
**United States Agency for International Development
&
Barents Group LLC**

Technical Assistance to the
Palestinian Monetary Authority

SEGIR GBTI
Contract No: PCE-I-800-98-00012

QUARTERLY REPORT #8

For Period Ending: December 31, 2000

Contracting Technical Officer
Jonhy Zeidan

Prepared by:
Barbara M. Kaminski, Resident Advisor
Daniel T. Callis, Jr., Resident Advisor

Quarterly Report

I. Background

USAID awarded Barents Group of KPMG Consulting LLC a delivery order for a three-year comprehensive bank supervision technical assistance program on September 29, 1998. The original program provided for two full-time resident advisors in the Palestinian Monetary Authority (PMA) complemented by short-term assistance in various areas of the bank supervision function. A subsequent revision to the contract in September 1999 allowed for a full-time advisor in the PMA/Gaza offices. The purpose of this program is to provide the PMA with the assistance necessary to carry out an independent bank supervision function.

Given initial concerns within the PMA regarding secrecy of information, the technical assistance program did not receive approval from the Palestinian Authority until late December 1998. Resident Advisor, Jay S. Doeden, arrived in West Bank/Gaza to begin the program on February 1, 1999. Progress toward Tangible Results and Benchmarks will be discussed from this date.

On August 24, 1999, USAID/West Bank & Gaza confirmed, in writing, the appointment of two counterparts for this technical assistance program. Mr. Moosa Salman was named to serve as the counterpart for onsite bank supervision; Mr. Ahmed Abdul Halim was to serve as the counterpart for offsite supervision. This was the counterpart designation until early June 2000 when Mr. Halim left his post at the PMA and Mr. Qasim M. Qasim was named as the onsite counterpart. Mr. Qasim resigned as the Executive Director Bank Supervision during the third quarter of 2000 and Mr. Salman assumed the counterpart role for both onsite and offsite supervision as well.

Mr. Salman retired from the PMA on October 30, 2000. Mr. Khaled Kayed has been named Deputy Executive Director for Offsite Supervision and assumed the counterpart role for the offsite component. The PMA hired Mr. Mohammed Kirresh in November 2000 to serve as Deputy Executive Director for Onsite Supervision and he assumed the counterpart role for the onsite component.

Mr. Ali Shaheen served as the counterpart for the Resident Advisor-Gaza until he resigned from the PMA on August 31, 2000. Mr. Salem Sabbah took over the role of counterpart in Gaza until the resident advisor was reassigned to the Ramallah office on November 15, 2000.

II. Status of the Financial Sector

The population of banks supervised by the PMA totals 23. These banks are a combination of institutions in West Bank and Gaza (national banks) as well as institutions from other Arab countries, Western Europe and Australia (foreign banks). The PMA began efforts during 1999 to conduct onsite bank examinations in each of these institutions. PMA

senior management approved a comprehensive examination schedule, which was followed throughout the year. As of December 31, 1999, six banking entities remained to be examined. Bank examinations commenced during 2000 to accomplish reviews of the six banks not examined during 1999. Prior to the 1999 examinations, primary bank supervision was accomplished through offsite surveillance. Although the PMA uses monthly and quarterly reporting forms provided through an IMF technical assistance program, the lack of verification of data by the onsite examination process raises concerns as to the validity and reliability of the numbers.

III. Progress Relative to Tangible Results

This report encompasses the project's progress during the months October - December 2000, inclusive. This is the eighth quarterly report filed since the advisors' onsite presence began in February 1999.

The Resident Advisors have been unable to access the PMA on a regular basis since September 28, 2000, due to violent conflicts in the West Bank and Gaza Strip. The U.S. State Department issued a travel warning on October 1, 2000, advising U.S. citizens to defer travel to the West Bank and Gaza Strip. For the first two months of the quarter, the advisors worked from their homes in Jerusalem. Beginning on December 7, 2000, the advisors began traveling to the PMA up to three times each week.

The Tangible Results for this program can be grouped into seven categories:

1) Organizational Structure and Policy; 2) Onsite Supervision; 3) Offsite Supervision; 4) Legal and Regulatory; 5) Problem Bank Supervision; 6) Licensing, and; 7) Training.

Organizational Structure and Policy

There were no organizational structure and policy advisory services provided during this quarter. Mr. H. Joe Selby remains in contact with the resident advisors and provides policy guidance on an ad hoc basis to the team. At the time of this report, he has not scheduled his next visit to West Bank and Gaza.

Onsite Supervision

Jay S. Doeden

The resident advisor prepared a plan of action for the advisory team during the current civil unrest. He coordinated review and completion of the plan with the advisors and the DC Project Management and presented the plan to the USAID mission. In addition, he worked on commercial bank outreach programs in the areas of improved supervision techniques and bank reporting forms.

Resident Advisor Jay S. Doeden resigned from the project on November 15, 2000. Daniel Callis, previously the Onsite Resident Advisor – Gaza has been reassigned to be a Resident Advisor in Ramallah.

Daniel Callis

During the first month of the quarter, the Resident Advisor – Onsite conducted research on Islamic banking and completed preparations for the training program provided to coordinators in Ramallah. The program covered the new Report of Examination and the application of CAMELS ratings in the local banking environment. Delivery of the training was under way in the third quarter; the resident advisor has been unable to deliver the final sessions of the program due to the current intifada.

