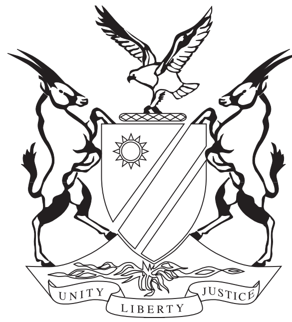

GOVERNMENT GAZETTE

OF THE

REPUBLIC OF NAMIBIA

N$8.00 WINDHOEK - 5 April 2024 No. 8339

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General Notice

BANK OF NAMIBIA

No. 154 2024

DETERMINATIONS UNDER THE BANKING INSTITUTIONS ACT, 2023:
ASSET CLASSIFICATION, SUSPENSION OF INTEREST
AND PROVISIONING

In my capacity as Governor of the Bank of Namibia (Bank) and under the powers vested in the Bank in terms of section 108(3) of the Banking Institutions Act, 2023 (Act No. 13 of 2023). I hereby issue the Determination on **Asset Classification, Suspension of Interest and Provisioning (BID-2).**

J. !GAWAXAB
GOVERNOR
BANK OF NAMIBIA Windhoek, 29 March 2024

BANK OF NAMIBIA

Determination No. BID-2

ASSET CLASSIFICATION, SUSPENSION OF INTEREST AND PROVISIONING

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PART I: PRELIMINARY

1. **Short Title** - Classification and provisioning.

2. **Authorisation** – Authority for the Bank to issue this Determination is provided in section 108(3) of the Banking Institutions Act, 2023 (Act No.13 of 2023).

3. **Application** – This Determination applies to all banking institutions authorised by the Bank to conduct banking business in Namibia.

4. **Definitions** - Terms used in this Determination are as defined in the Act, as further defined below, or as reasonably implied by contextual usage.

4.1 **"Act"** – means the Banking Institutions Act, 2023 (Act No. 13 of 2023).

4.2 **"Bank"** – means the Bank of Namibia as referred to in section 2 of the Bank of Namibia Act, 2020 (Act No. 1 of 2020).

4.3 **"Capitalised interest"** – means any accrued and uncollected interest which has been added to the principal amount of a loan at a payment date or at maturity; capitalised interest also includes unpaid interest which is refinanced or rolled-over into a new loan. For purposes of this Determination, capitalisation of interest will not be permitted **unless:**

(a) The borrower has the ability to repay the full debt (including principal and interest) in the normal course of business; or

(b) The capitalisation of interest was anticipated at approval of the initial loan based on the borrower's planned temporary lack of cash flow; or

(c) The debt is well-secured by the net realisable value of collateral security; or

(d) Repayment, including all capitalised interest, is based on a reasonably ascertainable future event.

For other loans or advances not having pre-established repayment schedules or where interest is normally capitalised to the account, deposits to the account during a temporary period of diminished cash flow must at least be sufficient to cover accrued interest for the period.

4.4 **"Concession"** – in relation to restructured and forborne exposures, the term refers to special contractual terms and conditions provided by a banking institution to a counterparty facing financial difficulties to make the counterparty able to service the debt.

4.5 "**Counterparty"** – means a natural or legal person to which a banking institution has an exposure of financial risk.

4.6 **"Default"** – a default is considered to have occurred regarding an obligor when one or both of the following events have taken place:

(a) The banking institution considers that the obligor is unlikely to pay their credit obligation to the banking institution in full, without recourse by the banking institution to actions such as realising security (if held); or

(b) The obligor is past due 90 days or more on material credit obligation to the banking institution. Overdraft facility will be considered as being past due once the customer has breached an advised limit for 90 days or has been advised of a limit smaller than current outstanding balance of the facility.

For retail exposures, the definition of default can be applied at the level of a facility, rather than at the level of obligor. As such, default by a borrower on one obligation does not require a banking institution to treat all other obligations to the banking institution as defaulted.

4.7 **"Exposure"** – for purpose of this Determination exposure refers to exposure as defined in the Banking Institutions Act, 2023 (Act No. 13 of 2023). Which includes loans, advances, and irrevocable commitments to lend, leasing, guarantees, any other form of finance; or any other exposure contemplated for the purpose of capital requirements under sections 39 and 40 of the aforementioned Act.

4.8 **"Forbearance"** – refers to a concession granted to a borrower for reasons of financial difficulty that would not be otherwise considered by the lender. Forbearance takes place when banking institutions grant their clients concessions in situations where the borrower is already facing repayment difficulties, or pre-emptively to loans still considered to be "performing" but for which repayment difficulties are anticipated. While the term forbearance is commonly used by regulators and supervisors, banking institutions may refer to these concessions as loan restructuring, rescheduling, or renegotiation.

4.9 **"Forborne/restructured loans and advances"** – refers to any loans and advances for which the banking institution has granted a concession to a borrower owing to deterioration in the borrower's financial condition. The forbearance/restructuring may include but is not limited to –

(a) A modification of the terms of the original structure of the loan(s) in order to relieve pressure on the borrower with the expectation that such concession will result in the full repayment of the new loan(s). For example, extension of maturity, changes in the schedule of payments, granting of grace periods, or changes in interest rates;

(b) Consolidation of all exposures from a borrower in a single suitable schedule, granting additional loans, releasing/lowering collateral, forgiving, deferring, or postponing principal, interest, and fees, as well as converting debt to equity, among others;

(c) Changes in the conditions of the existing contracts, giving considerably more favorable terms to the borrower;

(d) A supplementary agreement, or a new contract to refinance the current transaction;

(e) The substitution or addition of new debtor for the original borrower; or

(f) The exercise of clauses embedded in the contract that enable the borrower to change the terms and conditions of its contract or to take an additional loan, debt securities or off-balance sheet item at its own discretion. These actions should only be treated as concessions if the banking institution assesses and proves that the counterparty is in financial difficult.

All forborne loan agreements shall be formally documented and agreed with the client in writing.

4.10 **"In the process of collection"** – means that collection of an obligation is proceeding in due course in a timely manner either through:

(a) Legal action, including the enforcement of a judgement against the borrower; or

(b) Collection efforts not involving legal action, but which are reasonably expected to result in full repayment of the debt (including principal and all accrued interest), or in restoration of the debt to a current status through payment of all principal and interest which is due.

(c) In a timely manner shall mean, in the case of secured loans within three (3) years and in the case of unsecured loans within one (1) year.

4.11 **"Liquidation and/or recovery costs"** – refers to the cash outflows and expenses incurred during the collateral realisation process, and the sales process (also called recovery costs) and includes:

(a) All applicable legal costs;

(b) Selling costs, taxes, and other expenses;

(c) Any additional maintenance costs to be incurred by the banking institution in relation to the repossession and disposal of the collateral; and

(d) Any cash outflow up to the date of liquidation.

4.12 **"Loans and advances"** – means any direct or indirect advance of funds (including obligations as maker or endorser arising from discounting of commercial/business paper) which are made to a person on the basis of an obligation to repay the funds. "Loans and advances" also include all exposures as defined in the Act and this Determination.

4.13 **"Market value"** – in relation to loan collateral, refers to the estimated amount for which an asset or liability should be exchanged on the valuation date between a willing buyer and willing seller in an arm's length transaction after proper marketing and where the parties had each acted knowledgably, prudently and without compulsion.

