HARMONIZATION OF THE TURKISH DEPOSIT INSURANCE SYSTEM WITH THE EU DIRECTIVE*

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Abstract:

The core objective of this article is to evaluate the harmonization level of the Turkish deposit insurance system with the EU Directive. Moreover, the article presents a brief historical framework and the existing structure of the deposit insurance system in Turkey. The results indicate that although the Turkish system has achieved a high level of harmonization with the EU Directive, it will require one major adjustment about the reimbursement period for the insured deposits in order to comply with the current EU Directive. Furthermore, this article argues the need for updating the 1994 EU Directive on deposit insurance. In particular, the coverage limit for deposit insurance needs to be reconsidered and revised. Finally, the organizational structure and funding of the system requires standardization across the EU.

Keywords: *Deposit Insurance, Turkish Deposit Insurance System, EU Deposit Insurance Directive, The Financial Service Sector.*

Özet:

Çalışma, Türkiye'deki Tasarruf Mevduat Sigorta Fonu'nun 94/19/EC Avrupa Parlementosu Konsey Direktifine gösterdiği uyum seviyesini incelemeyi hedeflemektedir. Türkiye'deki tasarruf mevduat sigorta sisteminin geçmiş ve mevcut uygulaması çalışmada kısaca anlatılmıştır.

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Çalışmanın sonuçları göstermiştir ki, Türkiye'deki sistem, AB Direktifiyle büyük ölçüde uyum içindedir. Bununla birlikte Türkiye'deki sistem için yapılması önerilen tek değişiklik, mevduat sigortası kapsamındaki mevduatların standart bir prosedür çerçevesinde sistematik olarak mevduat sahiplerine geri ödenmesi şeklindedir. Bu makale ayrıca 94/19/EC Avrupa Parlementosu Konsey Direktifinin revize edilmesini önermektedir. Özellikle, tasarruf mevduat sigortası kapsamındaki mevduat limiti tekrar gözden geçirilmeli ve revize edilmelidir. Son olarak, AB ülkeleri arasında tasarruf mevduat sigorta fonunun organizasyon yapısı ve finansmanıyla ilgili bir standart oluşturulması önerilmektedir.

Anahtar Kelimeler: *Mevduat Sigortası, Türk Mevduat Sigorta Sistemi, AB Mevduat Sigorta Yönerge, Finansal Hizmetler Sektörü.*

Introduction

The objectives of the European Union (EU) have become ever more complex compared to those at the time of its establishment in the 1950s. The integration process of the six countries[1], which was started as a common policy for only coal and steel industries in 1951, has turned into an economic and a monetary union. The expansion of EU from six to twenty five members verifies the need for new regulations and directives in order to develop the single integrated market.

Turkey has to adopt its national laws to EU acquis communautaire before becoming a full member. Turkey has been an associate member of EU since 1963 and a candidate since 1999. In December 2004, an important progress has been achieved in the membership process. EU approved that Turkey had fulfilled Copenhagen political criteria and negotiations for the full membership started in October 2005.

The financial service sector is one of the areas that the EU aims to establish as an integrated market. The basis of the banking policy of the EU is the mutual recognition principle.[2] As a result, all candidate countries are obliged to adopt all the EU banking directives before their full membership,

[1] Belgium, West Germany, France, Luxembourg, Italy and the Netherlands.

[2] A licensed credit institution has the right to operate and to provide services in any member country without any further legal requirements.

it would be essential for each candidate country to find out the mismatching issues in their system with the EU directives. This article will focus on the EU Directive on deposit insurance (the Directive 94/19/EC of 30 May 1994) and analyse the Turkish system from this perspective.

The purpose of this article is to identify the current harmonization level of the Turkish deposit insurance system with the EU Directive and to illustrate the parts that require revision. Another focus of this article is to identify neglected issues and the shortcomings of the EU Directive on deposit insurance. The article aims to find out whether a revision of the existing deposit insurance Directive would be useful since the continuous integration process of the EU is enforcing new requirements.

In the first section a brief review about the main objectives of deposit insurance will be explained. In the following section, a review of the fundamentals of the EU Directive on deposit insurance will be discussed. Furthermore, the Turkish system will be evaluated under this framework. In the third section other important issues, which the EU Directive fails to elaborate on will be mentioned. The final section presents conclusions.