The resident advisor maintained regular contact with the Gaza office by telephone during the first half of the quarter in order to assess the situation. After being reassigned to Ramallah, contact with Gaza became more infrequent.

Dr. Amin Haddad requested that advisors prepare a written response to a letter addressing issues related to progress to-date and clarifying areas of concern. The resident advisor participated in the preparation of the response, which was sent on October 30, 2000 to the Deputy Governor and to the USAID Mission. The letter addresses issues related to Offsite Analysis (CAEL ratings), Uniform Bank Performance Report, bank supervision regulations, Onsite and Offsite Manual for Operation, job descriptions, problem bank supervision, bank licensing and strategy development. The response letter is included as attachment # 1.

The resident advisor was on annual leave from November 9 through December 4, 2000.

At the beginning of December 2000, the resident advisor designed a new work plan and presented it to the PMA for approval. On December 7, 2000, resident advisors traveled to Ramallah to meet Dr. Amin Haddad, Mr. Khaled Kayed and Mr. Muhammed Kirresh to discuss issues related to the new work plan, Report of Condition and Income implementation, the Manual of Operations and translation of the examination manual.

Subsequently, the resident advisor traveled several times to Ramallah, assisting the PMA in the implementation of the Report of Condition and Income, amending the Manual for Operations outlining the mission, objectives and responsibilities of the Supervision Department Council, and conducting several meeting with Mr. Khaled Kayed and Mr. Mohammed Kirresh regarding the implementation of the Manual for Operations.

The resident advisor also assisted in the preparation of a presentation introducing the Report of Condition and Income. He then attended the presentation in Ramallah to assist with questions and technical issues.

Offsite Supervision

The resident advisor worked at home in October 2000, after travel restrictions issued on October 1, 2000, prevented the advisor from traveling to the PMA office in Ramallah. However, the advisor remained in telephone contact with PMA staff in Ramallah and with

local staff in Nablus and continued to work on the development of offsite tools for the PMA as well as to support the PMA's ad hoc requests.

PMA personnel assisted the resident advisor in organizing the moving of papers and files from Ramallah to Jerusalem thus facilitating the continuation of the design of offsite tools. As a result, the resident advisor was able to continue to develop the off-site supervision course previously delivered to the existing bank supervision staff and newly hired employees. The course focused on financial statement CAEL ratio analysis and its application in the early warning system. In addition, the course reinforced concepts of compliance tracking, regulations and enforcement actions, integrated supervisory approach and development of the supervisory strategy. The power point presentation was delivered to PMA employees in May and June 2000. In October 2000, the resident advisor added accompanying notes to the presentation so that it can be delivered by other presenters and will be added to the training library of the PMA supervision department.

The resident advisor contacted Deputy Governor Dr. Amin Haddad to discuss issues raised in his letter dated October 16, 2000. Dr. Amin Haddad requested that advisors prepare a written response, addressing issues related to progress to-date and clarifying areas of concern. The resident advisor participated in the preparation of the response, which was sent on October 30, 2000, to the Deputy Governor and to the USAID Mission. The letter addresses issues related to offsite analysis (CAEL ratings), Uniform Bank Performance Report, bank supervision regulations, Onsite and Offsite Manual for Operation, job descriptions, problem bank supervision, bank licensing and strategy development. The response letter is included as attachment # 1.

In November 2000, the resident advisor continued the development of the first phase of the Offsite Analysis Manual. This section focuses on the earnings analysis based on the review of the quarterly Uniform Bank Performance Report (UBPR). The resident advisor also researched accounting issues for Islamic banks in preparation for the development of reporting for the Islamic segment of the Palestinian banking sector.

On November 14 and 15, 2000, the resident advisor participated in meetings with James E. Horner, Barents Group Managing Director, and Mr. Johny Zeidan, USAID Contracting Technical Officer, to review progress on project deliverables and to discuss a plan of action for the next eleven months. The resident advisor subsequently prepared a new work plan for off-site supervision, containing the plan of action for Report of Condition and Income implementation, Uniform Bank Performance Report programming, testing and design of output reports and Early Warning System development for the PMA supervision department. The new work plan was presented for the USAID, Barents management and PMA management approval.

Throughout the month of November 2000, the resident advisor maintained on-going telephone and e-mail contact with PMA staff in Ramallah and local staff in Nablus.

At the beginning of December 2000, the resident advisor began to implement the new work plan and conducted the final review of the Report of Condition and Income. On December 7, 2000, the resident advisors traveled to Ramallah to meet with Dr. Amin Haddad, Mr. Khaled Kayed and Mr. Muhammed Kirresh to discuss issues related to the new work plan, Report of Condition and Income implementation, Manual of Operations and translation of the examination manual.

Subsequently, the resident advisor traveled several times to Ramallah, assisting the PMA in the implementation of Report of Condition and Income, amending the Manual for Operations outlining the mission, objectives and responsibilities of the Supervision Department Council and conducting several meeting with Mr. Khaled Kayed and Mr. Muhammed Kirresh regarding the implementation of the Manual for Operations.

The resident advisor also prepared a presentation introducing the Report of Condition and Income and conducted meetings with Mr. Ali Faroun and Mr. Ghassan in order to review the presentation and to coach the presenters before they delivered the presentation to PMA staff.