4.14 **"Materiality Threshold of Credit Obligation Past Due"** – in relation to past due exposures, refers to an amount defined in relative or absolute terms of the original loan amount/exposures or an amount that has been past due for 90 days and more. The materiality threshold comprises two components, an absolute limit and a relative limit as follows:

(a) A limit in terms of the sum of all amounts past due owed by the obligor which is equal to an amount to be specified by the Bank.

(b) A limit in terms of the amount of the credit obligation past due in relation to the total amount of all on-balance sheet exposures to that obligor, excluding equity exposures, equal to a percentage to be specified by the Bank.

A default shall be deemed to have occurred when both limits outlined above are exceeded for more than 90 consecutive days.

4.15 **"Net realisable value"** – means that amount after discounting collateral held as security to current market conditions and deducting the reasonable and estimable costs of liquidation and/or recovery and sale in paragraph 4.11, including but not limited to: legal fees, valuation costs, estate agent fees, insurance cover to date of sale, costs of maintenance, security, and expenses necessary to put the collateral in a saleable condition.

4.16 **"Non-accrual"** – means that accrual of interest has been suspended and an asset has been placed on a cash basis for financial reporting purposes. Interest is no longer taken into income unless paid by the borrower in cash.

4.17 **"Non-performing"** – means that an asset is no longer generating income. For purposes of this Determination, the entire outstanding balance of an asset is considered "non-performing" when:

(a) Any portion of principal and/or interest is due and unpaid for 90 days or more; or

(b) Interest due for 90 days or more has been capitalised, re-financed, or rolled-over into a new loan.

Current accounts (overdrafts) are considered "non-performing" when any of the following conditions exist:

(a) The debt exceeds the approved limit for 90 consecutive days or more;

(b) The borrowing line has expired for 90 days or more;

Other loans and advances not having pre-established repayment schedules are considered "non-performing" when any of the following conditions exist:

(a) Interest is due and unpaid for 90 days or more; or

(b) The account has been inactive for 90 days, or deposits have been insufficient to cover the interest that was capitalised during the period.

The entire principal balance outstanding (not just the amount of payments in arrears) is to be shown as "non-performing" for purposes of this Determination and when preparing and submitting financial returns to the Bank.

4.18 **"Obligor"** – means any party that has a direct or indirect obligation under a contract. In terms of loans and advances, the obligor is the borrower who has the obligation to repay the loan.

4.19 **"Overdue" –** means any exposure for which:

(a) Any portion of principal and/or interest is due and unpaid for 30 days or more; or

(b) Interest due equal to 30 days interest or more have been capitalised, refinanced, or rolled-over.

Current accounts (overdrafts) are considered "overdue" when any of the conditions below exist:

(a) The debt exceeds the approved limit for 30 consecutive days or more;

(b) The borrowing line has expired for 30 days or more;

Other loans and advances not having pre-established repayment schedules are considered "overdue" when any of the conditions below exist:

(a) Interest is due and unpaid for 30 days or more; or

(b) The account has been inactive for 30 days, or deposits have been insufficient to cover the interest capitalised during the period.

The entire principal balance outstanding (not just the amount of payments in arrears is to be shown as "overdue" for purposes of this Determination and when preparing and submitting financial returns to the Bank.

4.20 **"Past due**" – means an exposure where any amount due under the contractual arrangement (interest, principal, fee, or other amount) has not been paid in full at the date when it was due. An exposure should be considered past due from the first day of missed payment, even when the amount of the exposure or the past-due amount, as applicable, is not considered material. Overdraft facility will be considered as being past due once the customer has breached an advised limit or been advised of a limit smaller than current outstanding. For purpose of this Determination, the commencement of past due exposure stage precedes that of an overdue exposure.

4.21 **"Provisions"** – means a balance sheet account established through charges to "provision expense" in the income statement and against which uncollectible assets, or portions thereof, are written-off. Also referred to as "provision for loan losses"; includes both "specific" and "general" provisions. The provision accounts are offset against loans for financial reporting purposes.

For purposes of this Determination, provisions set aside for loans graded Substandard, Doubtful, and Loss are considered "specific" provisions; provisions for loans graded Pass, Special Mention, are considered "general" provisions.

4.22 **"Technical Default"** – means a deficiency in the loan agreement that arises from a failure to uphold certain aspects of the loan terms other than the regularly scheduled payments, the following situations refers:

(a) The identification of default results from a data or system error of the banking institution, including manual errors in standardised processes but excluding wrong credit decisions;

(b) There is evidence that the identification of default results from failure of the payment system; and

(c) The required payment has been made by the obligor before the relevant days past due criterion, including the materiality threshold, has been breached but default has been identified as a result of long or prolonged payment allocation process within the banking institution.

4.23 **"Unlikely full payment"** – means a case or cases where an exposure's full repayment of principal and/or interest by the counterparty is unlikely without relying on the banking institution's realisation of collateral or other credit risk mitigating techniques, even when it is not past due or has been past due for less than 90 days. The likelihood of repayment may also be assessed through a comprehensive analysis of the financial situation of the counterparty using all input available such as (i) patterns of payment behaviour in past circumstances; (ii) new facts that change the counterparty's situation; and (iii) financial analysis. The indications of unlikely to pay include but not limited to the following:

(a) The banking institution put the credit obligation on non-accrual status;

(b) The banking institution makes a charge-off or account specific provisions resulting from a significant perceived decline in credit quality after the banking institution taking on exposure;

(c) The banking institution sell other credit obligations from the same counterparty at material credit related economic loss;

(d) The banking institution consent to a distressed restructuring of the credit obligation where this is likely to result in a diminished financial obligation caused by the material forgiveness, or postponement of principal, interest or (where relevant) fees;

(e) The banking institution has filed for the obligor's bankruptcy or a similar order in respect of the obligor's credit obligation to the banking group; and

(f) The obligor has sought or has been placed in bankruptcy or similar protection where this would avoid or delay payment of the credit obligation to the banking institution or banking group.

4.24 **"Well-secured"** – means that a loan or advance is secured by:

(a) Collateral that can repay the full debt (principal plus accrued interest) through timely sale under an involuntary liquidation program; also, (i) proper legal documentation must be held, (ii) the collateral must have a "net realisable value" which covers principal, accrued interest, and costs of collection, and (iii) there can be no prior liens which prevent the banking institution from obtaining clear title; or

(b) A guarantee from a financially responsible party where the beneficiary banking institution has performed proper financial analysis and determined that the guarantor is financially sound, well-capitalised, and able to honour the guarantee on demand; such guarantees must be (i) affirmed, (ii) irrevocable and unconditional, and (iii) payable on default of the borrower.

PART II: STATEMENT OF POLICY

5. **Purpose** – This Determination is intended to ensure that: (a) all loans and advances are regularly evaluated using an objective grading system that is consistent with regulatory standards; (b) the accounting treatment for accrued but uncollected interest on non-performing assets is consistent with international accounting standards and regulatory reporting requirements; (c) timely and appropriate provisions and write-offs are made to the loan loss provisions account in order to accurately reflect the condition and operations of the banking institution; (d) the interaction of forbearance exposures and non-performing exposures is clear. The Determination is also intended to promote well-reasoned, effective work-out plans for problem assets, and effective internal controls to manage the level of such assets.

