 43.

(a) **Criminal Prosecution**

Criminal prosecution of bank directors and officers suspected of committing banking malpractices had faced severe challenges. Following the abrogation of the Failed Banks Tribunals in 1999, consequent upon the advent of democratic dispensation, the jurisdiction of the Tribunals was transferred to the Federal High Court. Since then, the prosecution of criminal cases had declined and convictions became rare events. The proceedings at the Federal High Court are characterized by slow judicial proceedings, frequent adjournments over long period of time and unnecessary legal technicalities.

Every unfavourable ruling against the accused is subject to interlocutory appeal to the Appeal Court and the Supreme Court.

(b) **Execution of Judgment Against Assets of the Corporation for Liability of Banks in Liquidation.**

The corporation had been faced with attachment levied on its assets in execution of judgment obtained against banks in liquidation. That anomalous situation was the result of the corporation's role as liquidator of failed banks in Nigeria. The courts had regarded that role as making the Corporation the successor-in-title to the failed bank, which should not be the case. For example, in the case of **Jackson Devos Limited v. NDIC**[134], the Federal High Court delivered a judgement against the defendant for N800 million in favour of the plaintiff on account of relationship between the plaintiff and Merchant Bank of Africa in liquidation.

The only connection between the judgement debtor and the judgement creditor is that NDIC was the liquidator of the bank. The Trial Court ordered that the money be deposited in court.

134. Suit No. FHC/ID/CS/5/2006 (Unreported).

(c) Challenges to Funding[135]

Some of the funding and fund management challenges the corporation has faced in the last two decades of its existence include premium avoidance. There is the general belief that the premium being paid by the insured banks constitute burden on them. For this reason, some of the insured institutions have been involved in acts of avoiding premium payable.

This they do through under reporting of their deposits which are usually deliberately reduced at year ends. This remained a challenge to the NDIC as it reduced the premium collectable, which also hampered the growth of the Deposit Insurance Fund.

In an effort to address the problem, the corporation embarked on premium examination on an annual basis, through which some banks were made to pay extra premium over what they had paid based on the inaccurate information they had earlier made available to the corporation.

Notwithstanding the use of e-FASS, which improved the reliability and accuracy of the data supplied by the banks, data integrity for the purposes of premium assessment remained a challenge as some banks still window-dressed returns to the supervisory authorities.

(d) Challenges of Bank Supervision

Integrity of data is an essential ingredient of supervisory process. Often, data submitted by banks to the regulatory and supervisory authorities did not fully reflect the true financial condition of insured banks. The corporation observed that, returns were either inaccurate or incomplete or outright misrepresentation. That, in effect, was capable of rendering supervisory actions ineffective.

135. *Ibid*, pp. 66 – 67.

There were incidence of understatement of deposit liabilities as well as reporting of credit exposures as off-balance sheet engagements.

As part of the measure taken by the corporation to address some of the challenges posed by data integrity, the Corporation in collaboration with the CBN, has reviewed the banks' reporting formats several times as well as computerized the process of rendition of returns through the development of a bank analysis software, known as Bank Analysis System (BAS) in the first instance and later electronic Financial Analysis and Surveillance System (eFASS)[136].

(e) Challenges of Managing Stakeholders' Expectation

The concept and operation modalities of the DIS are still being confused with those of conventional insurance business for protection against fire, marine losses, motor accidents, et cetera which started as far back as early 1920s in Nigeria. In conventional insurance, for example, the premium charged is supposed to be commensurate with the perceived level of risk inherent in the insured person, property or organization. Also, participation is usually voluntary. The same are not true for a DIS.

Again, the risks associated with debt obligations arising from deposit mobilization by deposit-taking financial institutions are quite different from those associated with contingent nature of conventional insurance contracts.

The confusion had in the last twenty years resulted in some of the challenges which the corporation had faced, particularly in the area of coverage. The corporation is not a conventional insurance company but a deposit insurance agency with mandate to guarantee deposits of less financially sophisticated depositors, especially the small ones, against the loss of their funds when a deposit-taking financial institution fails.

136. *Ibid*, p. 92.

Another major challenge facing the corporation in managing its stakeholders' expectations was the low response to its deposit pay-out which had been largely due to ignorance on the part of depositors.