Objectives of Deposit Insurance

By definition, a deposit insurance system is the guarantee given to the deposit holders in case of any bank failure. It was first introduced in the US, after several bank failures during 1929-1933, aiming to protect small deposit holders and to prevent systemic risk.[3] When the first ever deposit insurance system was introduced in the US in 1933, its coverage limit was set as $2,500. Thus, the protection of small depositors was one of the fundamental objectives of the deposit insurance system (Heffernan, 2005).

Deposit insurance has a social motive of protecting vulnerable people like widows and orphans. The regulators aim to protect them not only because they have poor standards of living but also they are unlikely to be able to understand information about their bank's risk. In general, small depositors lack the knowledge and the ability to evaluate the soundness of banks. Even if they possess such skills, the cost of obtaining the necessary data, makes the evaluation almost impossible. Since most of the governments and regulators are aware of the small depositors' weaknesses

[3] Systemic risk is the risk that a bank failure will cause a chain of events, leading to collapse of the banking system.

in information gathering and evaluation skills, many countries introduced deposit insurance systems, to maintain the trustworthiness of the banking system on the part of small deposit holders.

As banks are intermediaries between lenders and borrowers, their sound financial position is of great importance for economic stability. The purpose of deposit insurance system is not only to protect depositors from losing their deposits but also to prevent sudden and continuous withdrawals that can spread to the whole banking system. Bank failures can lead to serious financial stability problems since banks are the core intermediaries for currency circulation. The linkage among banks grows continuously as interbank loan markets and money transmission systems are becoming ever more complex. As a result, this makes the banking system more vulnerable to contagion effects as it increases the correlated risk of the banks.

Although deposit insurance systems are criticized for creating 'moral hazard'[4] in stable financial systems; in case of bank failures, their necessity and dispensability is accepted since the possible systemic crisis in many countries, such as Argentine, Chile and Turkey, are prevented with the help of deposit insurance schemes (Fry, 1995).

EU Directive on Deposit Insurance

The EU Directive on deposit guarantee schemes was accepted in 1994. The Directive is a framework for the completion of a single banking standard by harmonizing the member states' systems at minimums. The deposit insurance system as indicated in the EU Directive comprises of a scheme in each country to be governed by a national institution rather than a supranational system. The Directive can be summarized mainly under four headings.

Coverage Limit in the EU Directive

The minimum coverage limit introduced by the EU Directive is either €20,000 or 90% of the guaranteed amount. The EU Directive also gives the right to exercise co-insurance option. Thereby all depositors even the ones

[4] Moral hazard occurs, as deposit holders will have the tendency to ignore the risk but maximize returns as they are under the deposit insurance scheme. As a result, managers will engage in high risk businesses for higher returns as far as deposit insurance acts as a risk shield for depositors.

having less than €20,000 are exposed to lose their deposits up to 10%. Although the co-insurance option is a useful tool to increase the risk awareness of the depositors, the theoretical background of co-insurance percentage in the EU Directive is not clear.

Moreover the EU Directive does not clearly define what the coverage limit would be under unexpected circumstances such as, if two banks fail at a time. Although the intention is to apply the €20,000 per depositor per institution, the EU Directive is not clear about the issue as well.

Furthermore, it can be argued that setting a single coverage limit for all member countries may not be the best practiee especially if the countries' economic standards are very different. For instance, Luxembourg and Greece apply €20,000 as the deposit coverage limit although per capita GDP[5] in Luxembourg is three times higher than in Greece. For this reason, IMF suggests countries to apply a deposit insurance coverage limit equal to one to two times of their per capita GDP. Since the per capita GDP in Luxembourg is around €45,000, the €20,000 coverage limit may not be proper to protect all the small depositors in the country. On the other hand, €20,000 coverage limit is high for countries having lower levels of per capita GDP such as the case in most of the new member countries. In these countries, banking sector may lose competitiveness compared to the former members since premium payments are charged from the insured deposits. Therefore, with reference to IMF, it seems that a single deposit insurance limit for all EU countries does not seem as a good solution (Garcia, 1999). Besides, high level of coverage limit is not desirable as it distorts market discipline (Kunt-Demirguc& Huizanga, 1999).