6. **Scope** – This Determination apply to all loans and advances reflected on a banking institution's balance sheet or otherwise reflected as off-balance sheet items.

7. **Responsibility** – The board of directors of each banking institution must be responsible for adopting a written loan policy that includes a loan review process which accurately identifies risk, ensures the adequacy of provisions for loan losses, and properly reflects the condition and operations of the banking institution in required financial statements.

PART III: IMPLEMENTATION AND SPECIFIC REQUIREMENTS

8. **Loan Review**

(a) Frequency and reporting

The board of directors of a banking institution must cause a review to be made of the quality of a banking institution's loan book on a quarterly basis, at least at the end of each calendar quarter. Reports of such reviews must be made on a timely basis directly to the board of directors and must include enough information for the board to identify problems and require bank officers to correct the problems in a timely manner.

The frequency of reporting and reviews of a specific loan or group of loans may be enhanced or increased as and when reviewers detect significant increases in the credit risk of a specific loan or group of loans, caused by factors that are of a micro and or macro nature, that will negatively impact the performance of the loans.

(b) Objectives

The loan review function must ensure that: (i) the loan portfolio and lending function conform to a sound, written lending policy which has been adopted and approved by the board of directors; (ii) executive management and the board of directors are adequately informed regarding portfolio risk; (iii) problem credits are promptly identified, classified, and placed on non-accrual in accordance with this Determination; (iv) fully adequate provisions are made to the loan loss provisions account; and (v) write-offs of identified losses are taken in a timely manner.

(c) Board Committee

The loan review function must be performed by a committee of not less than three persons. The committee must be composed of persons who have been duly vetted and appointed by the Bank as directors in terms of section 53 of the Act and are not executive directors or substantial shareholders of the banking institution. The committee must meet at least four times per year or more regularly.

The committee shall assist the board of directors in fulfilling its responsibilities by providing oversight of the banking institution's policies and management activities relating to the identification, assessment, measurement, monitoring, and management of credit risk. Broadly, the responsibilities of the committee include but are not limited to:

(i) Review the credit risk management framework, practices, and programs for managing credit risk, and material changes to credit policies;

(ii) Monitor concentrations and limits of credit risk, and ensure they are within the risk appetite and tolerance of the banking institution;

(iii) Monitor the performance and quality of the loan portfolio;

(iv) Review and approve credit applications which have been submitted to the committee for consideration;

(v) Review non-performing loans, collateral, and the adequacy of loan loss provisioning in terms of this Determination;

(vi) Review the write-off of impaired loans and advances in terms of this Determination; and

(vii) Document and maintain records of proceedings and make regular reports to the board regarding matters reviewed and actions taken at each committee meeting.

9. <u>Suspension of Interest</u>

(a) Transfer to non-accrual status

A loan or advance is to be placed on non-accrual if: (i) it is maintained on a cash basis because of deterioration in the financial condition or paying ability of the borrower; (ii) payment in full of principal or interest is not expected; or (iii) it is non-performing unless it is <u>both</u> well-secured <u>and</u> in the process of collection.

However, banking institutions must still classify non-performing loans in line with paragraph 11 of this Determination regardless of whether the loan is well secured or is in the process of collection.

(b) Treatment of accrued interest

All interest which is accrued but is uncollected and still carried on the books must be reversed by the end of the calendar quarter in which the loan is, or should have been, placed on non-accrual status, but in no event later than 90 days after being transferred to non-accrual status or included in the loan balance with an adequate specific provision to offset the full amount which was previously accrued.

Interest which has already been taken into income and capitalised by increasing the principal amount of the loan must be reversed or written-off from the time the loan is, or should have been, placed in non-accrual status.

(c) Treatment of cash payments, and criteria for cash basis recognition of income

If a loan is on non-accrual and ultimate collection of the entire principal amount is in doubt, then any cash payments received must be applied only to reduce principal. However, if the balance left on the books after a partial write-off of principal is considered fully collectible, then cash payments may be shown as interest income.

When recognition of interest income on a cash basis is appropriate, the amount of income that may be shown is limited to the amount that would have been accrued on the book balance at the contractual rate. Any cash payments in excess of this amount (and not applied to the remaining book balance) must be recorded as recoveries of prior write-offs until all such write-offs have been fully recovered.

In order to claim that a loan is fully recoverable, it must be supported by a current, properly documented credit analysis, including evaluation of the borrower's historical repayment performance and any other relevant factors.

(d) Reclassification to accrual status

A non-accrual loan may only be reclassified to accrual status or performing status when all the following criteria are simultaneously met:

(i) No amount of principal or interest is overdue, and the full repayment of the exposure is likely, according to the original or, when applicable, modified conditions; or

(ii) When it becomes both well-secured and in the process of collection.

For purposes of (i) above, the bank must have received repayment in cash of all delinquent principal and interest unless the loan has been formally restructured and qualifies for accrual status. Until a loan is reclassified to accrual status, cash payments received shall be handled as required in paragraph (c) above. In addition, if a restructured/forborne loan deteriorates and qualifies again for non-accrual status, then the loan must be returned to non-accrual status and treated accordingly.

(e) Treatment of multiple loans to one borrower

If a banking institution has multiple loans to a single borrower, and one loan meets the criteria for placing on non-accrual status, then the banking institution must evaluate every other loan to that borrower and place other loans on non-accrual status if circumstances so require.

10. <u>Loan Forbearance</u>

(a) Before granting any forbearance measures, banking institutions must conduct acomplete assessment of the borrower's financial situation. This includes the assessment of all relevant factors, taking particular account of the debt servicing capacity and overall indebtedness of the borrower. This assessment must be based on documented current and verified financial information. There must be an assessment that the borrower will be able to meet the revised payment schedule (i.e., taking into consideration the concessions that have been granted) and unlikely to pay criteria.

(b) Forbearance measures must not be used to postpone the recognition of inevitable losses. Forbearance must therefore only be considered for borrowers that are cooperative and that are distressed but potentially viable. A forbearance solution must only be considered viable when:

(i) The banking institution can demonstrate (based on documented financial information) that the borrower can realistically afford the forbearance solution;

(ii) The resolution of outstanding arrears is fully addressed and a significant reduction in the borrower's balance in the medium (6-12 months) to long (more than 12 months) term is expected; and

(iii) The solution does not result in consecutive forbearance measures having been granted to the same exposure.

(c) The performance of the forborne borrower(s) should be closely and continuously monitored during the probation period.

10.1 Interaction of forbearance exposures with non-performing exposures

(a) Forborne exposures can be performing or non-performing. When granting forbear ance measures to performing exposure, banking institutions must assess whether these measures lead to a need to reclassify the exposure as non-performing. However, granting forbearance measures to non-performing exposures does not automatically clear their non-performing status. The exposure must continue to be identified as non-performing for at least the probation period;

(b) Banking institutions must pay attention to the appropriate categorisation of exposure(s) on which forbearance has been granted more than once. When a forborne exposure under the probation period is granted new forbearance, this should trigger a re-start of the probation period, and banks should consider whether the exposure should be categorised as non-performing; and

(c) The continuous repayment period for non-performing exposure and the probation period for forbearance can run concurrently.