That was in spite of the various public enlightenment measures adopted by the corporation. Although, this challenge had always been there, it had subsequently become an issue of serious concern as it might give an impression that the corporation was not doing enough to reach out to the depositors that the DIS was established to protect.

One of the recurring challenges in managing stakeholders' expectations had been the need to ensure the transparency and accountability of management of banking institutions and the curtailment of risk appetite. Many operators engage in unethical practices, including rendition of unreliable prudential returns that fail to disclose the true condition of their respective institutions. Such acts had in the past delayed prompt supervisory intervention.

The determination of financial soundness had emerged as a challenge in recent times. For example, the corporation had in the last few years witnessed debates as to whether or not some distressed banks should have been closed. Many commentators including top government officials made pronouncements on the issue which gave conflicting signals to members of the public on the bases of decisions taken by regulatory/supervisory authorities.

The misunderstanding and the challenge had informed the decision of the regulators/supervisors to articulate a Contingency Planning Framework for Systemic Crisis.

The framework specified intervention thresholds for capital, liquidity, change of management and other parameters in order to make supervisory intervention more transparent than hitherto[137].

(f) Challenges of Inter Agency Corporation

As earlier noted, financial system stability in any nation requires close collaboration and goodwill among the various safety-net players. To ensure adequate collaboration and goodwill, there is need for effective mechanism for the coordination and communication among safety net participants.

Although, concerted efforts had been made over the years to promote inter-agency cooperation and collaboration between the corporation and other safety-net participants, there are some lingering challenges that required further attention.

The various challenges that had faced inter-agency cooperation in the financial system could be linked to the passive posture of the Financial Services Regulation Coordinating Committee (FSRCC) in recent times. The FSRCC as noted earlier was established basically to coordinate and harmonize set standards as well as the supervisory efforts given the existence of multiple regulators and supervisors in Nigeria. However, the FSRCC had over the years not been able to achieve those laudable objectives for which it was established. The irregular meetings of the FSRCC had made the coordinated supervision of financial institutions especially conglomerates very difficult given the Nigerian universal banking system. It had to a large extent, created arbitrage opportunities in the supervision of financial institutions as a result of differing regulatory and supervisory standards among the various agencies.

137. *Ibid*, pp. 181 – 183.

The inadequate cooperation and collaboration among various agencies in the system had also resulted in information gap among regulatory/supervisory agencies particularly in their relationship with the various financial institutions in the system.

From the foregoing, efforts should be made to revive the FSRCC and make it functional. Although, some level of cooperation had been achieved between the CBN and the Corporation, particularly through the standing committees on supervision both at the executive and technical levels, reviving the FSRCC would further go a long way in addressing some of the lingering challenges facing inter-agency cooperation in Nigeria's financial services industry. Reviving the FSRCC would go a long way to minimize arbitrage opportunities for financial institutions and promote information sharing amongst regulators /supervisors in the Nigerian financial system.

(g) Malpractice in the industry

Some of the problems facing the banking industry include fraud, forgeries and other malpractices. These problems permeate all levels of staff in most banks including board of directors, top management and the generality of staff. Apart from colluding with customers to defraud their banks, key officials of some banks grant loans and advances to themselves, their relatives, own companies and other staff without collaterals and in questionable circumstances. Such loans and advances have often gone bad and problematic in recovery[138].

138. Peter, N. U., *Op. Cit;* p. 193.

4.6 Future Prospects

The prospects for the effective discharge of the corporation's mandate are based on the following factors, among others.

(a) Improved Legal Framework

One of the issues that constrained the effectiveness of the practice of the DIS in Nigeria for many years within the past two decades was inadequate legal framework. The NDIC Act, 2006, which replaced the 1988 Decree, had introduced some provisions that had the potential to remove some of the challenges imposed by the inadequate legal framework. In particular, the flexibility in the determination of premium rate/approach as well as deposit insurance coverage would enhance the responsiveness of the corporation to stakeholders' needs. Also, the legal protection granted to directors and officers of the corporation by the Act for actions taken in good faith in the discharge of their duty would enhance employees' vigilance in carrying out their responsibilities, particularly in cases where mandate emphasises early detection, intervention and closure of troubled insured institutions. It would also boost employees' confidence and commitment to duty thereby enhancing the implementation of the corporation's mandate.