The EU Directive on deposit insurance excludes interbank deposits, subordinated debt and money laundering transactions from the coverage. Moreover deposits by financial institutions, insurance undertakings, governmental authorities, pension funds, credit institutions management and other companies in the same group can be excluded or granted a lower level of deposit insurance coverage depending on the member states' decision. Additionally, member states have the right to exclude currencies other than € or currencies of the member states from the deposit insurance scheme. As a result, rather than a standardized deposit insurance system, a mixture of various applications arises within EU.

[5] Per capita GDP is purchasing power parity adjusted.

The Home-Host Country Branches

The EU Directive on deposit insurance is based on mutual recognition principle (Tison, 1999). Mutual recognition principle implies that a licensed credit institution from a member country can operate in all other member states without any additional requirement. Therefore, in the case of deposit insurance, home country's coverage limit is binding for the branches in other host member countries. However some limitations to the mutual recognition principal have been imposed to prevent competition regarding the different deposit insurance limits between credit institutions of member states. For instance, deposit coverage limit of a foreign branch in a host country cannot exceed the coverage limits of that host country's local banks. On the other hand, a foreign branch has the right to upgrade its coverage limit in a host country if its home country's coverage is lower than the host country's. Moreover, all branches established in the EU countries even though, their home country is not an EU member, must join the host country's deposit guarantee scheme. Since EU aims to achieve a single market, the borders between member countries should not be restrictive for the free movement of services. The home-host country principle of the EU Directive on deposit insurance is considered as a proper arrangement for the integration process.

Membership to the System in EU Directive

The EU Directive requires compulsory membership for the deposit guarantee scheme. However a member state has the right to exempt a credit institution from the deposit insurance coverage system if that intermediary ensures sufficient protection for its depositors. Under those circumstances, the deposit guarantee scheme should at least be equal to that of the country's deposit insurance system. Furthermore any bank that fails to meet its obligations regarding the deposit insurance scheme can be penalized or even excluded from the system. The excluded institution can continue to accept deposits if it generates an alternative guarantee scheme for its depositors. Most of the EU countries prefer to have a compulsory membership just like the EU Directive offered. Actually, some of the EU countries such as Germany and Italy have more than one deposit insurance system for different kind of banks. Since the EU Directive did not make any limitations about the number of the deposit insurance scheme, different countries have different applications.

Insured Deposit Payments in Case of Failure

The deposit insurance system has to pay the insured amount of deposits if the credit institution has failed to do so. Although the deposit insurance scheme must be in position to make the compensation payments within three months, the payment process can be extended up to twelve months under exceptional circumstances. The payment schedule suggested by the EU Directive cannot be evaluated as an ideal practice as far as the protection of vulnerable depositors is considered. A FDIC (Federal Deposit Insurance Corporation) survey reported that all of the EU countries that took part in the survey are actually paying back the insured deposits within three months. On the contrary, a World Bank study points out that the payment in some cases can be extended up to nine months. On the other hand, the US and some of the EU countries such as Germany and Italy are the good examples of immediate payers for insured deposits (Kaufman & Seelig, 2002).

Turkish Deposit Insurance System

Deposit insurance system has seventy-two years of background in Turkey. The initial insurance system, which was set up in 1933 (Deposits Protection Law 2243), was a protection for the reserve requirements in the Central Bank of Turkey (CBRT). In 1936, the deposit insurance system was introduced as a coverage limit of 40% per depositor for the savings deposits.