10.2 Probational Period

(a) The probation regime shall consist of continuous and timely payment of principal and interest, the absence of other impaired or defaulted exposures, as well as the existence of no concerns regarding the borrower's ability to pay the forborne loan in full.

(b) The probation period or the agreed new continuous payment term for forborne/restructured exposures must not be less than six (6) months.

(c) When a forborne exposure becomes non-performing during the arranged probation period, the probation period starts again. In this case, a banking institution must undertake a fresh review of the financial condition of the borrower to determine the viability of the second forbearance solution prior to the actual granting of the second chance.

(d) The starting date of the probation period must be the scheduled start of payments under the revised term, regardless of the performing or non-performing status of the exposures at the time that forbearance was granted.

10.3 Exit Criteria

(a) Exposure will be removed from the forborne category when the borrower has satisfied all the following requirements:

(i) When all payments, as per the revised contractual terms, have been made in a timely manner over a continuous repayment period of six (6) consecutive months (probation period for reporting);

(ii) The borrower has resolved its financial difficulty; and

(iii) The exposure meets the exit criteria for discontinuation of the impairment and default classification.

(b) If any new forbearance measures are granted to a borrower within a six (6) months period after exiting the forborne category, this will require the reclassification of these exposures to the non-performing category. The same will apply when these exposures become more than thirty (30) days past-due.

11. Classification of Loans[1]

(a) All loans and other assets must be classified into one of the five (5) classification grades listed below based on the criteria provided. A banking institution may choose to use other classification groups for internal use, as long as they can be correlated to the regulatory grades. (A sample loan classification (grading) matrix is provided for reference as **Appendix A**).

(b) Significant departure from the primary repayment source may justify adverse classification even when a loan is current or supported by apparent collateral value. Classification may also be warranted if the original repayment terms were too liberal or if a delinquency has been technically cured by modification of terms, refinancing, or additional advances.

(c) In cases where different classification grades may be assigned based on the subjective criteria in **Appendix B**, the more severe classification generally must apply. Moreover, nothing contained in the definitions below precludes assigning a more severe grade when analysis of a borrower's financial condition, ability, and willingness to repay justifies the more severe grade.

11.1 Classification Categories

The classification categories are to be viewed as groupings or buckets within which certain actions are required. Each time band or classification category requires settlement in full of

[1] A bank may have an asset classification system that differs from the framework used or suggested by the Bank. However, each bank that maintains an assets classification system that differs from the Bank's should maintain documentation that translates its assets classification into pass, special mention, substandard, doubtful and loss. This documentation should be sufficient to enable Bank Examiners to reconcile the totals for various loan grades under the bank's system to the Bank categories listed under paragraph 11 of this Determination.

all due and unpaid principal and/or interest before reclassification to a lesser time band or classification category can occur.

Table 1: Loan Classification Categories

Performing		Non-Performing		
Pass/Acceptable	Special Mention	Substandard	Doubtful	Loss
0 - 59 days	60 - 89 days	90 - 179 days	180 - 359 days	360 + days

(a) Pass or Acceptable

Loans, or other assets, in this category are fully protected by the current sound worth and paying capacity of the obligor or the collateral pledged, is performing in accordance with contractual terms, and is expected to continue doing so.

(b) Special Mention

Loans, or other assets, in this category are currently protected, but exhibit potential weaknesses which, if not corrected, may weaken the asset or the bank's position at some future date. Examples of such weaknesses include but are not limited to: inability to properly supervise due to an inadequate loan agreement; deteriorating condition or control of collateral; deteriorating economic conditions or adverse trends in the obligor's financial position which may, if not checked, jeopardise repayment capacity. Risk potential is greater than when the loan was originally granted; but this category must not be used as a compromise between Pass and Substandard.

Any asset which is overdue for 60 days or more, but less than 90 days must be classified as Special Mention, at a minimum.

(c) Substandard

Loans, or other assets, in this category are not adequately protected by the current sound worth and paying capacity of the obligor. The primary source(s) of repayment is not enough to service the debt, and the banking institution must look to secondary sources such as collateral, sale of fixed assets, refinancing, or additional capital injections for repayment. Substandard assets have well-defined weaknesses that jeopardise the orderly repayment of the debt. These assets may, or may not, be overdue but carry more than a normal degree of risk due to the absence of current and satisfactory financial information or inadequate collateral documentation. There is also the distinct possibility that the bank will sustain some loss if the deficiencies are not corrected.

Any asset which is overdue 90 days or more but less than 180 days must be classified as Substandard at a minimum.

(d) Doubtful

Loans, or other assets, in this category have all the weaknesses inherent in a Substandard asset plus the added characteristic that the asset is not well-secured. These weaknesses make collection in full, on the basis of currently existing facts, conditions, and value, highly questionable and improbable. The possibility of loss is high, but because of important and reasonably specific pending factors which may mitigate, the actual amount of loss cannot be fully determined. Pending factors may include a proposed merger, acquisition, or liquidation, a capital injection, perfecting liens on additional collateral, and refinancing plans. If pending events do not occur within 180 days and repayment must again be deferred pending further developments, a Loss classification is warranted.

Any asset which is overdue 180 days or more, but less than 360 days must be classified as Doubtful at a minimum. Guarantees must be honoured within 90 days of call to preclude a Doubtful classification.

(e) Loss

Loans, or other assets, which are considered uncollectible must be classified Loss. Loss classification does not mean there is no recovery or salvage value; rather it is not practical or appropriate to defer writing off the asset even though partial recovery may be realised in the future. Losses shall be taken when identified as uncollectible and shall not remain on the books while pursuing long-term recovery efforts.

In some cases, a reduced carrying value for a distressed asset may require a partial write-down. Partial write-downs must be made by a charge to the provision for loan losses account, and the remaining book value must be supported by tangible facts and reported in writing to the board of directors**.**

Any asset which is overdue 360 days or more must be classified as Loss.

11.2 Classification of Forborne Loans and Advances

(a) Performing loans granted forbearance measures must, at a minimum, be classified in the category of special mention in terms of this Determination. If the loans were already classified as non-performing i.e. "Substandard", "Doubtful" or "Loss", then the loan shall retain the same classification and provisioning status.

(b) Banking institutions must not use forbearance measures to influence or delay the past due or non-performing classification of loans, as such forbearance measures do not reset the number of payments outstanding or period of arrears to zero. Therefore, if forbearance is granted to any loan which would have otherwise become non-preforming if not for the concession granted, such a loan must, at a minimum, be classified in the "Substandard" category.

(c) Loans benefitting from forbearance measures must maintain their original classification and continue to be classified "Special Mention", "Substandard", "Doubtful" or "Loss" as the case may be unless both of the following conditions have been met:

(i) All overdue amounts (principal, interest, fees, and other charges) are paid up in cash at the time of reclassifying the account to a better classification (i.e., "Pass"); and

(ii) Loans have maintained a sustained record of performance according to the modified repayment program of no less than six (6) consecutive months.