The resident Advisor left for annual leave on December 22, 2000, and returned to Jerusalem on January 6, 2001. Resident advisor was also absent between December 10 and 14, 2000, traveling to Poland for family reasons.

Legal and Regulatory

No legal and regulatory activities were conducted during this quarter.

Problem Bank Supervision

No problem bank supervision assistance was conducted during the quarter.

Licensing

No licensing assistance was provided during the quarter.

Training

No training assistance was provided during the quarter.

IV. Progress Relative to Benchmarks

Upon completion of the diagnostic review during March 1999, the advisory team began the task of starting several aspects of the program. Tangible Results and Benchmarks were reviewed under the subject task order. A work plan was devised by the initial resident advisor/project manager, encompassing the project's plan of action over the period of February 1999 through September 2001. This workplan was submitted under separate cover to USAID/West Bank & Gaza on April 1, 1999. A revised workplan was submitted to USAID and the PMA on March 9, 2000.

Barents Group Managing Director James E. Horner traveled to the region during the week of November 13, 2000, to participate in meetings and discussions necessary to define the status of the ongoing assistance program to the PMA and to reach agreement in making suggestions to USAID relative to the focus of the program over its final year. Further, suggestions were made relative to the composition of Barents Group's advisory team. For complete details of this trip, please see the trip report included here as attachment #2. As a result of this trip, new workplans were developed by the advisors and presented to the PMA, USAID, and Barents Group management for approval.

Benchmarks

A policy proposal for dealing with cross-border supervisory issues should be presented to the Governor of the PMA within two quarters from the beginning of the contract. By the end of the first year evidence should be presented that policy & procedures for handling this issue are in place and being executed.

Initial work on the cross-border policy began in May 1999 when senior policy advisor, Mr. H. Joe Selby, worked to identify the weaknesses in the current Cross-Border Agreements with the countries of Jordan, Egypt and Tunisia. The draft Agreement was presented to Governor Fouad Beseiso on July 19, 1999 and later approved, verbally, by Dr. Beseiso, on August 17, 1999. As of this report, the Cross-Border Agreement has not been negotiated or implemented with other central banks having banking activities in the West Bank/Gaza.

By the end of the first year the BSD should have a strategy statement and within eighteen months there should be clear evidence that this strategy is being translated into day-to-day operations.

The senior policy advisor presented the draft Bank Supervision Strategic Plan to Governor Fouad Beseiso on September 7, 1999. At that time, Governor Beseiso agreed to review the document and to prepare his comments for the advisor's continued assistance in late third quarter 1999. As of this report, the Strategic Plan has not been prepared by the PMA for review nor have efforts been taken to prepare it to day-to-day operations. It was the expectation of the senior policy advisor during his November 1999 visit to accomplish this. PMA senior management was not prepared to carry this out. The Strategic Plan remains in draft form and under the review of Governor Beseiso and his senior management team.

The advisors developed a manual for operations upon the request of PMA management. This manual outlines the mission, objects, and responsibilities of the Bank Supervision Department as a whole, the Supervision Department Council and of each unit of the department. In addition, it contains detailed descriptions of each professional job in the department, including job summaries, responsibilities, and requirements. It further provides detailed descriptions of each responsibility and describes lines of authority and

communication. The manual has been undergoing extensive review by PMA management and staff.

Within two quarters a bank examination schedule should be prepared as well as preliminary versions of standardized documents relating to onsite examination such as report of examinations, request letters to banks and formatted working papers. By the end of the first year, evidence should be presented that examinations are being conducted according to a pre-determined schedule and standardized documents are being routinely employed.

A 1999 bank examination schedule was prepared by PMA during the first quarter of this project (February 1999). This was a comprehensive plan of action to examine all banks (including branches) in the PMA system by year-end 1999. It was an aggressive expectation given the current staffing levels and the expertise of the examination teams in West Bank/Gaza. Although the advisor has presented numerous tools for use in the onsite examination process, they are not being used as a standard practice. Such documents must be used, after appropriate training, in the context of a revised onsite bank supervisory process. Given the continued reluctance of PMA senior management to allow advisors in the onsite bank examination process, this benchmark target date should be adjusted to reflect this perspective. Benchmarks will be reviewed upon the signing of the agreement between PMA and USAID.

Although the advisors are not allowed in the onsite exam process, efforts continue to prepare a handbook (manual) for onsite bank supervision. As of this report, chapters on the following subjects have been written, translated and undergone first review for use:

Planning and Control; Internal and External Audits; Review of Regulatory Reports; Analytical Review of Income and Expense (Earnings); Capital Accounts and Dividends; Deposit Accounts; Commercial Loans; Letters of Credit; Guaranties Issued; Funds Management (Asset-Liability Management); Management and Board Processes, Foreign Exchange, Real Estate Loans, Loan Portfolio Management and Related Organizations.

With these chapters, the PMA bank supervision department has the tools to conduct onsite bank examinations under an international approach using the CAMELS rating system. It should be noted that the process to use these procedures must be supported and enhanced by the use of scheduled classroom training courses.