Furthermore, the new Act had made the procedure for appointment of the NDIC as liquidator upon revocation of operating licence of a failed insured institution by the CBN less cumbersome. In specific terms, the Act provides that upon revocation of operating licence of a failed insured institution by the CBN, the corporation shall act as the provisional liquidator and such appointment shall be deemed as having being made by the court. The opportunities for litigants to obtain frivolous injunctions against the corporation while performing its role particularly with regard to depositor reimbursement have been reduced as it is now the Court of Appeal that has jurisdiction on such matters with a decision to be taken within 60 days. The end result is that depositor reimbursement can be handled more promptly than hitherto.

(b) **Enhancement of the Supervisory Tool**

The introduction of the electronic Financial Analysis and Surveillance System (e-FASS) jointly developed by the NDIC and CBN would ease the compilation of data and make information usually required by the NDIC when closing a bank readily available. With such information, NDIC could undertake preparatory review of deposit liabilities held by problem insured institutions. In the event that a bank is closed, NDIC would have sufficient information to facilitate early compilation of deposit registers and other relevant reports so as to ensure prompt payment of depositors' claims.

(c) **Availability of Framework for Early Intervention**

Apart from the statutory criteria provided for in the enabling Acts, the Contingency Planning Framework for Banking Systemic Crisis introduced in 2002 and which is being revised, if properly implemented will facilitate prompt resolution of problem banks. The framework, which seeks to reduce the incidence of systemic distress, could also be found useful in promptly addressing isolated bank failures. This will assist in reducing failure resolution costs.

(d) **Bank Consolidation Programme**

The emergence of a few well capitalized banks with diffused ownership structure, had the potential of improving the corporate governance practices in banks with positive consequences for reducing the risk of failure and associated cost to the NDIC.

(e) **Enhanced Public Awareness**

Public Awareness is one of the key pillars to the success of any DIS. Effective public awareness efforts promote public confidence and therefore contribute to the actualization of DIS's public policy objectives.

In recent times, the corporation had embarked on efforts at enhancing its public awareness activities with a view to creating and maintaining an appropriate level of awareness among depositors and other stakeholders as well as enhancing their understanding of key features of deposit insurance. At different times, the corporation had mounted different public awareness and education programmes to diverse target audience. It had also embarked on mass public education through advertisements in the media and wide distribution of its publications such as pamphlets, reports, books and other publications on deposit insurance. In addition, it organizes annual depositors' awareness week as well as annual workshop to educate and update the knowledge of finance correspondents and editors of different media organisations.

These concerted efforts will help to reduce poor perception of the scheme as well as reduce the slow response by depositors of failed institutions in coming to collect their monies during pay-out exercise.

(f) **Improved International Networking**

In order to ensure a good grasp of the latest international trends in deposit insurance systems and promote cooperation and collaboration with deposit insurance institutions in other countries, the NDIC joined the International Association of Deposit Insurers (IAD) based in Basle, Switzerland as a founding member in May, 2002.

In addition, the corporation continues to host visits by personnel from foreign deposit insurance organisations and sends its own staff to economically advanced countries with DISs to learn from their experiences with a view to attaining international standards for the implementation of the DIS in Nigeria. With its membership of the IADI and other efforts at reinforcing cooperation and collaboration with other deposit insurance agencies in different counties, the NDIC

is well positioned to partake in the sharing and exchange of expertise/information on deposit insurance issues. This has the effect of enhancing the effectiveness of deposit insurance practice in Nigeria[139].

139. *Ibid*, pp. 199 – 202.

CHAPTER FIVE

SUMMARY AND CONCLUSION

5.1 Introduction

This chapter concludes the research work with a summary, findings and recommendations on how to effectively implement the DIS in Nigeria.

In conclusion, it is worth noting the following:

First, the importance of DIS, as one of the fundamental components of the financial safety-net, has been recognized in many jurisdictions across the globe and Nigeria is not an exception in this regard. The DIS serves to insulate the economies of nations against the devastating effects of systemic bank failure.

Secondly, as discussed in this work, the perennial problem of incessant bank failure in Nigeria and its devastating economic consequences have been reduced to the bearest minimum with the introduction of the DIS in Nigeria.

The NDIC, which is charged with the statutory mandate of the implementation of DIS in Nigeria, took drastic measures immediately after its establishment in order to inject sanity into the banking system.