11.3 Non-reclassification Criteria

(a) The following situations will not lead to the reclassification of a non-performing loan as performing:

(i) Partial write-off of an existing non-performing exposure, (i.e. when a banking institution writes off part of a non-performing exposure that it deems to be uncollectible);

(ii) Repossession of collateral on a non-performing exposure, until the collateral

is disposed of and the banking institution realises the proceed (when the exposure is kept on the balance sheet, it is deemed non-performing); or

(iii) Extension or granting of forbearance measures to an exposure that is already identified as non-performing subject to the relevant existing criteria for non-performing exposures.

11.4 Write-off of Loans

(a) Any loan/advance which is unsecured, and which is overdue for three hundred and sixty (360) days, or more must be classified as "Loss" and must be written-off within one (1) year after being classified as a "Loss" against the provision for loan losses.

(b) Any loan/advance which is secured, and which is overdue for three hundred and sixty (360) days, or more must be classified as a "Loss" and must be written off within three (3) years after being classified as a "Loss" against the provision for loan losses account unless such loan is:

(i) well secured; and

(ii) in the process of collection; and

(iii) judgement has been received, and the time needed to realise the collateral does not exceed three (3) years after judgment.

(c) Where judgement is passed in a competent court regarding a loan that has been classified as "Loss", and the conditions mentioned under this section have been satisfied, a period of three (3) years will be allowed for recovery to be completed, failing to recover the loan will then require the banking institutions to write off the loan. With pertinence to an estate being administered or the liquidation of a commercial entity, once judgment has been obtained, the period of recovery may be extended from three (3) years to five (5) years, failing which the loan must be written off.

(d) Loan write-offs must include all interest that is accrued but unpaid. Current period interest which has accrued but is uncollected must be reversed from the income account. Prior period accrued interest which has already been taken into income must be written-off.

12. <u>Provisioning Requirements</u>

12.1 Provisions for loan losses account

(a) All banking institutions must maintain a provision for loan losses account which must include both specific and general provisions. The provisions account shall be created by charges to provision expense in the income statement and must be maintained at a level that is adequate to absorb potential losses in the loan/assets portfolio.

(b) At the end of each calendar quarter, or more frequently if warranted, the board of directors shall cause management to evaluate the collectability of all loans, including any accrued and unpaid interest, and shall require that appropriate entries be made to (i) accurately report earnings, and (ii) ensure that the provision for loan losses account is fully adequate to absorb potential losses. The evaluation of the appropriate level of provision should be performed in a systematic way and in a consistent manner over time. Management must maintain records to support their evaluations and shall make them available for inspection by examiners as requested.

12.2 Provisioning amounts

(a) In determining the potential loss in specific loans, groups of loans, or in the aggregate loan portfolio, all relevant factors shall be considered including, but not limited to: current economic conditions, historical loss experience, delinquency trends, the effectiveness of the banking institution's lending policies and collection procedures, and the timeliness and accuracy of its loan review function.

(b) The following minimum provisioning amounts are to be maintained unless reliable data suggests that loss potential is higher and thus larger provisions are warranted.

(i) for loans graded **"Pass"** or **"Acceptable"**	1%
(ii) for loans graded **"Watch"** or **"Special Mention"**	2%
(iii) for loans graded **"Substandard"**	10%
(iv) for loans graded **"Doubtful"**	50%
(v) for loans graded **"Loss"**	100%

(c) The above percentages shall be applied against the total outstanding balance regardless of whether the loan is analysed separately or as part of a pool of loans. Provisions must be determined on the basis of the short-term (12 months) realisable value for collateral or a conservative present value estimate of the borrower's likely repayments, not on longer-term (more than 12 months), potentially optimistic projections of future value. Collateral must be treated as provided in paragraph 14. Suspended interest, if any, must be deducted first.

(d) Any loan, or portion thereof, which is fully secured by cash, by a segregated deposit in the lending bank, by security issued by the Government of Namibia, or by an explicit unconditional obligation or guarantee by the Government of Namibia to repay both principal and interest, is exempt from the provisioning amounts.

(e) Any loan, or portion thereof, which is, or should be, classified as "Loss" may be fully provisioned when the classification is, or should have been, assigned and shall be written off at the end of the quarter but not later than one (1) year for unsecured loans and three (3) years for secured loans after being classified Loss subject to the conditions in paragraph 11.4.

12.3 Treatment of differences between International Financial Reporting Standards (IFRS) and regulatory provisions

(a) Banking institutions are required to calculate their provisions (impairments) in accordance with the requirements of both the IFRS accounting standards and this Determination.

(b) Banking institutions that have implemented the IFRS accounting standard are required to compare the amount of provisions (specific and general) computed in terms of the IFRS accounting standards, with the amount of provisions computed in terms of this Determination. The higher of the two provisioning amounts must be considered as being the minimum regulatory provision amount required for compliance and reporting purposes.

(c) Should the IFRS accounting provision amount be less than the regulatory general provisions, an additional general credit-risk reserve (GCRR), on a pre-tax basis equal to or exceeding the shortfall, must immediately be created through an appropriation of distributable reserves to eliminate the shortfall.

12.4 Regulatory treatment of the International Financial Reporting Standards (IFRS) accounting provisions

(a) For regulatory capital purposes, the IFRS accounting provisions shall be calculated utilising models to be developed by individual banking institutions (model-based) and shall be classified as either general provisions (GP) or specific provisions (SP) as follows:

(i) Loans and advance for which the banking institution determines that at the reporting date, there has been no significant increase in credit risk since initial recognition (i.e. Stage 1 exposures in line with the requirements of IFRS), the associated accounting provisions must be treated as general provisions;

(ii) Loans and advances for which the banking institution determines that at the reporting date, there has been a significant increase in credit risk since the initial recognition, but that they are not credit impaired (i.e. Stage 2 exposures in line with the requirement of IFRS), the associated accounting provisions must be treated as general provisions; and

(iii) Loan and advance for which the banking institution determines that at the reporting date, they are credit impaired (Stage 3 exposures in line with IFRS), the associated accounting provisions must be treated as specific provisions.

12.5 Supervisory review

(a) The management shall maintain adequate records supporting its evaluation of potential loan losses and the entries made to ensure adequacy of the provision for loan losses account. Such records must be available for supervisors to assess management's loss estimation procedures, the reliability of the information on which estimates are based, and the adequacy of the provision for loan losses account. If the provision for loan losses account is determined to be inadequate by more than +5%, adjusting entries will be required.

(b) Banking institutions must, upon request, furnish the records and documentation pertaining to the classification and provision for loan losses in a timely manner and ensure the integrity of the records and documentation submitted to the Bank.

13. <u>Non-performing Loans</u>

13.1 Non-performing loan strategy

(a) Banking institutions must develop a non-performing loans (NPL) strategy to establish strategic objectives for timely recovery and reduction of high NPLs. The NPL strategy must lay out the banking intuitions' approach and objectives for the effective management and ultimate reduction of NPLs, including setting targets in terms of operational capabilities (qualitative) and projected NPL reductions (quantitative) in the short, medium, and long term.

(b) The NPL strategy must encompass, at a minimum:

(i) Time-bound quantitative NPL targets supported by a comprehensive operational plan; and

(ii) Must be based on assessment and analysis of NPL strategy implementation options in terms of internal capabilities, external conditions, and capital implications; and

(iii) Must be approved by the board of directors and reviewed at least annually.

(c) Banking institutions with high NPL levels should report their NPL strategy to the Bank on an annual basis, summarising the quantitative targets and the level of progress made in the past one (1) year against the plan. The board of directors should approve the reporting prior to submission to the Bank.

