A History of the Nigeria Deposit Insurance Corporation (NDIC) and its Role in the Banking Sector of Nigeria Since 1988

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Abstract

A 'Deposit Insurance Scheme' (DIS) is an arrangement whereby a designated agency (usually government- owned) guarantees deposits in the insured financial institutions. The guaranty is usually limited to discourage moral hazard, a situation whereby the financiers and depositors would care little about the safety of the deposits because such deposits are fully insured. Most deposit insurance agencies act as liquidators of failed insured institutions while some, in addition, act as supervisors of insured institutions as well. In Nigeria, the decision by the Ibrahim Badamasi Babangida (I.B.B.) led Federal Military Government to establish the Nigeria Deposit Insurance Corporation (NDIC) in 1988 was informed by a number of factors chief of which was, the country's past bitter experience of bank failures. It was Decree No. 22 of 1988, which established the corporation to ensure deposit liabilities of all licensed deposit-taking financial institutions in Nigeria. Thus, the corporation was introduced following the deregulation of the financial sector under the Structural Adjustment Programme (SAP) in 1986, to provide a further layer of protection for depositors and promote financial stability, by complementing the supervisory activities of the Central Bank of Nigeria (CBN) in ensuring a safe and sound banking system. The aim of this paper therefore, is to highlight factors responsible for establishment of the NDIC by the I.B.B led military administration in Nigeria, mode of operation of the corporation and effects of its establishment on the banking sector of the country in particular and the financial sector as a whole. It will be shown in the paper that the corporation has during nearly thirty years of its existence, successfully minimised fear of distress and failure of banks from the minds of Nigerians and relatively restored their confidence in the banking sector.

Introduction

A bank deposit insurance scheme is widely seen as a financial guarantee to depositors, particularly the small ones, in the event of a bank failure. It developed out of the need to protect depositors, especially the uninformed, from the risk of loss; and also to protect the banking system from instability occasioned by runs and loss of confidence.[1] It was in view of acquiring bank deposit insurance scheme that the Nigeria Deposit Insurance Corporation (NDIC) was established by the Ibrahim Badamasi Babangida led military regime in 1988 consequent upon some economic circumstances and other considerations. While the economic circumstances had to do with new economic policies of the government as a result introduction and implementation

[1]. J.U. Ebhodaghe, "Bank Deposit Insurance Scheme in Nigeria", in P.T. Umoh, (ed.), *Safe and Sound Banking Practices in Nigeria: Selected Essays,* Lagos, Page Publishers Services Ltd., 1997, p. 3.

of Structural Adjustment Programme (SAP), which was aimed at deregulating the economy in the direction of market-determined pricing; the other consideration had to do with the bitter experiences of prior bank failures as well as the lessons of other countries with bank deposit insurance schemes.[2]

As a regulatory agency in the banking sector, the NDIC is expected to assist monetary authorities in the formulation and implementation of banking policies so as to ensure safe and sound banking practice. Section 5 of the 1988 NDIC Decree replaced by the NDIC Act 16 of 2006, states the functions of the Corporation to include insuring the deposit liabilities of licensed banks and such other financial institution operating in Nigeria; giving assistance in the interest of depositors to financially distressed banks; etc.[3] Thus, the primary aim of establishing the NDIC is to maintain stability and public confidence in the banking sector by guaranteeing payments to depositors in the event of failure of insured institutions as well as promoting safe and sound banking practices through effective supervision. It is an autonomous regulatory body with powers to examine the books of insured banks and other deposit-taking financial institutions and to restrict the activities of banks found not to be in compliance with regulations. It can also arrange for other banks to assume the deposit liabilities of a failing bank or take over the management of a bank where such action becomes necessary to protect depositors' interest.[4] It is against this background that this paper seeks to discuss factors responsible for establishment of the NDIC by the I.B.B led military regime in Nigeria, mode of operation of the corporation as well its effects on the banking sector of Nigeria in particular and the financial sector of the country as a whole. But before doing so, the paper first all discusses background to military rule in Nigeria.