Thirdly, in the over two decades of its existence, the NDIC had been faced with numerous legal challenges which have hampered its operation. Several statutory amendments have been carried out to address these challenges.

In spite of these efforts, there are still inherent lacunae in the present Act for which this work has proffer sound recommendations for its amendment in order to enable the NDIC achieve its statutory mandates.

5.2 **Summary**

This work discussed the concept, meaning, evolution of deposit-taking financial institutions in Nigeria as well as the historical development of the DIS. It also examined the devastating effects of incessant bank failure on the economic life of Nigerians prior to the establishment of the NDIC. It also shows how the NDIC can effectively discharge its statutory mandates of bank deposit guarantee or deposit insurance, bank supervision, bank failure resolution and liquidation under the present legal regime.

An appraisal of the current DIS regime in Nigeria, which was first introduced with the establishment of the NDIC by the NDIC Decree, 1988[140] has been provided. The study delved into the importance of the DIS in the settlement of problems of failed and failing deposit-taking financial institutions in Nigeria with a view to ensuring sound banking system and protecting depositors' confidence in the banking system.

The historical development of the DIS, the reasons for the establishment of the DIS in Nigeria, powers and authorities of the NDIC, legal framework as well as prospects of the NDIC were equally examined.

Issues surrounding implementation of the DIS in Nigeria have been discussed in the light of the lacunae in the present legal framework and the unending problem of bank failures in Nigeria. It was clearly stated that a successful implementation of the DIS will ultimately depend on adequate legal framework.

This work also shows how the NDIC deals with the problems of distress condition in the banking system through distress resolution options as well as issues and challenges surrounding the process.

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140. Supra.

5.3 **Findings**

The following are some of the findings that this work has unearth in the course of the research:

(i) Execution of Judgement Against the Assets of the Corporation for Liability of Banks Liquidation

The corporation had been faced with attachment levied on its assets in execution of judgment obtained against banks in liquidation. That anomalous situation was the result of the corporation's role as liquidator of failed banks in Nigeria. The courts had regarded that role as making the Corporation the successor-in-title to the failed bank, which should not be the case.

(ii) Inadequate Deposit Reimbursement/Claim in the Event of Failure of an Insured Deposit-taking Institution

The amount fixed as maximum deposit claim under section 20(1) of the Act to all the classes of depositors and regardless of the amount of deposit lost by a depositor in the event of failure of an insured deposit-taking financial institution is not reasonable. For example, by the provision of the section, if a man losses N200,000,000.00 in the event of failure of a licence bank, he is only entitled to a maximum reimbursement or claim of N200,000.00 from NDIC. Whereas, in the case of other deposit-taking financial institutions like microfinance banks the depositor is only entitle to a maximum deposit claim of N100,000.00. The provision of this section, to say the least, is not reasonable and can discourage savings which is capable of stifling the economy of investable funds.

(iii) Inadequate Penalty for Non-compliance with the Provisions of the Act

The penalty provided under section 45 of the Act for non-compliance with the provisions of the Act is less punitive.

5.4 **Recommendations**

In the light of the findings, the following recommendations are hereby made for effective implementation of the DIS in Nigeria.

(i) Amendment of the Act to Bar Courts from Executing Judgement Against the Assets of the Corporation.

The Act should be amended to bar courts from regarding the corporation as a successor-in-title of failed banks as a result of its statutory role as a liquidator of such banks. This practice often results in execution of judgement against the assets of the corporation and has greatly affected the effective and efficient operation of the DIS in Nigeria.

(ii) Full Deposit Reimbursement/Claim in the Event of Failure of Insured Deposit-taking Financial Institution

The fixed amounts of maximum deposit claim provided under section 20(1) of the Act to all the classes of depositors and regardless of the amount of deposit lost by a depositor in the event of failure of a licensed bank or other deposit-taking financial institution should be amended as it is not reasonable. Reimbursement of any deposit lost by a depositor in a failed licensed insured bank or other deposit-taking financial institutions should be made full as this will encourage savings and also boost the economy.

(iii) Adequate Penalty Regime for Non-compliance with the Provisions of the Act

The penalty provided under section 45 of the Act for non-compliance should be reviewed upward to carry the force of deterrence so as to discourage flagrant disregard to the Act.

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