13.2 Non-performing loan governance

(a) In terms of the non-performing loan (NPL) strategy development and implementation, the board of directors of the banking institutions must:

(i) Approve annually and regularly review the NPL strategy and implementation plan;

(ii) Oversee the implementation of the NPL strategy;

(iii) Periodically, at least quarterly, monitor progress made in comparison with targets and milestones in the NPL strategy;

(iv) Define an adequate approval process for the recovery of large NPL exposures;

(v) Approve NPL related policies and ensure that they are embedded in the credit management process; and

(vi) Ensure sufficient internal controls over the NPL management process, focusing on activities related to NPL classification, provisioning, collateral valuation, and forbearance measures.

14. Collateral

(a) Banking institutions may utilise collateral and guarantees, among other instruments, to help mitigate credit risks. Banking institutions must have in place documented policies and/or guidelines for the treatment and valuation of collateral, which must be approved by the board of directors.

(b) Banking institutions must define criteria in their collateral valuation policies and procedures for determining that a significant decline in collateral value has taken place.

14.1 Treatment of Collateral

(a) Collateral is a secondary source of repayment, and classification grades do not depend on the amount or quality of collateral pledged. Therefore, collateral is only used in determining the amount of provision for loans graded Substandard, Doubtful or Loss. This is especially true where the validity, value, and ability to realise collateral are questionable.

(b) For loans graded Substandard, Doubtful or Loss, the net realisable value of collateral shall be deducted from the loan balance before applying the provisioning percentages. In the case of real property collateral, the net realisable value may be deducted only if transferability of title is certain and an active market for the property exists. An "active market" means that a willing buyer and willing seller exist, and a sale can be achieved within a reasonable period (not exceeding three (3) years after judgment or five (5) year after judgement in the case of estate being administered or the liquidation of a commercial entity).

(c) At the time an asset is classified as Substandard, a banking institution when determining the net realisable value of collateral must consider an adequate collateral haircut based on the banking institutions experience and relevant external factors. To further mitigate the risk of the loss of value to collateral for the duration the asset will remain in non-performing loan category and on the books of the banking institution, i.e., the recovery period, the banking institution must apply model-based haircuts in accordance with the International Financial Reporting Standards (IFRS) classification and provisioning models.

(d) When accepting guarantees for credit facilities, banking institutions must evaluate the level of coverage being provided in relation to the credit quality, legal capacity, and strength of the guarantor. The institution must differentiate between explicit guarantees and implicit ones (e.g. anticipated support from the Government). If implicit guarantees are taken into account, they must be adequately justified. The banking institutions must ensure the enforceability of guaranteed agreements.

14.2 Valuation of collateral

(a) Valuation should be based on the net realizable value of the collateral and should not be biased in order to enable the banking institution to grant a higher credit limit to the borrower or improve its internal credit rating, make a smaller amount of provision, or continue interest accrual for a problem loan.

(b) Banking institutions should ensure that the valuation method used, whether internal or external, is based on assumptions that are both reasonable and prudent and all assumptions should be clearly documented.

(c) To cater for collateral, whose market value is highly volatile, banking institutions should apply a conservative haircut[2] when valuing it for the purpose of determining the extent to which an exposure is secured. The quantum of that haircut will depend on the price volatility of the collateral, the term of the exposure and whether the collateral is denominated in a different currency to the underlying debt. Banking institutions must maintain documentation detailing the collateral haircuts applied and the rationale thereto.

(d) A more conservative approach must be adopted for valuing the collateral of problem loans. This is because, in practice, the forced sale value, rather than the open market value, is likely to be closer to what eventually may be realised from an asset sale when the market conditions are unfavorable. Therefore, a discount to the estimate market value must be applied where appropriate.

(e) In assessing the value of an asset, temporary aberrations should be disregarded (e.g. a sudden rebound in the market price).

[2] Haircut (i.e. discount the value of the collateral)

14.3 Frequency of revaluation

(a) The value of collateral must be revalued and updated on a regular basis, though the frequency may vary with the type of collateral involved and the nature and the internal credit rating of the underlying credit.

(b) The frequency of valuation must be carried out on (i) a less-frequency basis for exposures classified pass or special mention and on (ii) a more frequency basis for exposures classified substandard, doubtful and loss categories in response to the deterioration of credit quality and financial conditions of the counterparty, as demonstrated in the table below.

Table: 1 Frequency of valuation

Classification grade or category	Frequency of valuation
“Pass” or “Acceptable”	Valuation of collateral must be conducted in line with the banking institutions collateral valuation policies and guidelines.
“Watch” or “Special mention”	Valuation of collateral must be conducted in line with the banking institutions collateral valuation policies and guidelines.
“Substandard”	Valuation of collateral must be performed upon initial classification of exposure into the “Substandard” classification category or earlier if, conditions of unlikeliness to pay by the counterparty is well established (based on borrower’s patterns of payment behaviours in the past circumstances and new facts that change the counterparty’s financial situation).
“Doubtful”	Valuation of collateral must be conducted in line with the banking institutions collateral valuation policies and guidelines.
“Loss”	Valuation must be performed at classification of the exposure into the “Loss” category. Subsequently, collateral must be valuated and must be performed at a minimum every 12 months while the exposure continues to be classified in the “Loss” category or more frequently if there are any external or internal indicators of deterioration in the value of collateral. In this regard banking institutions must consider all relevant qualitative and quantitative factors. If the loan account continues to remain classified as loss in subsequent years and no better collateral is offered, then a deep haircut as contemplated in paragraph 14.1 of this Determination must be applied to the value of existing collateral.

15. <u>Nonconforming</u>

(a) A loan or an extension of credit, that was within a banking institutions legal lending limit when made being either a regulatory limit or the banking institutions internal limit, will not be deemed a violation, but will be treated as nonconforming if the loan is no longer in conformity or compliance with the bank’s lending limit due to:

(i) a decline in the banking institutions capital position;

(ii) borrowers subsequently merged or formed a common enterprise;

(iii) collateral securing the loan to satisfy the lending limit requirements has declined in value; or

(iv) either the bank’s internal lending limit, the regulatory limit or capital requirements changed.

(b) A banking institution must use reasonable efforts to bring the loan or credit facility that is nonconforming as a result of paragraph (a) above of this section into conformity with the bank's lending limits, unless it would be inconsistent with safe and sound banking practices to do so.

(c) A banking institution must bring a loan or credit facility that is nonconforming as a result of circumstances described in paragraph (a) above of this section into conformity with the bank's lending limit within 30 calendar days, except when judicial proceedings, regulatory actions or other extraordinary circumstances beyond the banking institutions control prevents it from taking action.

16. Stress Testing

(a) All banking institution must document the stress testing policies that need to be followed when conducting credit risk stress testing, which must be approved by the board of directors. The stress testing policies must include the following:

(i) The frequency and procedures for identifying principal risk factors affecting the portfolio;

(ii) The methodology for constructing appropriate and plausible stress testing scenarios;

(iii) The procedures for setting stress loss limits and the authority for setting those limits;

(iv) Remedial actions to be taken if stress test results show losses in excess of limits.