In addition, the advisors presented the PMA with a standardized examination report and a document on CAMELS ratings. The document outlines the CAMELS ratings process and provides extensive definitions of each of the CAMELS components and of the composite rating. A training program was conducted in the third quarter of 2000 for examiners-in-charge in Ramallah, specifically focusing on how these processes can be used in West Bank/Gaza. The training was underway at the start of the civil unrest.

By the end of the first year the BSD should be able to conduct a full scope examination.

The resident advisors are not participating in onsite examinations at this time. Bank supervision management in Ramallah and Gaza are prohibiting such participation until the PMA Board and Governor Beseiso approve. At the time of this report, this remains an impediment to progress.

By the end of six months a preliminary plan for rationalization of a Call Report should be presented which should be adopted by the end of the first year of the contract. By the end of the first year of the contract at least a rudimentary early warning system should be in place with summary management reports for senior management. By the end of the first year a draft offsite policy and procedures manual should be in place.

The resident advisor/offsite supervision has made substantial progress in the area of rationalization of the banks' Call Report (bank reporting forms). As of this report, the final review of the English version of the Call Report has been completed and the report and accompanying schedules and line item instructions are ready to be sent to the banking industry. Currently, the Arabic version is being reviewed again by PMA staff pending announcement of an implementation date.

By the end of six months, work should have begun on a pilot program for problem bank resolution.

Given the focus of the PMA bank supervision department on the examination schedule, no work has been completed to date on the problem bank program. Although a problem bank advisor met with bank supervision and senior PMA management in October 1999, no specific pilot program has been initiated. This benchmark will be reviewed and revised with regard to target dates upon the signature of the agreement between PMA and USAID. The PMA's limiting access to banks is also impeding this process.

By the end of the first year a draft policy and procedures manual for problem bank resolution should be prepared.

The short-term problem bank advisor provided a draft problem bank manual. This manual must be incorporated into the pilot problem bank program in order to test it for applicability to the Palestinian legal framework and banking environment.

By the end of the first year recommendations should be prepared regarding policies and procedures for evaluating licensing applications.

During October 1999, a licensing expert continued efforts started earlier in the contract. The advisor developed a comprehensive bank license approval package. This package provides for more detailed information regarding the potential bank's founders along with the managing board and bank administrators. The advisor also developed a document

processing checklist to ensure that all pertinent documents relating to the bank's application are checked when received. The advisor provided guidance on the treatment of Money Changers under the bank regulatory processes in the West Bank/Gaza. These policies and procedures remain outstanding items with regard to follow-up by the PMA.

By the end of the first year an outreach program to improve communication with the commercial banks should be in draft form.

The senior policy advisor began efforts on this benchmark during his November 1999 visit. Mr. Selby met with several commercial bankers as well as representatives of the accounting community in order to determine the concerns they faced in their dealings with the PMA. From these meetings, Mr. Selby determined that a more comprehensive approach to standardize communication activities with the banking and financial community is needed. This will be addressed during subsequent visits by the policy advisor. The policy advisor is not scheduled to return to the PMA until an agreed upon period for the advisor's work is received from Governor Beseiso.

By the end of the first six months an evaluation should be made on the deficiencies in the regulatory structure. By the end of the first year drafts of changes to the regulatory structure should be prepared for discussion with counterparts.

Work on this benchmark was initially deferred pending the approval by PMA senior management of the overall Strategic Plan submitted by the Barents Group Senior Policy Advisor. Draft regulations were subsequently developed in August and September 2000 covering Provisions and Collateral for Facilities, Credit Concentrations and Investment in Securities, Capital Adequacy Ratio and Minimum Capital Requirements, Open Currency Positions, Liquidity Requirements, and Investment Securities and Bank Dealer Activities. In addition, a definition of 'resident' was prepared according to IMF requirements. The draft regulations were compared against the draft of the Palestinian Banking Law to ensure that they complied with its articles. PMA management decided to postpone implementation of the new regulations indefinitely.

Within three months, a draft integrated bank supervision training program should be prepared for approval by the PMA. By the end of six months at least monthly classes should be in place.

A comprehensive training program was provided to new hires during the first and second quarters of 2000. In addition, several ad hoc training sessions have been conducted throughout the run of the project as needed. No training was conducted during the current quarter, as the advisors were unable to travel regularly to the PMA.

V. Status of Project Sequencing

Per the discussions between USAID and the PMA regarding a written Letter of Agreement, the advisory team prepared a revised workplan. This workplan addresses the

period from March 2000 through September 2001. It is based on the existing Tangible Results and Benchmarks. New work plans were developed as a result of the visit of the Managing Director in November and presented to the PMA, USAID, and Barents Group senior management. Should revisions need to be addressed, the advisors will discuss and finalize with CTR Johny Zeidan, USAID/West Bank and Gaza.

VI. Impediments to Progress

The senior policy advisor continues to note the lack of focus on organizational and policy issues within the PMA. This is demonstrated through PMA management's failure to identify the next steps regarding the Bank Supervision Strategic Plan as well as the lack of implementation of the Cross-Border Supervisory Agreement.

Senior PMA managers and bank supervision middle management are prohibiting the participation of Barents Group technical advisors during the onsite bank examinations. An integral portion of this technical assistance program relies on the fact that the experts will provide "on-the-job" technical assistance.