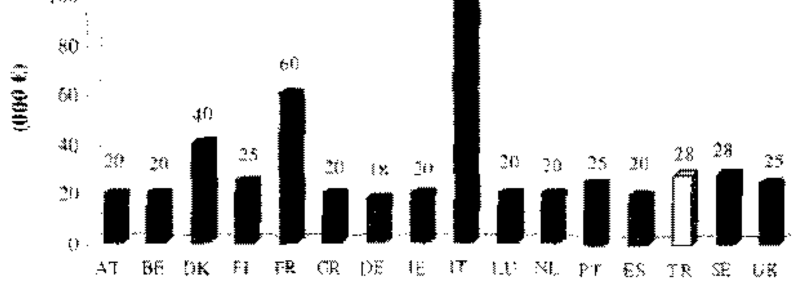
Even though the deposit insurance coverage limit was introduced in 1930s, the introduction of the premium system, which would fund the insured deposits, was not established until 1960. The establishment of the "Banks Liquidation Fund" and the premium payment system were both introduced in 1960 (Banks Act Nr 153). All banks automatically became members of the deposit insurance system.

The legal formation of the current deposit insurance system, 'Savings Deposit Insurance Fund' (SDIF) was introduced in 1983(Law on banks Nr 70). In the same year, the CBRT was chosen as the governor and the representative of the system. In 1994, the responsibility area of SDIF was widened. Aside from its funding function, SDIF was charged for restructuring and strengthening of the banking sector. The responsibility area of the SDIF is not only collecting premiums from banks but also overtaking the management of the banks, which can harm the soundness of the banking sector.

In 1999, important structural changes have been undertaken once more in the SDIF. Banking Regulation and Supervision Agency (BRSA) was established as a public legal entity and the representation of the SDIF was given to BRSA. The administrative and the representative body of the SDIF were changed from CBRT to BRSA. At the end of 2003, SDIF was separated from the BRSA and the board of the SDIF was charged as the decision making body of the fund (Altınok & Ilseven, 2004).

Coverage Limit in the Turkish System

The current deposit insurance coverage limit in Turkey, which is introduced in July 2004, is YTL 50 thousands (approx. €28,250) per account per institution. However for depositors having more than one account in an institution, the accounts are aggregated and considered as a single account. On the other hand, a person can have a full deposit insurance coverage as far as he/she splits his/her total deposit among banks, each account being equal to YTL 50 thousands. Although the coverage limit in Turkey is consistent to the EU standards, the coverage is high compared to the country's per capita GDP.



Deposit Insurance Coverage Limit in Turkey and in EU Countries[6]

[6] Denmark, Sweden, the UK and Turkey have limits in their local currencies, therefore the exchange rate movements increase or decrease their figure over time. Source: Worldbank

All saving accounts of natural people (native or foreign) in the form of YTL, gold and foreign currency are under the coverage of deposit insurance system in Turkey. Not only the interbank, subordinated debt or money-laundering transactions but also all other kind of deposits other than owned by natural people are not insured. The only difference between the EU Directive and the Turkish implication is the insurance provided for foreign currency accounts. The EU Directive gives right to exclude foreign currency savings from the coverage while the Turkish system includes all foreign currency deposits.

The basic framework of the Turkish deposit insurance system is as mentioned above, however, it has been observed that under certain circumstances, the actual practice varied significantly. As an example, even though deposit insurance system in Turkey is designed to pay only the insured amount of savings deposits, the recent banking crisis in Turkey was a totally different experience. The recent banking crisis was managed by the take-overs of the twenty-one troubled banks by SDIF from 1997 to 2003. Although the deposit insurance coverage was limited when most of those banks were failed[7], government announced to fulfil all domestic and foreign obligations of those banks. Total liability burden of those banks were $32 billion from which $26 billion was deposit accounts. Besides, total burden could be as low as $16.8 billion[8] if the deposit insurance in force has been executed (BRSA a, 2003).

As a consequence of bank failures, required cash to restructure and pay back all the liabilities of those banks was enormously higher than the annual premium payments of banks to SDIF[9] (SDIF b, 2004). The main source of SDIF became the borrowing from the treasury. SDIF used the debt not only to pay the deposits but also to restructure the financial situation of the undertaken banks. After strengthening the financial structure of the failed banks, the institution tried to organize mergers and acquisitions. If there was no chance for a merger or acquisition, the institution took control of the liquidation process.

[7] Full coverage for saving deposits was introduced in July 2003 just before Imarbank's license revocation.

[8] The figures exclude Imarbak case.

[9] SDIF annual income from premium payment is around $350 million.

