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*Strengthening of the Palestinian Monetary Authority
SEGIR GBTI
Contract No.: PCE-I-800-98-00012*

**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 #10

For Period Ending: June 30, 2001

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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 was named Deputy Executive Director for Offsite Supervision and assumed the counterpart role for the offsite component. In January 2001, Mr. Khaled Kayed resigned from his position in offsite supervision and the counterpart role. The PMA hired Mr. Mohammed Kirresh in November 2000 to serve as Deputy Executive Director for Onsite Supervision. He assumed the counterpart role for the onsite component in November 2000 and for the offsite component in January 2001.

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

On September 28, 2000, a period of serious civil unrest began in the West Bank and Gaza, straining the financial sector as well as all other aspects of life.

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). Prior to the 1999, primary bank supervision was accomplished through offsite surveillance. 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, 2000, eighteen banks had been examined during the year. Among those eighteen banks, four were examined according to the CAMELS methodology; these examinations were completed during the first quarter of 2001. 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. Barents Group Resident Advisors have developed methodologies whereby these forms can be verified by onsite staff during examinations and is supporting PMA staff as they gain experience with this process.

III. Progress Relative to Tangible Results

This report encompasses the project's progress during the months April through June 2001, inclusive. This is the tenth quarterly report filed since the advisors' onsite presence began in February 1999.

The Resident Advisors have traveled regularly to the PMA during the quarter despite the civil unrest and resultant safety concerns.

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

The Resident Advisor has been meeting daily one-on-one or in small groups with examiners-in-charge and their teams to discuss specific examination issues. Advice is given on a wide range of topics, including safety and soundness issues, compliance issues, examination procedures, interpretation of regulations, effective utilization of staff, and communication of examination findings to banks and to the PMA.

Several of these meetings have been held with examiners-in-charge with their exam teams to discuss written comments in the report of examination. These sessions often reveal areas where the examiners could have delved more deeply into problem areas and have at times resulted in additional visits to the bank to clarify examination findings. Also, Call Report verification procedures have resulted in the PMA requesting banks to submit corrected financial reports. These processes improve the quality of examination findings, the quality of information available for offsite analysis, and provides practical on-the-job training to examiners.

The Resident Advisor continued weekly meetings with all onsite and offsite coordinators, discussing general supervision and examination issues. The meetings continued discussions of the Core Principles of Bank Supervision, accounting issues, the manual for operations, and the examination manual. We also continued training in the use of the CAMELS rating system using a case study. The meetings are held in Ramallah with the Gaza office included by conference call.

The Resident Advisor revised the format for the Report of Examination, taking into account results from branch examinations and adding elements requested by Dr. Amin Haddad. The report was distributed to the examination staff for immediate use; reports currently in progress are being revised to meet the new format.

At the PMA's request, the Resident Advisors began developing a formal course on improving PMA staff's communication in Arabic. Professors have been located, hired, and are developing the materials for a 40 hour training course. The report of examination and CAEL analysis samples have been incorporated into the course materials. The PMA has now delayed the course pending other more pressing training needs, including a course on the use of Microsoft Excel.

Throughout the quarter, the Resident Advisors worked with the offsite and onsite units to encourage and enhance coordination and cooperation. Specifically, the Advisors developed a system whereby the offsite unit helps to prepare the onsite unit for examinations. The program involves an offsite financial analysis, and the units work together to outline issues and violations previously noted at a bank. The offsite unit then presents its findings to the examiner-in-charge. At that point, the examiner-in-charge is expected to develop a scope of examination before onsite work begins.

The Resident Advisor assisted in the effort to finalize the Regulation on Provisions and Collateral for Facilities so that it can be issued to the banks.

Offsite Supervision

At the beginning of the quarter, the Resident Advisor met with Dr. Amin Haddad to discuss changes to the onsite and offsite supervisory processes. As a result, PMA management required the staff to work daily with Resident Advisor in order to improve the performance of the offsite unit. The Resident Advisor designed a spreadsheet containing about 70 ratios and values and began to teach coordinators and analysts how to analyze the information. The spreadsheet also contains data for several quarters and is utilized for trend analysis. In addition, the Resident Advisor and the offsite staff reviewed data in terms of correctness and integrity of reporting and identified reporting errors. The results of the analysis were presented to the coordinators, who included the information in scopes of upcoming onsite examinations.

The offsite staff is required to prepare analysis of all banks in a new format on a quarterly basis and to ask banks for corrections when problems are identified in the supervisory reporting. In addition, the Resident Advisor reviewed compliance and the overall system of offsite reports and instituted report streamlining and rationalization process.

During May 2001, the Resident Advisor continued to meet daily with members of the offsite unit to discuss specific offsite examination issues. Each analyst is required to prepare a spreadsheet containing basic values and ratios for an individual bank. In addition, each analyst prepares a written report identifying reporting mistakes and containing the results of quarterly offsite analysis according to the CAEL methodology.

The offsite unit analyzed additional four banks according to the new methodology. The Resident Advisor discussed the results with each analyst and supported the offsite unit in developing a rudimentary Early Warning System. Each analyst communicated the results of the analysis to PMA management. The Resident Advisor plans to assist PMA management in development of a supervisory strategy for each bank.