Establishment of the Nigeria Deposit Insurance Corporation (NDIC)

One of the problems facing financial sectors particularly the banking sector in both developed and developing countries is the phenomenon of bank distress. No matter the cause or origin, once a bank starts showing signs of distress, the confidence of the customers of such bank gradually become eroded. In Nigeria, the decision by the I.B.B led Federal Military Government to establish the NDIC in 1988 was informed by a number of factors chief of which was the country's past bitter experience of bank failures. Others included lessons of other countries' experiences with deposit insurance schemes, increased competition in the banking industry caused by multiplicity of banks as a result of deregulated interest rates, the need for effective supervision and prudential regulation as well as change in government bank support policy.[5] It was thus, in reaction to bank distresses of the late 1980s caused by the SAP, that the NDIC was established in 1988, as an explicit deposit insurance scheme under the Nigerian Deposit

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2. *Ibid*, p. 6.
3. E.C. Emenike, "Performance of the Nigeria Deposit Insurance Corporation (NDIC)", *African Research Review*, Vol. 8. No. 3, 2014, p. 103.

4. *Ibid*. Quite a number of this instances occurred in Nigeria where assets and liabilities of failed banks were ordered by the NDIC to be taken over by other banks or dissolve an incumbent and appoint new management team for a distress bank.
5. G. A. Ogunleye, "Deposit Insurance Scheme in Nigeria: Problems and Prospects", a Paper Presented at the First Annual Conference of International Association of Deposit Insurers, at Basel, Switzerland May, 2002, p. 2. The presenter was a former Managing Director and Chief Executive of the NDIC.

Insurance Corporation Decree No. 22 of 1988, which established the corporation and vested it with the responsibility of implementing the system in the country. It subsequently commenced operations in March, 1989.[6] The scheme was therefore, introduced to provide a further layer of protection to depositors and complement the CBN's supervisory activities in ensuring a safe and sound banking system.

Section 1 (1) of the NDIC Act provides for its establishment to maintain stability and public confidence in the banking sector by guaranteeing payments to depositors in the event of failure of insured institutions as well as promoting safe and sound banking practices through effective supervision. It is an autonomous regulatory body with powers to examine the books of insured banks and other deposit-taking financial institutions and to restrict the activities of banks found not to be in compliance with regulations. It can also arrange for other banks to assume the deposit liabilities of a failing bank or take over the management of a bank where such action becomes necessary to protect depositors' interest.[7]

The headquarters of the NDIC was formerly located at Lagos but later relocated to Abuja (The Federal Capital of Nigeria) situated at 447/448 Constitution Avenue, Central Business District. The Lagos office was later converted to Special Insured Institution Department (SIID) of the corporation, and it was responsible for 'risk base supervision' of the banks across the country.[8] At the moment, there are eight (8) zonal offices of the NDIC in Nigeria which are responsible for compliance and bank examinations of the deposit money banks and microfinance or primary mortgage banks. They are: Bauchi, Benin, Enugu, Ilorin, Kano, Port Harcourt, Sokoto and Yola Zonal offices.[9]

Mode of Operation of the NDIC

The NDIC operates under the Nigeria Deposit Insurance Corporation Act (1990). It was and still a member of the Financial Reporting Council of Nigeria. It also complemented the regulatory and supervisory role of the CBN in the liquidation of distressed banks and management of their assets until they are fully liquidated, although it reports to the Federal Ministry of Finance. Under a 'Purchase & Assumption' arrangement, the NDIC may arrange for the assets and liabilities of a failed bank to be taken over by another bank. For instance, in October 2007, the United Bank for Africa (UBA) assumed the fixed assets and private sector deposit liabilities of African Express Bank (AEB) under direction of the CBN and the NDIC.[10]

Depositors of insured banks are by the law that established the NDIC also allowed to file their claims (which signify that depositors have money in the banks) within 18 months after the bank has been closed. Whenever a bank is closed, and the assets and liabilities of the bank are determined by the NDIC and claims filed by depositors, the NDIC would pay insured deposits of maximum of ₦50,000 from the pool of premium, which is normally being paid by a bank when it was alive. Later, the NDIC would embark upon the sale of assets of the bank while debts are