The past experiences show that none of the depositors of the failed banks suffered losses in Turkey even though the deposit insurance coverage was limited at the time of failures. SDIF took over all deposit accounts and paid them by borrowing from treasury. As a result, all taxpayers in the country paid the liabilities of those failed banks. The depositors, who were reluctant to monitor the risk of those banks, have just enjoyed the higher levels of interest rates until the failures occurred. On the other hand all other domestic and foreign obligations of those banks were also repaid by SDIF (BRSA b, 2004). Probably the reason behind those payments regarding the foreign loans was to keep the trust of Turkish banking sector in the eye of foreign investors. This point of view has a basis when future borrowing of the existing banks is considered. However, full compensation of the deposit accounts is viewed as unfair on the part of taxpayers since the risk of the failed banks was already reflected in the high interest rates that they offered.

Home-Host Country Branches in Turkey

The Turkish deposit insurance system covers all local bank branches including foreign banks operating in Turkey. However none of the saving accounts in offshore branches of the Turkish banks or any offshore branches located in Turkey are under deposit coverage. Turkish system has nothing contrary to the EU Directive since the Directive also excludes deposits in offshore bank branches.

Membership to the System

In Turkey only banks and private finance houses[10] have the right to collect deposits. All banks are obliged to be a member to the deposit insurance system while private finance houses have their own deposit insurance system, which is also compulsory. The union of private finance houses is responsible to guarantee profit and loss accounts (deposits) with its guarantee fund. The Banking Regulation and Supervisory Agency monitors the private finance houses' system and the requirements for the private finance houses are the same as the banks' (UPFH).

[10]Private finance houses are operating in accordance with the Banking Law and the deposit accounts in those institutions are called profit and loss accounts. There are currently five private finance houses operating in Turkey and their deposit accounts are approximately 3 percent of the total deposits in Turkey.

Deposit Payments in Case of Failure

Deposit insurance system has to pay the insured amount of deposits if a bank fails. The payment schedule does not have a standard timing process and each failure is handled separately. In case of the latest bank failure, Imarbank, deposits are started to be paid six months after the licence of the bank abrogated. The deposit payments are handled by the deposit insurance system through a public bank. The deposits were announced to be repaid within a three and a half years period. The deposit accounts less or equal to €5,650 are paid six months after the liquidation process. Whereas the amount of deposits more than €5,650 are transformed into time deposits in the public bank and were scheduled to be paid at the end of their maturities. Moreover, the duration of the time deposits varies three months to three years depending on the size of the account (Ziraat, 2004).

Although the payment process of the Turkish system functioned slower than the EU average, it is believed that the high frequency of bank defaults and their considerable burden on the system was not easy to deal with in a shorter period.

The comparison of the two systems illustrates that the current Turkish deposit insurance system is quite compatible with the EU Directive. The main difference is the timing of payments in case of a failure. The EU Directive sets a time limit of up to twelve months for the payment process while in the Turkish system there is no predetermined payment schedule.

Neglected Issues about Deposit Insurance in the EU Directive

Since the EU Directive does not impose any requirements regarding the organizational and the financial structure of the deposit insurance system, various differentiated methods are implemented by the member countries. The objective of this section is to clarify whether an ideal organizational and financial structure exist for deposit insurers and to determine whether the EU Directive could be more prescriptive in this regard in order to foster a stable and efficient banking system in the EU.

Organizational Structure

The current EU Directive on deposit insurance does not clearly define the legal framework of the system. Each EU country is independent to administer the system by a legal entity of its choice either functioning under an existing authority (eg: Central Bank) or as a separate legal entity.

Many smaller countries prefer to exercise the deposit insurance function as a department of a central bank or a publicly owned supervisory authority (Garcia, 1999). The main advantage of a publicly owned scheme is the perception of guarantee associated with the state ownership (Gulyamov 2002). Additionally, having a deposit insurance system under an existing entity would save time and personnel expenses when controlling the bank activities.

On the other hand, functioning as a department of a central bank or a supervisory authority has serious disadvantages for the deposit insurance system as well. One of the main drawbacks is the conflicting objectives of the existing entity and its deposit insurance function. For instance, CB would prefer to provide liquidity to a troubled bank as a lender of last resort and at the same time prefer to pay all insured deposits and liquidate the bank under its deposit insurance function. In other words, an existing public entity may have difficulties in balancing its deposit insurance function with its existing responsibilities (FDIC).