In addition, the offsite unit is required to notify banks about reporting errors and ask for explanation and correction.

The Resident Advisor continued to support system reports streamlining and rationalization process. Advisor met several times with offsite coordinator and discussed additional systemic analysis elements.

During June 2001, the offsite unit began to incorporate audited banks' statements into the overall analysis. The resident advisor met daily with offsite and onsite staff in order to identify, reconcile and correct the differences between the audited statements and financial data in the PMA database. The PMA has communicated the results of this analysis to the banks and external auditors, asked for explanation of differences and for

correction of the PMA data. This process has been very beneficial not only in terms of disciplining the banks and increasing transparency in financial system but also as an educational tool for examiners and analysts who are trained not only to identify errors but also to communicate with banks in order to correct them.

The banks are implementing the new Report of Condition and Income. The PMA organized an outreach program for banks and invited banks' representatives to discuss issues and timeframes related to the new report implementation. The first outreach meeting was held at the PMA between April 9 and April 11, 2001. The Resident Advisor was invited to participate in the meeting and delivered a presentation outlining the differences between the new and the current reporting systems. Dr. Aruba Al-Barghothi, the head of the Payment System section of the PMA, also attended and addressed the reporting requirements of the Balance of Payment statistics. Dr. Jemal Nouh, the head of the IT department, presented the IT department plan to support the banks in the implementation of the new reporting and interface module design.

The second outreach meeting was held on May 8, 2001. Representatives of banks met with the PMA staff and the Resident Advisors to discuss Report of Condition and Income implementation issues. Information technology was the main topic of discussion during this workshop and the PMA gained an appreciation of the banks' perspective on cost and time estimates for the new reporting implementation. Dr. Jemal Nouh, the head of the IT department, continued to educate banks' IT staff on requirements of the new reporting and interface module design. The PMA plans to utilize the banking network, currently developed for the payment system, to help banks in linking their branches with their headquarters. Such a link should improve banks' ability to produce correct and timely financial statements and will have a positive impact on the new reports' implementation process.

The Report of Condition and Income had been revised until the moment it was released to the banks. Therefore, the existing version of the test bank does not reflect all the subsequent changes. Resident Advisor began to update the test bank and plans to deliver it to the IT department in May 2001. The test bank will be used during the development, design and testing of the Early Warning System.

On April 5, 2001, Resident Advisors met with the entire staff of the supervision department to discuss the regulatory data validation process. The Advisors presented a new validation form and provided detailed explanations related to the use of this new form. The Advisors also outlined unique and separate tasks and responsibilities of the onsite and the offsite staff in the validation process. The Resident Advisor assisted onsite examiners with the financial data verification process. The Resident Advisor reviewed data validation forms and developed additional spreadsheets combining multiple currencies into a total balance sheet. In addition, the Resident Advisor worked with onsite examiners at reconciling the PMA financial reporting with audited statements of

the banks. The process is completed for one bank and continued for two additional banks in June 2001.

The Resident Advisor met several times with Mr. Mohammed Kirresh to discuss progress of the new onsite and offsite process. During financial data validation review, the Resident Advisor discovered that most of the junior examiners do not have adequate Excel skills in order to validate complex, multiple currency reports and general ledgers. Therefore, the Resident Advisor asked Dr. Amin Haddad to authorize an Excel training session for the supervision staff. Dr. Jemal Nouh is in the process of organizing such training.

PMA management decided to issue a regulation prepared by the Advisors together with the PMA staff and reviewed by the IMF representatives regarding asset classification, provisions and admissible collateral. The Resident Advisors prepared the final draft with Mr. Salem Sabah and the regulation is ready to be approved by the Board and to be signed by the Acting Governor.

On June 27, 2001, Resident Advisors participated in a conference on Governance and the Business Environment in the West Bank and Gaza organized by the World Bank and Paltrade, under the patronage of the Minister of Economy and Trade, Mr. Maher Al-Masri.

On June 27, 2001, Resident Advisors met with Mr. Karim A. Nashashibi, senior analyst at the Middle Eastern Department at the IMF and discussed progress to date and possible future increased cooperation between the IMF and Barents advisors in strengthening the PMA supervisory capacity.

Legal and Regulatory

The PMA is in a process of issuing a new regulation on asset classification, provisions and admissible collateral, prepared by the Advisors in consultation with the IMF representative and the PMA staff. The regulation will supersede and be an improvement over an existing regulation. The new regulation conforms to Basle Core Principles and international regulatory practice. Other regulations regarding Capital Adequacy, insider lending, concentration and trading and investment were prepared concurrently with the asset classification regulation and are awaiting PMA decision to issue them.

Problem Bank Supervision

The PMA has put a bank into a limited receivership. The Resident Advisors supported the receiver by conducting analysis of the financial data of the institution, analyzing audited statements and discussing possible actions that could be taken by the receiver in order to improve the bank's condition.

Licensing

No licensing assistance was provided during the quarter.