Several impediments to progress occurred during the Call Report development process. The most serious is lack of consistent and clear regulatory framework, making the design of compliance reports a challenging task. Presently, the proposed Banking Act remains in draft form and the existing regulations and circulars are not always aligned with its requirements. In addition, several important areas of banking operations, such as securities trading and investment and overdraft provisioning remain unregulated, and other areas such as capital adequacy require a thorough review and much more detailed treatment. This situation makes any effort to bring transparency and uniformity to the system practically unattainable. The advisors assisted PMA staff in preparing a comprehensive set of regulations that would address the problems outlined above. PMA senior management has decided to defer implementation of the regulations until a future date.

At the beginning of this quarter, a period of serious civil unrest began in the West Bank and Gaza Strip, severely limiting access to the PMA offices to both advisors and PMA staff. However, the advisors have repeatedly traveled to the PMA office and have sought numerous ways to proceed with implementation of the Call Report, the manuals, and the new organizational structure of the department, as well as assisting PMA management in various ad hoc requests. The civil unrest is continuing, negatively impacting the implementation process.

VII. Role of the Counterpart

Although the staff levels of the PMA are very receptive to all technical assistance, members of middle management are reluctant to fully use the technical advisors. Advisory services are expected to be more "offsite" which impedes the ability of the technical advisory team to fully understand how to best provide training regarding the Palestinian

banking sector. Given the pressures of the examination schedule, it has been difficult to determine the overall counterpart buy-in at all levels. However, during individual discussions and small ad hoc training sessions, the bank examiners are anxious to improve their bank supervision skills, receive training, and to examine their banks in a more professional, international manner.

VIII. Additional Tasks Delivered During the Quarter

None

IX. Role of Other Donor Organizations

There has been no activity with other donor organizations during the quarter.

Appendices

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November 27, 2000

Mr. Johny Zeidan
Cognizant Technical Officer
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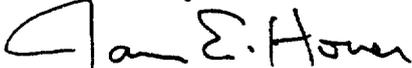
Subject: Strengthening of the Palestinian Monetary Authority
Task Order No: PCE-I-800-98-00012-00
Trip Report of James Horner: 11/13-17/00

Dear Mr. Zeidan:

Please find the attached trip report covering the scope and conclusions of my recent visit to Israel under the above referenced project. As you are aware, I was involved in a number of meetings and phone calls with Barents' resident team, Dr. Amin Haddad of the Palestinian Monetary Authority, and USAID officials during the period of Tuesday, November 14th thru Friday November 17th. This trip report summarizes those meetings/conversations and also proposes staffing and work objectives as we enter the final 12 month period of this project. A number of conclusions are reached, and recommendations submitted.

If you have any questions, please feel free to contact me via email at jhorner@kpmg.com or via phone at (703) 237 8876.

Sincerely,



James E. Horner
Managing Director
Barents Group of KPMG Consulting, LLC

**United States Agency for International Development
Strengthening of the Palestinian Monetary Authority
Task Order No: PCE-I-800-98-00012-00**

**Trip Report of James Horner: 11/13-17/00
Managing Director, Barents Group**

Purpose of Trip:

Barents' Managing Director for the subject project traveled to Israel the week of 11/13/00 to participate meetings and discussions necessary to define the status of the ongoing assistance program to the Palestinian Monetary Authority and to reach agreement in making suggestions to USAID relative to the focus of the program over its final year. Further, suggestions would be made relative to the composition of Barents' advisory team.

Nature of Meetings and Conversations:

11/14/00: Afternoon meeting between Mr. Horner and Chief of Party Mr. Jay Doeden and Offsite Advisor Mrs. Barbara Kaminski to discuss project status and establish recommendations for future approach.

11/15/00: Morning meeting between Horner and Offsite Advisor Kaminski. Afternoon meeting with between Horner and USAID Project Officer Mr. Johny Zeidan and Offsite Advisor Kaminski. Afternoon phone conversation between Horner and PMA Vice Chairman Dr. Amin Haddad. All meetings/conversations related to project status, underscoring the building of consensus as to program focus and objectives from the current period thru the scheduled completion date 9/30/01.

11/16/00: Morning phone conversation between Horner, Zeidan, and Dr. Amin Haddad. Afternoon meeting between Horner and USAID (Margo Ellis, Courtney Blair, Johny Zeidan). Discussions of program scope and approach, and recommendations for the future.

11/17/00: Morning meeting between Horner and Deputy Mission Director William Hammink and Johny Zeidan. Discussion of program status, and recommendations for future.

Summary of Findings:

Discussions during this trip confirmed the need for Barents, the PMA and USAID to reach a common understanding and commitment regarding the scope and delivery of the technical assistance program. Due primarily to a communication breakdown within the PMA, and between Barents and the PMA, the need to restructure the composition of the Barents team and prioritize the focus of the work plan was agreed by all parties. Further, the increasingly clear role of Dr. Amin Haddad in leading the PMA's efforts to strengthen its banking supervision capacity reflects the need to incorporate Dr. Amin's views into the project's terms of reference. Importantly, Dr. Amin's objectives do not differ from the intent of the original terms of reference of the USAID program. However, it was agreed that Dr. Amin should (and desires to) have a greater voice in the method in which the technical assistance is delivered.