[6]. G.A. Ogunleye, *Perspective on the Nigerian Financial Safety-Net*, Abuja, NDIC, 2010, P. 154.
[7]. P. Aguolu, *Financial Institutions in Nigeria*, Onitsha, Adson Educational Publishers, 2009, p. 17.
[8]. Interview with Malam Shafi'u Muhammad (Head of Establishment), NDIC Zonal Office, Sokoto, on Wednesday, 22nd July, 2015.
[9]. See *Basic Knowledge on Banking and Deposit Insurance*, a Pamphlet Published by the NDIC, 2013, pp 22-24.
[10]. A. Idris, "UBA Takes Over Afex Bank, Pays out ₦ 9bn to Customers of Acquired Banks", *Daily Sun Newspaper*, Wednesday 10th October, 2007, p. 17.

recovered from their debtors. The proceed would, then be used to pay liquidation dividend (excess deposit amount above ₦50,000) to depositors of the bank. If there is any amount remaining after all depositors have been paid, the money would be used to settle creditors and then later, share holders of the bank.[11]

However, following enactment of the NDIC Act, 2006 the maximum insured deposits to be paid by the NDIC had since then been reviewed upward to ₦500,000 and ₦200,000 for money deposits and microfinance banks respectively.[12] Henceforth, the NDIC pays up to a maximum of ₦500,000 (insured amount) for each depositor in respect of deposit held in each deposit money bank or non-interest bank and ₦200,000 (insured amount) for each depositor in microfinance bank or primary mortgage bank. It has been a responsibility of banks to bear the cost of protection enjoyed by their depositors. That cost of protection being paid by banks for their depositors to insurance services in the event of distress or collapse is called 'premium'.[13] This implies that the protection which the depositors enjoyed under the deposit insurance scheme administered by the NDIC was free for the depositors.

It is important at this point to note that the CBN in conjunction with the NDIC had begun a process of bank restructuring in 1990. Initially, 6 insolvent banks were identified and were allowed self-restructuring under the close supervision of the CBN and NDIC. However, since then, there was an increase in the number of insolvent banks in the system. Since late 1992, a joint committee of the CBN and NDIC involving a sector of the Banks and Other Financial Institutions Decree (BOFID) had assumed greater control over distressed banks. Thus, banks took over by the CBN had their Board of Directors dissolved and an interim management board appointed to exercise powers normally vested in the Board of Directors of a bank and some turn-around measures, including the downsizing of operations through rationalisation of staff and branch-network. The Boards are also empowered to appoint independent firms of auditors to ascertain the true financial condition of each of the banks. Thereafter, appropriate restructuring or liquidation options would be adopted.[14] A typical example of this scenario took place in the banking sector of Nigeria later in 2011, when the NDIC after due consultations with the CBN and the Federal Ministry of Finance and through the Asset Management Corporation of Nigeria (AMCON), established in July, 2010, opted for the use of 'bridge bank' mechanism to resolve the failure of Afribank Nig. Plc, Bank PHB Plc and Spring Bank Plc. Consequently, the NDIC incorporated three (3) bridge banks, namely: Mainstreet Bank Ltd, Keystone Bank Ltd and Enterprise Bank Ltd; to assume the assets and liabilities of the aforementioned failed banks.[15]

Role of NDIC in the Nigeria's Banking Sector

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11. E.C. Emenike, "Performance of the Nigeria Deposit..., p. 105.
12. Malam Shafi'u Muhammad...,
13. Basic Knowledge on Banking and Deposit Insurance..., p. 21.
14. S.I. Ikhide, "Financial Sector Reforms and Monetary Policy in Nigeria", IDS Working Paper, 68, 1996, p. 28.
15. The term 'bridge bank' refers to a temporary bank established and operated usually by a deposit insurer to acquire the assets and assume the liabilities of a failed bank until a final resolution is accomplished. It is said to have originated from the United States of America (USA), following the enactment of the Competitive Equality of Banks Act of 1987. The United States, through the Federal Deposit Insurance Corporation (FDIC), was therefore the first to establish a bridge bank in 1987. For more on this and resorting to bridge bank mechanism in Nigeria, see NDIC, *Bridge Bank as a Failure Resolution Option in Nigeria*, Abuja, 2013, p. 10 and p. 29.