The other alternative on the contrary is to design the deposit insurance system as a separate legal entity. In this case, the management of the legal entity can either be public, private or joined. The separate legal entity usually has its board of directors to control the management of the system. In publicly managed systems, the board of directors is responsible to the legislature whereas in privately or jointly administered legal entities, the responsibility is both to the member institutions and to the legislature (FDIC). Establishing a separate legal entity not only eliminates the disadvantages arising as a result of the conflicting objectives but also mitigates the pressures that could harm the independency of the system.

In EU, organizational structure of the deposit insurance systems varies among countries. The deposit insurance system in the United Kingdom is an example of a separate legal entity, while in the Netherlands the system is directly administered by the central bank (BIS 1998).

The core criterion for the management of a deposit insurance system is its independence. A healthy functioning decision-making body should not be influenced through political or industrial pressures. A separate legal entity with an independent management seems as the common view for sound governance. However there is no consensus on the ownership of the separate legal entity. One view supports the publicly owned system as it considers the importance of the social protection, while the contrary view believes that banks should be capable of managing their own system (Faulend & Kraft, 2005). Meanwhile, the empirical study of Demirguc-Kunt and Huizinga (1999) shows that joint and privately managed entities have a positive effect on the market discipline. As a conclusion, establishment of a separate legal entity with private participation seems to be a suitable alternative for the harmonization of the EU countries' deposit insurance organizational structures.

Financing the System

Funding the deposit insurance system is another important issue that the current EU Directive does not elaborate on. Although the EU Directive enforced countries for a compulsory membership to the system, it was reluctant to specify the funding procedures. As a result, all EU countries acted separately in the formation of the funding process.

One of the key issues related with the financing is the establishment of a permanent fund, which is known as 'ex-ante funding'. Existence of a fund fastens the payment process in case of a failure. Additionally, self-sufficient funds will not cause any unexpected disbursement neither to banks nor to the governments. Another benefit of the ex-ante funding is the rising motivation of the banks to monitor the banking system since they are permanently paying premiums (Ketcha, 1999). Although most of the EU countries and Turkey implement ex-ante systems, some member countries like the Netherlands, Italy, Luxembourg and Austria have the 'ex-post system' (Faulend & Kraft, 2005). Under the ex-post system, banks are not obliged to pay any premiums until a failure occurs. Therefore ex-post systems are considered to be suitable for countries having stable banking systems. However even for stable banking systems, any unexpected bank failure can weaken the payment ability of the survival banks and may result inability to pay back the insured deposits. Moreover ex-post system cannot be regarded as fair since surviving banks are the source of finance most of the time and the failed bank does not contribute to the funding at all (BIS, 2001). Therefore it is believed that harmonizing the funding systems of the EU countries on an ex-ante basis and supporting them with ex-post system in case of severe failure would be the best practice.

Another critical issue regarding the financial structure of deposit insurance is the source of funding. The main source of a deposit insurance system is the premiums paid by the members. There are two premium payment methods namely flat and risk-related premiums. The flat rate is the simple method for assessing premium amounts in which all banks have standard contributions to the fund regardless of their risk profile. The risk related premium on the other hand, is more difficult to calculate but more precise as it considers the risk levels of the banks. Moreover, empirical evidence indicates that the risk-related premium is more effective to curb the moral hazard problem and to stimulate banks to monitor their risk position (Zadeh, Xie & Zoli, 2002). Although risk-related premiums are regulatory in general, in case of an economic downturn, riskier banks can be negatively affected as a result of their high levels of premium payments (Ketcha, 1999). However risk-related premium payments seems to be a fair solution since riskier banks may be in need of the contributed funds more than the others as their probability to default is higher.