Composition of Team:

Mutual agreement was reached between USAID, the PMA and Barents that Chief of Party Doeden would cease working under the project effective 11/15/00. This decision was largely based upon the need create a new, revitalized working relationship between the Barents Chief of Party and Dr. Amin. Although Dr. Amin expressed praise for Mr. Doeden's technical skills, he did feel that communication channels were strained. Barents had a similar view and suggested the change. USAID and the PMA concurred.

Dr. Amin agreed to work with Barbara Kaminski on a daily basis as the Chief of Party. Further, once travel clearance is granted for advisors to work inside PMA headquarters, Barents indicated its willingness to propose to USAID and the PMA a new "senior" and "experienced" advisor to supplement the efforts of Mrs. Kaminski and Resident Onsite Advisor Daniel Callis. This new advisor would work directly with Dr. Amin and a soon to be appointed Executive Director on priority issues as defined by the PMA. Barents suggests that such an advisor initially only be detailed to the project for a period of 2-3 months, and then an assessment could be made whether the person and role was appropriate in addressing project and PMA needs.

Work Plan: 11/15/00 thru 9/30/01:

Benchmarks and Tangible Works as initially defined under the task order remain valid. Progress in achieving objectives over the first two years is evident, but to differing degrees.. In most cases, programs, policies, procedures, supervisory tools, etc. have been defined or drafted. What has been lacking in a number of cases is implementation of these "principles" by the PMA. Barents' view is that the lack of implementation is not by PMA "design" but rather a previous lack of direction and accountability within the middle management ranks of the organization. During the course of discussions, Dr. Amin repeatedly committed to address this obstacle by providing concrete direction

(orders) to his managers relative to working with the Barents advisors and relative to implementing the recommendations (rather than just “considering” or “learning” about them). Further, Dr. Amin desires to provide “expressed authority” to the Barents advisors – in essence, allowing the advisors to require PMA staff to attend working group meetings and formal/on-the-job training sessions, as well as the ability to take action in implementing new supervisory methods that Dr. Amin has agreed to.

Barents and the PMA agreed that effective immediately, the program of the advisors (Kaminski and Callis) should be very focused on several specific objectives/work steps. Barents and the PMA collectively believe that near-term progress can be made in both implementing key regulatory changes and in providing on-the-job training to PMA staff. The immediate focus will include:

- Implementation of modernized commercial bank call report and the building of a regulatory *bank performance report*:
 - Finalization of revised call report schedules and instructions
 - Testing of commercial bank data under the new call report structure
 - Internal training for PMA staff in the call report content and implementation plan
 - External training/orientation for commercial banks regarding the report
 - Implementation assistance to the commercial banks (thru the PMA)
 - Programming and testing of the *bank performance report*
 - Training to PMA staff in the use of the performance report, including the development of consistent and timely reports summarizing individual bank condition for use by PMA management

- Training and advice to the leaders of on-site examination teams (examiners in charge and team leaders):
 - Regular scheduled briefings/discussions either at the beginning of each day, or the end of each day
 - Direct advice from the Barents advisor to the PMA staff relative to planning, approach and procedures taken during the examinations
 - Implementation of the new supervisory manual and principles developed over the previous 24 months
 - Assistance in implementing a consistent, and internationally acceptable report of examination format
 - Advice relative to judgments and decisions/recommendations suggested by the PMA staff during the examinations
 - Suggestions relative to further instituting the supervisory plan and on-site examination calendar by the PMA

- Senior level consulting advice and assistance to Dr. Amin and the next Executive Director of Bank Supervision (subject to travel restrictions being lifted):
 - Responsive to the critical needs of the PMA
 - Focus on actions to address problem banks or crisis situations
 - Advice of organizational and personnel issues

- Advice relative to changes in regulation (those subject to PMA Board approval)
- Advice relative to supervisory strategy implementation by the PMA
- Development of customized study tour for Dr. Amin and/or the new Executive Director to the United States regulatory agencies, and possibly participation in the Toronto Leadership Centre for Financial Sector Supervisors:
 - 5-7 day highly focused study tour
 - Consultation with key officials from the Office of the Comptroller of the Currency, Office of the Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, etc.
 - Consideration for enrollment in the Toronto program (Summer 2001)
 - Content of study tour would be jointly developed by Dr. Amin and Barents Managing Director Horner

The above outlined program will be specifically detailed in specific work plans developed by the resident Barents advisors. Advisor Kaminski will maintain principle responsibility for the call report and bank performance report implementation. In fact, the detailed work steps for this element of the program have already been drafted, cleared through USAID, and provided to Dr. Amin for comment.

Advisor Callis will maintain responsibility for the on-site examination portion of the program. To truly be successful, this objective requires access to PMA examiners at PMA headquarters. Thus over the next 4-6 weeks (or until travel restrictions are lifted) Mr. Callis will assist Mrs. Kaminski with the aggressive schedule desired by Dr. Amin relative to call report and bank performance report implementation. Once travel clearance is provided, Mr. Callis will immediately define and implement a plan to ensure the necessary level of interaction with PMA on-site examination leaders. In the period prior to travel clearance being granted, Mr. Callis will also attempt to advise PMA examiners based upon working relationships he has already developed.