(b) All banking institutions must at each calendar quarter report the credit risk stress testing outcomes to the Bank.

17. Disclosure in Annual Financial Statements

(a) In submitting annual financial accounts to the Bank, banking institutions shall disclose whether the accounting treatment of the annual financial statements comply with this Determination.

(b) The foregoing therefore places certain responsibilities on the independent auditors of banks. Therefore, in order for independent auditors to discharge the responsibility placed on them as such, as the minimum the following shall apply:

(i) the directors of a banking institution shall include in the directors' report in the annual financial statements, a statement of compliance with the provisions of this Determination;

(ii) the directors of a banking institution shall include in the notes to the annual financial statements, under the accounting policies, a statement of compliance with the provisions of this Determination; and

(iii) while conducting their audit of loans and advances the independent auditors of a banking institution must be satisfied that the statements of compliance as indicated above under paragraphs (i) and (ii) are included in the annual financial statements of the banking institution and that such compliance is achieved. The independent auditor then by signing the annual financial

statements would have discharged the onus placed on them by this Determination.

18. Reporting Requirements

The reporting requirements and expectations by banking institutions outlined in this Determination must be made in accordance with the Banking Supervision Circular on Standard Returns or as otherwise directed by the Bank. Banking institutions must submit the required regulatory returns, reports or other information specified in this Determination by the reporting date associated with a specific reporting frequency (i.e., quarterly, half-yearly, yearly, daily), whatever the case may be.

18.1 Regulatory returns reporting

A banking institution shall, at the end of each calendar quarter submit to the Bank all returns in terms of this Determination.

18.2 International Financial Reporting Standards (IFRS) reporting

(a) A banking institution must at the end of each calendar quarter submit to the Bank the loan classification and provisioning in terms of International Financial Reporting Standards (IFRS).

(b) A banking institution must submit, on an annual basis, after the audit of the financial statements is completed by external auditors:

(i) The inputs in the expected credit loss (ECL) model i.e., probability of default (PDs), loss given default (LGDs), forward looking indicators and significant judgments applied;

(ii) Factors for assessments of significant increases in credit risk (SICR);

(iii) Evidence of the validation of models used to assess and measure ECL; and

(iv) The computation and considerations of the collateral discounting applied under the expected credit loss (ECL) model.

PART IV: REMEDIAL MEASURES

19. **Remedial measures** - If a banking institution fails to comply with this Determination, then the Bank may pursue any remedial measures as provided under the Act or any other measures the Bank may deem appropriate in the interest of prudent banking practice.

PART V: EFFECTIVE DATE

20. **Effective date** - This Determination comes into effect on the date of publication of notice in the *Gazette*. Any existing arrangements of the repealed BID-2 must be brought into compliance with this Determination within one (1) year of the publication of the Determination in the *Gazette*.

21. **Repeal of BID-2** - This Determination repeals and replaces the Determination on Asset Classification, Suspension of Interest and Provisioning (BID-2) published, as General Notice No. 278, in the Government Gazette No. 3078 of 30 October 2003.

Questions relating to this Determination should be addressed to:

The Director,
Banking Supervision Department,
Bank of Namibia,
Tel: +264-61-283 5041.

APPENDIX A

LOAN CLASSIFICATION (RATING) MATRIX

A combined assessment of financial condition and repayment history of a borrower should be used to arrive at an initial classification grade for a loan. Adjustments to the initial grade should then be made based on mitigating or unique circumstances. The Loan Classification Matrix below provides criteria for assigning a preliminary rating.

LOAN CLASSIFICATION MATRIX			
	Repayment History		
Financial Condition	**Strong**	**Fair**	**Unsatisfactory**
Strong	Pass	Special Mention	Substandard
Satisfactory	Special Mention	Substandard	Substandard
Fair	Substandard	Substandard	Doubtful
Marginal	Substandard	Doubtful	Loss
Unsatisfactory	Doubtful	Loss	Loss

Definitions: The following definitions are used in the Loan Classification Matrix above.

FINANCIAL CONDITION	
Strong...	Borrower’s financial condition is of highest quality; normal indicators of financial health show that borrower is clearly able to repay both principal and interest according to original terms of loan agreement.
Satisfactory	Borrower is financially stable but various unsatisfactory aspects exist regarding the financial condition of the borrower which are generally minor.
Fair...	Borrower is financially stable but various unsatisfactory aspects exist regarding the financial condition of the borrower, some of which may be significant.
Marginal...	Borrower is financially unstable and significant unsatisfactory aspects exist regarding the financial condition of the borrower.
Unsatisfactory	Borrower’s financial condition is highly unsatisfactory; it is likely that liquidation or other formal insolvency proceedings have begun or will commence shortly.

REPAYMENT HISTORY	
Strong	Interest and principal are current (i.e., not overdue) and there is no evidence that the current loan balance includes any capitalized amounts of either principal or interest from previous loan roll-overs. A grace period of no more than 7 days may be allowed before payments are considered overdue to allow for administrative errors on the part of borrower or the bank.
Fair	Interest or principal has historically been overdue for more than 7 days but less than 30 days, or there is evidence of interest or principal capitalization.
Unsatisfactory	Interest or principal has been overdue for more than 30 days, or there is evidence of equivalent rescheduling of payments or capitalization of interest.

APPENDIX B

SUBJECTIVE CRITERIA FOR THE QUALITATIVE ASSESSMENT OF A BORROWERS UNLIKELINESS TO PAY

The table below provides examples of possible indicators of financial difficulty but is not intended to constitute an exhaustive enumeration of financial difficulty indicators.

Retail portfolio	Wholesale and Treasury portfolio
The borrower meets one or more of the following: - · In short-term forbearance · Direct debit cancellation · Extension to term initially granted · Previous arrears in the last 12 months · 30 days and more past due on its contractual payments · It became probable that the borrower will enter bankruptcy or other financial reorganization · The purchase of or origination of financial asset at a deep discount that reflect incurred credit loss · The lender for economic or contractual reasons relating to the borrower's financialdifficulty granted the borrower a concession that would not otherwise be considered · Significant change in collateral value or in the quality of the third-party guarantee or credit enhancement supporting the obligation (secured facilities only) which is expected to increase the risk of default · Actual or expected significant internal credit rating downgrade or decrease (worsening) in behavioral scoring used to assess credit risk internally.	If the borrower is on the watch-list and/or the instruments meets one or more of the following: - · Significant increase in credit spread · Significant adverse change in business, inancial and/or economic conditions in which the borrower operates · Actual or expected forbearance or restructuring · A breach of contract such as default or past due events · Actual or expected significant adverse change in operating results of the borrower · Significant change in collateral value or in the quality of the third-party guarantee orcredit enhancement supporting the obligation (secured facilities only) which is expected to increase the risk of default · Early signs of cashflow/liquidity problems such as delay in servicing trade creditors or loans · Significant change such as, reduction in financial support from a parent entity or affiliates · The disappearance of an active market for the financial asset because of financial difficulty · Actual or expected significant downgrading in an external credit rating

APPENDIX C

SUPERVISORY GUIDANCE FOR CREDIT RISK AND ACCOUNTING FOR EXPECTED CREDIT LOSSES (SUMMARIZED VERSION OF BCBS PRINCIPLES)