The establishment of NDIC following the deregulation of the financial system under the SAP was to provide a further layer of protection for depositors, promote financial stability by complementing the supervisory activities of the CBN in ensuring a safe and sound banking system. According to the mission statement of the NDIC, it was established:

To protect depositors and contribute to the stability of the financial system through effective supervision of insured institutions, provision of financial and technical assistance to eligible insured institutions, prompt payment of guaranteed sums and orderly resolution of failed insured institutions.[16]

Since the NDIC was established to ensure the safety of bank deposits, it was therefore a body helping to ensure peace and stability in the banking sector.[17] The corporation has to a larger extent so far, achieved some of these by working in collaboration with other safety net participants particularly the CBN, to restore confidence of Nigerians in the banking sector.[18]

Another area, in which the NDIC is playing a critical role in the Nigeria's banking sector during the nearly thirty years of its existence, is in the area of assisting the CBN to safeguard the banking sector of the country. Depending on the severity and peculiarity of the distress, the NDIC in collaboration with the CBN, has, over the years, successfully adopted such measures as provision of financial assistance, imposition of prompt corrective actions, assumption of control and management, restructuring and sale of some distressed banks as well as liquidation of the terminally distressed banks as a last but unavoidable option.[19] The corporation has therefore, recorded remarkable progress towards restoring stability and soundness to the Nigerian banking system. Hence, it has successfully minimised fear of distress and failure of banks from the minds of Nigerians and relatively promotion of financial literacy in the country. By financial literacy, it means basic money management skills like budgets, savings, investments and insurance. It can also be defined as the ability to use knowledge and skills to manage one's financial resources effectively for life time financial security.[20] Being one of the major stakeholders in the Nigerian financial system, the NDIC embarked on studies on financial literacy with a view to assessing its level and identifying areas that requires prompt action in the country. This, the corporation achieved later in 2013 by publishing a report titled, "Financial Literacy in Nigeria: A Study Report."[21] The report captured areas of money management, financial behaviour, financial planning, financial knowledge and financial experiences. It among other things examined Nigerians and their attitude to money; how they earned it, how they managed it, how they saved it and how they spent it. The report finally, revealed that larger population of Nigerians need to be better educated on the importance of tracking their expenses and how to go about it. It further revealed the need for Nigerians to exhibit good financial behaviour such as keeping themselves informed about personal money management and seeking for financial advice from professionals.[22] The report is indeed a contribution to financial awareness and literacy in Nigeria.

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16. NDIC, "A brief on Nigeria Deposit Insurance Corporation (NDIC) to the House Committee on Banking and Currency", p.1.
17. Oral interview with Ahmad Sanda (Professor of Financial Economics), 55 years, Department of Economics, Usmanu Danfodiyo University, Sokoto, on Sunday 16th August, 2015.
18. NDIC, "A brief on Nigeria Deposit Insurance Corporation…", p. 1.
19. G. A. Ogunleye, "Deposit Insurance Scheme in Nigeria...", p. 7.
20. See NDIC, *Financial Literacy in Nigeria: A Study Report*, Abuja, NDIC, 2013, P. 9.
21. Malam Shafi'u Muhammad...,
22. NDIC, *Financial Literacy in Nigeria*..., p. VI.

Conclusion

The economic reforms introduced by the Babangida military regime under the auspice of SAP in Nigeria were responsible for deregulation and liberalization of the country's economy in general, and that of its financial sector in particular. It was the deregulated banking sector of the regime that increased the number of banks and elaborated inter competition among the banks in the country. The ultimate result of that development was gradual collapse of a number of banks in the country. In order to deal squarely with the problem, the NDIC was established in 1988. It has been clearly demonstrated in the paper that, the Corporation has during almost three decades of its existence, achieved some of the main purposes of its establishment i.e. protection of depositors' deposits especially in the event of bank distress or failure and promotion of stability in the Nigeria's banking sector.

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