Training

No formal, classroom training assistance was provided during the quarter. However, the Advisors continue to provide on-the-job training daily. They also identified a need for training in Microsoft Excel and facilitated the development of the course which will be conducted in the third 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. As a result of this trip, new work plans were developed by the advisors through March 2001 and approved by Barents Group and PMA management.

During March the Resident Advisors revised and updated their work plans through September 2001 and submitted them to 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 Foaud 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, objectives 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. Acting Governor Dr. Amin Haddad approved the manual for operations as an official guideline for operations of the supervision department. The Resident Advisors have met with the supervision staff on several occasions to provide training on the manual and to reinforce concepts of integrated supervision.

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 the 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 staffing levels at the time and the expertise of the examination teams in West Bank/Gaza. Although advisors have 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 during the 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 have 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 and was interrupted for several months. Training resumed in the first quarter of 2001.

During the first quarter of 2001, PMA management has increased its interest in these standardized reports and manuals and has supported Barents Group Advisors in implementation. Examiners have begun to test sections of the manual during on-site work and the examination report format has undergone further customization.

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 Acting Governor Haddad 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 new Report of Condition and Income, including schedules and line item instructions, has been completed and released to the banks. Banks reviewed these reports and the PMA, in conjunction with Barents Group advisors, conducted consultation sessions with the banks to promote timely and accurate submission of financial data. Currently, banks are adjusting their accounting and computer systems in order to submit data to the PMA in the new format at the end of December 2001. The PMA staff is monitoring banks' progress and supporting their effort as necessary. In addition, the PMA facilitated the development of electronic links connecting banks' headquarters with their branches, which will enhance speed and accuracy of financial data gathering by the banks.

Programming instructions for the Uniform Bank Performance Report (UBPR), an integral part of the early warning system, have been completed and submitted to the PMA's Information Technology Department. Presently, the Information Technology Department is designing an Oracle database that will capture data submitted by the banks and generate the UBPR.

In July 2000, a Manual for Operations was submitted to the PMA which includes policies and procedures, as well as lines of responsibility and mission objectives. The manual is awaiting approval by PMA management.

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. However, Advisors have begun to assist the PMA with bank receivership activities.

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 West Bank and Gaza until an agreed upon period for the advisor's work is received from the PMA.

Although no formal outreach program is in place, the PMA has begun to consult with banks on issues such as new regulations, regulatory reporting, management information systems, and information technology, and has included Barents Group advisors in these consultations.

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 is in the process of issuing the regulation on Provisions and Collateral for Facilities.

During the first quarter of 2001, Barents Group advisors assisted in the development of a specific regulation on Provisions and Collateral for Facilities for Islamic Banks. The regulation is awaiting PMA management approval.

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 project as needed. No classroom training sessions were conducted during the current quarter.

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.

At the request of the PMA, Resident Advisors prepared terms of reference for a senior advisor to work directly with the Acting Governor. The TOR was approved by the PMA and by the USAID.

VI. Impediments to Progress

Middle management has changed frequently in the past two years, as outlined in the Background section above. Program's success depends on trust and rapport between advisors and counterparts. Middle management and /or counterpart frequent turnover leads to lack of continuity and constant need to reestablish trust and rapport.

There has been no progress on the development of a Bank Supervision Strategic Plan. In addition, Cross-Border Supervisory Agreements, which would set the framework for cooperation between the PMA and foreign bank supervisors, were prepared by the Barents Group senior policy advisor in 1999 but have not been implemented.

Senior PMA managers and bank supervision middle management are prohibiting the participation of Barents Group technical advisors during 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. However, the PMA has now given Barents Group advisors access to bank information and is requiring examiners-in-charge and other staff to discuss all aspects of supervisory activity with the advisors. The advisors

have been actively involved in the preparation of the scope of examination, analysis of examination findings, and in preparation of the content and format of the report of examination. In addition, supervision staff has begun to employ CAMELS and CAEL ratings as a means to measure the level of risk in banks.

Several impediments to progress were identified during the Call Report development process and remain in place. The most serious is a lack of a 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 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. Development of the Call Report was completed and schedules together with full line instructions were distributed to the banks. In addition, the PMA has held consultations with the banks regarding the new regulations prepared in cooperation with the advisors on Classification of Problem Facilities, Provisioning Requirements, and Admissible Collateral. PMA senior management has begun to implement one of the regulations during second quarter of 2001.

Beginning in September 2000, 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 traveled regularly to the PMA office and have proceeded successfully with implementation of the Call Report, early warning system, on-the-job training, and the manuals, 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. Regardless, counterpart buy-in has increased at nearly all levels. 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. Barents Group has noted in its experience with similar programs in several countries that counterpart buy-in significantly increases approximately two years from the beginning of full-time resident advisor presence.

VIII. Additional Tasks Delivered During the Quarter

None

IX. Role of Other Donor Organizations

During the second quarter of 2001, the Advisors met with Mr. Karim A. Nashashibi, a senior advisor at the IMF, to discuss progress to date and the increased cooperation between the IMF and Barents Group advisors in strengthening the PMA supervisory capacity.