Principle 1 Board and management responsibilities	· A banking institution's board of directors and senior management are responsible for ensuring appropriate credit risk practices, including an effective system of internal control, to consistently determine adequate allowances
Principle 2 Sound ECL Methodologies	· The measurement of allowances should build upon robust methodologies to address policies, procedures, and controls for assessing and measuring credit risk. · Banking institutions should clearly document the definition of key terms and criteria to duly consider the impact of forward-looking information including macro-economic factors, different potential scenarios and define accounting policy or restructuring
Principle 3 Credit risk rating and grouping	· A banking institution should have a credit risk rating process in place to appropriately group lending exposures on the basis of shared credit risk characteristics.
Principle 4 Adequacy of allowances	· A banking institution's aggregate amount of allowances should be adequate and consistent with the objectives of the applicable accounting framework regardless of whether allowance components are determined on a collective or an individual basis. · Banking institutions must ensure that the assessment approach (individual or collectively) does not result in delayed recognition of ECL, e. g. by incorporating forward-looking information incl. macro-economic factors on collective basis for individual assessed loans.
Principle 5 Validation of ECL Models	· A banking institution should have policies and procedures in place to appropriately validate models used to assess and measures expected credit losses.
Principle 6 Experienced Credit Judgement	· Experienced credit judgement in particular with regards to forward-looking information and macro-economic factors is essential · Consideration of forward-looking information should not be avoided on the basis that banking institutions consider costs as excessive or information too uncertain if this information contributes to a high-quality implementation
Principle 7 Common systems and data	· A banking institution should have a sound credit risk assessment and measurement process that provides it with a strong basis for common systems, tool, and data
Principle 8 Disclosure	· A banking institution public disclosure should promote transparency and comparability by providing timely, relevant, and decision-useful information.

APPENDIX D

REGULATORY TECHNICAL GUIDANCE ON MATERIALITY THRESHOLD FOR PAST DUE CREDIT OBLIGATION

1. Purpose

This document is intended to provide a high level regulatory technical guidance (RTG) on the treatment of the regulatory materiality threshold, for past due credit obligation. For this guidance and in relation to past due exposures, the term materiality threshold is used to refer to an amount (equal to a percentage %) of original loan amount/exposures or an amount that has been past due/overdue for 90 days and more or an absolute amount set by regulatory authority, for all on-balance sheet exposures. The threshold will be utilized for the purpose of identification of defaulted exposures that are past due more than 90 days with the following objectives:

(a) To determine whether the credit obligation past due is material or not,

(b) To efficiently eliminate cases where the past due exposures is not a result of materialization of credit risk but occurs due to other circumstances,

(c) To effectively and timely identify real material defaults, and

(d) To estimate risk parameters more accurately.

2. Application of the threshold

The materiality threshold should be applied by reference to an individual exposure, and aggregated exposures or past due amount related to the counterparty's total debts as determined by the supervisor in relation to the counterparty's debt. Under this guidance, a default shall be considered to have occurred if the obligor is past due more than 90 days (while for overdraft credit facilities, default is considered to have occurred when such facility operated above the approved limit for similar period) on any material-credit-obligation[3] to the banking institution.

2.1 Non-retail exposures

Banking institutions must apply the past due criterion at either individual level or at an aggregated or group credit facilities, or related party exposure or combined loans to separate borrowers in relation to the total obligations of the counterparty to the banking institution where appropriate.

2.2 Retail exposures

Banking institution must apply the past due criterion at the level of an individual credit facility rather than in relation to the total obligations of the borrower. For this guidance, the following exposures are grouped in the retail exposure class, subject to the condition that they satisfy the requirements of paragraph 15.7 and 18.7 of BID-5 and BID-5A, respectively.

(a) Exposure secured by residential property,

(b) SME Commercial immovable property,

(c) Exposures to the Public Sector Entities, and

(d) Other retail exposures (to individuals retail borrowers and SMEs)

3. Composition of the materiality threshold

The materiality threshold must consist of an absolute component and a relative component. <u>The absolute component</u> shall be expressed as a maximum amount for the sum of all amounts past due owed by an obligor to the banking institution. In terms of this guidance, the limit or maximum amount shall not exceed an amount equal to NAD 2,005 (EUR 100) for retail and NAD 10,000 (EUR 500) for non-retail.

<u>The relative component</u> must be expressed as a percentage reflecting the amount of the credit obligation past due in relation to the total of all on-balance sheet exposure to that obligor of the banking institution excluding equity exposure. In terms of this guidance, the limit or the percentage is set at an amount equal to 0.5% of the original loan/exposure (total on-balance sheet debts).

[3] According to paragraph 30 of the Basel document titled "Prudential treatment of problem assets-definition of non-performing exposures and forbearance" the term material refers to an exposure that hit the materiality threshold in force in a given jurisdiction as defined by supervisor.

PROOF

4. Calculations threshold amount and Ageing analysis

Examples of how the amounts of materiality thresholds are computed are provided for in respect of both normal credit facilities and overdraft credit facility in table "A" and table "B" bellow. Additionally, an example of ageing analysis for purposes of determining the cut off amount and date for past due 90 days and more, is provided for in table "C" below

Table "A"

	1	2	3	4	5	6	7	8	9	10	11	12
No	**Type of credit facility**	**Term of matuirity**	**Original loan amount**	**Applicable interest rate (%)**	**Monthly principal amount**	**Monhtly interest chargers**	**Total monthly payment**	**Total outstanding amount**	**Total amount of past due or arrears**	**MTH-1 0.5% of the original loan amount**	**90 days past due amount**	**MTH-1 retail N$1000 no- retail N$10,000**
1	Commercial.M.I	180 months	15,000,000	10.05%	83,333	128,034	211,367	15,300,769	634,101	75,000	211,367	10,000
2	R. Home loan	240 months	1,000,000	10.85%	4,167	9,215	13,382	1,203,478	40,146	5,000	13,382	1,000
3	Instalment SA	58 months	200,000	10.85%	4,167	6,010	6,010	201,362	18,030	1,000	6,010	1,000
4	Personal loan	24 months	150,000	14.40%	6,250	8,085	8,085	149,255	24,255	750	8,085	1,000

Table "B" Overdraft credit facility

	1	2	3	4	5	6	7	8	9	10	11
No	**Credit type**	**Term of facility matuirity**	**Approved original amount**	**Total oustanding balance**	**Applicable interest rate (%)**	**Monhtly interest Chargers**	**Amount of Exces and charges**	**Total payment due**	**MTH-1 0.5% of the original loan amount**	**90 days past due amount**	**MTH-1 retail N$1000 no-retail N$10,000**
1	O/D	12 months	100,000.0	126,327.0	12.50%	1,327.0	22,346.0	26,327.0	500.0	26,327.0	1,000.0

Table "C" Againg analysis

No	Original loan amount	Total outstadning amount	Total amount of past due or arrears	30 days and and more	60 days and and more	90 days and and more	120 days and and more	150 days and and more
1	15,000,000	15,300,769	634,101	634,101	422,734	211,367	-	-
2	1,000,000	1,203,478	40,146	40,146	26,764	13,382	-	-
3	200,000	201,362	18,030	18,030	12,020	6,010	-	-
4	150,000	149,255	24,255	24,255	16,170	8,085	-	-

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