Existing travel restrictions do impact the ability of the Barents advisors to provide the best possible assistance. However, we do believe, at least over the next several months, that the advisors will still add great value to PMA objectives even while working from Jerusalem. Further, in an effort to maintain contact with the counterparts (beyond daily phone contact with both the counterparts and the Barents local hire assistant), efforts will be made to periodically meet in agreed "safe-haven" locations (subject to concurrence by USAID).

Program Status – Reevaluation:

Given the complexity of the situation in West Bank and Gaza, and the history of this particular technical assistance program, Barents agrees that the program should remain

*USAID – Palestinian Monetary Authority
Trip Report: James E. Horner*

under continuous reevaluation. Discussions between Dr. Amin, Mr. Zeidan and Mr. Horner during this trip did seem to reflect a new consensus and commitment from all parties that the program should and will be successful. Mr. Horner pledged to stay closely involved from Washington. Resident advisors Kaminski and Callis will go to great length to ensure full consultation with Dr. Amin. Once travel clearance is authorized, not only will the two residents be able to fully implement the programs referenced in this trip report, but Barents can then also suggest other short term advisors (specifically a senior advisor to work with Dr. Amin and his Executive Director).

Submitted: James E. Horner 11/27/00



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January 16, 2001

Dr. Amin Haddad
Deputy Governor
Palestine Monetary Authority

Subject: Response to Memorandum dated October 16, 2000

Dear Dr. Haddad:

I am writing in response to your letter dated October 16, 2000 which I received last week from Mr. Johny Zeidan. I have met with the advisory team who have provided valuable input to this letter. We find it unfortunate that the Palestine Monetary Authority is not satisfied with the technical assistance program. It is our objective to provide you with quality assistance under the Terms of Reference signed with USAID on September 28, 1998.

The sources of our responses are the USAID monthly and quarterly reports, memorandums prepared by our advisors to senior PMA management and bank supervision staff, as well as documentation we maintain on meetings and discussions held. We hope this information will clarify the progress to date and will alleviate many of your concerns with regard to the program. As always, we welcome your comments and feedback regarding these matters.

Training in Offsite Analyses (CAMEL ratings)

In April and May 2000, the Resident Advisor – Offsite Supervision conducted an offsite analysis course, including the CAEL rating system for the 12 new bank supervision hires. She repeated the course at the end of May for existing examiners and analysts in Ramallah. All course work was completed at the beginning of June. The course was scheduled for existing examiners and analysts in Gaza; however, you cancelled the Gaza course just prior to its commencement. Please refer to the quarterly report for April – June 2000 for a complete description of the course and its contents.

In late July 2000, the Advisors scheduled time with Mr. Salem Sabbah to review the current offsite analysis techniques and to propose improvements. However, you directed the Advisors at that time instead to spend that time revising regulations.

In September 2000, the Resident Advisor – Offsite Supervision met with each member of the offsite supervision unit in Ramallah, reviewed their day to day operations, identified problem areas, proposed solutions. Please refer to the Quarterly Report for the Period Ending September 30, 2000 for a complete description of identified problems and proposed solutions.

All examiners in Ramallah and Gaza were given a thorough review of CAMELS ratings in May 1999 through classroom seminars. The Resident Advisor - Gaza developed a more extensive CAMELS course to be delivered in August 2000; however, you cancelled this

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course before it began. The Gaza Advisor next developed a CAMELS course specifically for the onsite coordinators. The course was nearly completed at the end of September 2000.

Uniform Bank Performance Reports

The Report of Condition and Income, or Call Report, was completed on schedule in August 2000; this report forms the basis of the Uniform Bank Performance Report (UBPR). The next phase of this project is for the PMA to develop and program the UBPR while the banks are programming their systems to meet the new reporting requirements. Details of this project were explained in an October 16, 2000 memorandum to Mr. Moosa Salman.

In addition, a portion of the training program described in the first point above involved an extensive UBPR case study. Participants were required to submit two written reports, analyzing the case banks using a UBPR. The Ramallah Advisors reviewed these reports and provided feedback, both oral and written, to each participant individually to ensure that they will be ready to properly use this tool when it is available.

Bank Supervision Regulations

Beginning August 14, 2000, the Advisors met with PMA staff in Ramallah and Gaza, reviewed current circulars, and drafted a new set of regulations in accordance with your instructions. A final draft was developed in both English and Arabic with Mr. Moosa Salman on September 7, 2000. On September 10, 2000, you directed IMF Advisor Mr. Douglas Kruse to further review these regulations and make any changes he deemed necessary. The Barents Advisors met numerous times over the next two weeks with Mr. Kruse and Mr. Salman to complete the revisions. The process was finalized between these individuals with the final revisions to have been presented by Mr. Kruse to Mr. Salman prior to his departure.

Onsite and Offsite Manual for Operations

The draft Onsite Examination Manual (both English and Arabic versions) was delivered to the PMA in the Spring 2000. It contains extensive explanations of an organized and systematic approach to examining banks onsite. It includes step-by-step procedures whereby examiners must be trained in order to carry out the processes. In addition, the documents must be customized to the Palestinian banking system through their daily use and review. The PMA has pledged several times to review the documents but no action has been taken to date. Training courses mentioned above have already included sections on the purpose and practical use of this manual.