Risk-related premium system is used in most of the EU countries and in Turkey. The EU countries have various risk related premiums where the average premium differs from 0.02% to 0.8% (Tison, 1999). The premium ratios in Turkey have minimum base ratio of 0.15% on insured amount of deposits was announced for all banks[11]. However, higher premiums up to 0.2% are applicable for the riskier banks depending on the bank's capital adequacy ratios. The base ratio is applicable for the banks that have capital adequacy ratio of 12% or higher. The banks that have 8%-12% capital adequacy ratio, pay a total of 0.17% premium. The rest of the banks having less than 8% capital adequacy ratio, are not only paying the base amount 0.15% but also paying additional 0.05% premium (BRSA c, 2004). The fundamental differences between member countries are the upper and the lower premium limits assigned for the banks and the methods for risk calculation. Therefore, combining the risk-related premium systems of the EU countries would be a further step for the standardization. In brief, the EU Directive would be more comprehensive if the harmonization of the funding standards for the deposit insurance is also achieved.

Conclusion

The main contribution of this article is the comparison of the Turkish deposit insurance system with the EU Deposit Insurance Directive. Arising

[11] Until 30.09.2004 premium amounts were calculated depending on total savings deposits rather than on the insured amount of the savings deposit.

from this analysis the article raises questions about the need for updating of the EU Directive itself.

This article identifies one major amendment required for the Turkish deposit insurance system to achieve harmonization with the EU Directive. The suggested improvement for the Turkish system is on reducing the reimbursement period for the insured deposits in case of a bank failure. Compared to the EU Directive, the Turkish system has an unpredictable length for the reimbursement period. The EU Directive stipulates that payouts to depositors must be made within three months, however extensions to this are permissible up to a maximum period of twelve months. The twelve months payment period is not acceptable since vulnerable depositors might have no access to banking facilities for long periods. Therefore it is argued that an ideal payment process would pay the insured deposits in less than one month whatever the exceptional circumstances might be.

As a conclusion, the revision in the reimbursement period will make the Turkish deposit insurance system as comprehensive as the EU Directive. The below table illustrates the current harmonization level of the Turkish system with the EU Directive.

STANDARDS	EU Directive	Turkey
Coverage	Min. € 20,000	YTL 50,000
Co-insurance	Optional up to 10%	NONE
Explicit	YES	YES
Membership	Compulsory	Compulsory
Average time to pay	Max 12 months	Not defined
Management	Not defined	LE[12], Public
Risk Adjusted Premium	Not defined	YES

Source: Nenovsky, N & Dimitrova, K (2003), SDIF and World Bank

A further suggestion regarding the Turkish deposit insurance system could be the reduction of the coverage limit to the level of the EU Directive.

[12] LE: Legal Entity

In fact, the EU Directive does not require any revision, as long as the coverage limit of a country is above the suggested amount. Nonetheless, it can be argued that the coverage limit in Turkey is considerably higher than the EU average, when per capita GDP of the country is taken into account.

With reference to the EU Directive on deposit insurance, it can be accepted that some updating is necessary. The harmonization level of the deposit insurance systems in the EU countries cannot be considered as successful since there are important differences in the fundamentals of their systems. It is argued that the EU Directive should have specific and guiding principles about the organizational structure and the funding of the system. These two main aspects are critical for a harmonized and competitive banking sector within the EU.

First of all, introduction of a separate legal entity for the management of deposit insurance systems might prevent the system from political or industrial pressures. Additionally, some degree of private ownership in the management would be useful for sustaining independence. The main step regarding the funding of the system is harmonizing the systems of the EU countries on an ex-ante basis. Establishment of a permanent fund will increase the trust for the system and also will shorten the reimbursement period in case of a failure. The other possible suggestion for the funding could be the introduction of a risk related premium payment system.

Finally, requiring the same coverage limit and insisting on a single minimum coverage standard for all member countries, cannot improve the harmonization level of the EU systems. Although the coverage limit used to be appropriate for the former twelve members, with the changing profile of the member countries, it also requires revision. Moreover, disregarding the revision of the coverage limit for years implies that the inflationary pressures and changing economic structure of the EU are not taken into consideration. Therefore, a review about the coverage limit would be useful for a strong and sound protection scheme. A possible suggestion might be to arrange a ratio for coverage limits depending on the each country's per capita GDP as Garcia used in her studies. As a conclusion, the dynamic structure of the EU banking sector requires changes in the EU Directives in order to achieve a competitive single market.

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