The draft Offsite Analysis Manual (English and Arabic versions) was delivered to Mr. Qasim M. Qasim, the former Executive Director of Bank Supervision in July 2000. It contains descriptions of types of offsite analysis, regulatory reporting requirements and the offsite supervisory process. As Resident Advisor Kaminski has informed you, the final version will be developed when the UBPR is programmed because the manual must to be customized to contain references to actual ratios and values.

The final Manual for Operations was delivered to the PMA in July 2000. After numerous discussions with you and your staff, the finalized version outlines the group's perspective on

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the mission, objectives, and responsibilities of the Bank Supervision Department as a whole and of each unit. In addition, it contains customized job responsibilities of managers, examiners and analysts. You announced the manual to be implemented in the PMA as of July 1, 2000; however to date, this has not happened.

Job Descriptions

Barents first learned of the specific request for job descriptions on September 12, 2000. The advisors developed eleven categories of job descriptions for offsite and onsite staff and reviewed them with PMA staff at the end of September. They were to be delivered to you upon your return from the IMF meeting in Prague; however, due to the problems in the West Bank and Gaza, we have been unable to work directly with your staff since October 1, 2000.

Reviewing Banking Supervision Circulars

Please see response to "Bank supervision regulations" above.

Problem Bank Supervision

Governor Fouad Beseiso approved the technical assistance of a senior bank supervision expert in October 1999. The purpose of this short-term trip was to review several problem banks and to provide guidance on the development of a problem bank supervision system. However, prior to his travel, the PMA took exception to providing any financial information to this advisor [lacking financial information, it would have been impossible for the advisor to complete a thorough bank analysis]. During his visit, he succeeded in obtaining limited financial documents for review from the bank supervision department.

The advisor reviewed three Palestinian problem banks that were identified by the bank supervision departmental management. Based upon these reviews (including financial analysis), our advisor prepared three extensive written memorandums that were presented to you on October 20, 1999 and also discussed with the bank supervision department on October 26, 1999. Our advisor also provided bank specific classroom training to the bank supervision staff in both Ramallah and Gaza.

With regard to the supervision of problem banks, there are three essential components. First, there must be a manual for problem bank supervision that stipulates the process for dealing with problem institutions. A draft manual was prepared by our short-term advisor and given to bank supervision management prior to his departure in October 1999. Second, there must be full access to the banks' financial information. This has not been granted by the PMA. Finally, the problem bank supervision experts/advisors must be allowed to work with the PMA staff (both onsite and offsite) in the examinations process. As we have discussed, the PMA does not allow access at this time to the onsite bank examinations process.

Bank Licensing

Barents Group has provided two short-term visits of a bank licensing expert. The first review in May 1999 included a comprehensive analysis of the existing bank licensing process which was conducted in collaboration with the PMA bank licensing personnel. The review also included an assessment of the Money Changer environment and the impact it has on the

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banking system. During the course of his visit, our advisor prepared a draft bank licensing manual which incorporated the local banking and legal environment. This manual was reviewed with the PMA Licensing staff who agreed it was beneficial to improve the processes.

The advisor returned in October 1999 to make an assessment of the implementation of the bank licensing manual. Mr. Henry Janiszewski conveyed his findings to you and Mr. Moosa Salman in a meeting on October 20, 1999. During the meeting, Mr. Janiszewski stated his finding that the manual had not been implemented. In addition, he raised the concern that the PMA needed a directive on bank licensing in order implement the improved process. It was agreed during the meeting that the PMA staff would prepare a directive that would be reviewed by Mr. Janiszewski (from offsite) and then taken through the necessary PMA approval process. The directive was not completed nor has the manual been implemented to date.

Strategy Development

Mr. H. Joe Selby, Senior Policy Advisor, provided policy advice on the organizational structure and strategy of bank supervision during 1999. Mr. Selby completed a strategy document at the culmination of his three-month assignment in the PMA, submitting the final report to Governor Foad Beseiso in September 1999. The document contained a revised organizational chart; workplan for strategy development; a proposed mission statement with objectives; and a plan for implementation (timeframes). At that time, he asked Dr. Beseiso to review the document and to prepare comments for the next Policy Advisor visit. In November 1999, Mr. Selby returned to follow-up on the strategy review and implementation process. Dr. Beseiso referred Mr. Selby to the PMA middle level management for their review and input. He met with these individuals and in general, received consensus that the document was feasible and appropriate for the PMA.

During early June 2000, when you initiated the efforts regarding the Manual for Operations, I met with you to discuss the process. At that time, I suggested that you use the Strategy document for the initial phases of your work given Mr. Selby had laid out exactly what you planned to do. I provided you with a copy of the Strategy and offered to provide my assistance in implementing the process. You advised that you would prefer to have the Strategy process remain with the Governor and Mr. Selby so we went directly to developing the Manual for Operations.

On behalf of the resident advisory team, I trust that this memorandum clarifies issues raised in your letter. As you know, our Managing Director, Mr. James E. Horner, planned to travel here in mid-October to finalize a 12-month project workplan. His trip has been temporarily postponed in light of the current travel restrictions. However, it is the intention of Barents Group and USAID to work collectively with you to finalize the final segment of this contract's assistance to fit the PMA's needs. If you have any questions, please do not hesitate to contact me at 050-803-753 or Mr. Johny Zeidan, Private Sector Specialist, USAID at 03-511-4841.

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Very truly yours,

Barents Group LLC

Jay S. Doeden
Project Manager