GOVERNMENT GAZETTE

OF THE

REPUBLIC OF NAMIBIA

N$6.00 WINDHOEK - 14 March 2019 No. 6855

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BANK OF NAMIBIA

No. 48 2019

DETERMINATION ON LIMITS ON EXPOSURES TO SINGLE BORROWERS, LARGE EXPOSURES AND CONCENTRATION RISK (BID-4): BANKING INSTITUTIONS ACT, 1998

In my capacity as Governor of the Bank of Namibia (Bank), and under the powers vested in the Bank by virtue of section 71(3) of the Banking Institutions Act, 1998 (Act No 2 of 1998), read in conjunction with section 34 of the aforementioned Act, I hereby issue **this Determination on Limits on Exposures to Single Borrowers, Large Exposures and Concentration Risk (BID-4)**, which determination shall become effective on 31 December 2019.

I. SHIIMI
GOVERNOR Windhoek, 19 February 2019

BANK OF NAMIBIA

Determination No. BID-4

LIMITS ON EXPOSURES TO SINGLE BORROWERS, LARGE EXPOSURES AND CONCENTRATION RISK

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PART I: PRELIMINARY

1. **Short Title -** Single Borrowers, Large exposures and concentration limits.

2. **Authorization** - Authority for the Bank to issue this Determination is provided in Section 71(3) of the Act.

3. **Application** - This Determination applies, on both solo and consolidated basis, to all banks authorised by the Bank to conduct banking business in Namibia.

4. **Definitions** - Terms used within 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, 1998 (Act No. 2 of 1998) as amended;

4.2 **"bank" -** means banking institution as defined in the Act.

4.3 **"bankers' acceptances"** - means drafts or bills of exchange drawn upon a bank and having a term not more than six months, exclusive of days of grace and (i) which arise out of transactions involving the importation or exportation of goods; (ii) which arise out of transactions involving the domestic shipment of goods or financing of operations; or (iii) which are secured at the time of acceptance by a warehouse receipt or other such document conveying or securing title over readily marketable commodities.

4.4 **"capital funds"** - For the purpose of this Determination, "capital funds" are as defined in the Determination on Capital Adequacy (BID-5).

4.5 **"commercial paper"** - means a short term unsecured money market obligation issued by commercial and financial companies, having a term not more than one year; proceeds are used to finance current obligations; commercial paper is a negotiable instrument and may be issued either at a discount basis or as interest-bearing paper.

4.6 **"commodities"** - means a basic good used in commerce that is interchangeable with other commodities of the same type; commodities are most often used as inputs in the production of other goods or services. The quality of a given commodity may differ slightly, but it is essentially uniform across producers. When they are traded on an exchange, commodities must also meet specified minimum standards, also known as a basis grade.

4.7 **"common enterprise"** - a common enterprise exists when (i) the expected source of repayment is the same for loans or advances made to different related parties or connected borrowers, or (ii) exposures are made to persons related by common control, where the persons are engaged in inter-dependent businesses, or where there is substantial financial inter-dependence among them.

For purposes of this paragraph, "control" is presumed to exist when: (a) two or more persons acting together directly or indirectly own, control, or holds 50 per cent or more of any class of voting shares of another person; or (b) two or more persons acting together control, in any manner, the election of a majority of the directors, trustees, or others exercising similar functions over another person; or (c) any other circumstances exist which indicate that one or more persons acting together exercise a controlling influence, directly or indirectly, over the management or policies of another person.

4.8 **“common or correlated underlying factors”** - for the purpose of this Determination refers to those risk factors to which a person or group of counterparties in a specific economic or industry sector are exposed; and (a) whose performance is dependent on the same activity or commodity; or (b) where correlations in the probability of default can be identified.

4.9 **“concentration risk”** - means the risk of a possible loss due to direct or indirect overexposure to a single person or group of related persons or unrelated counterparties in a specific economic or industry sector.

Risk concentrations can arise in a bank’s assets, liabilities, or off-balance sheet items, through the execution or processing of transactions (either product or service), or through a combination of exposures across these broad categories. By their nature, risk concentrations are based on common or correlated risk factors, which, in times of stress, have an adverse effect on the creditworthiness of each of the individual counterparties making up the concentration.

4.10 **“exposure”** - for the purposes of this Determination exposure must have the same meaning as credit facility and shall include any direct or indirect advance of funds made to a person or group of related persons on the basis of an obligation to repay the funds. Examples of exposure are, but not limited to, on-balance sheet loans, advances, overdrafts, redeemable preference shares, holdings of papers off-balance sheet commitments (e.g. acceptances and guarantees on behalf of the person or group of related persons), underwriting facilities, endorsements, placements, documentary credits issued, performance bonds and other contingent liabilities.

4.11 **“ large exposure”** - means any exposure to a single person or group of related persons which, in the aggregate, equals or exceeds 10% of a banking institution’s eligible capital funds.

4.12 **“marketable commodities”** - means agricultural or mining commodities such as agricultural staples, mineral ores, etc. which are traded on established domestic or international markets and for which there are recognized daily price quotations and meet specified minimum standards, also known as a basis grade.

4.13 **“money market instruments”** - means financial instruments with outstanding maturities of less than a year which are traded under ordinary circumstances with reasonable promptness at a fair market value determined by quotations based on actual transactions at an auction or a similarly available daily bid and ask price market. This includes, but not limited to, notes, bonds, treasury bills and debentures, commercial papers, negotiable certificates of deposit, and bankers’ acceptances.

4.14 **“Person(s)”** - for the purpose of this Determination, refers to natural and juristic persons. It includes any partnership, any public body, and any body of persons, corporate or unincorporated. It applies to any single person or group of related persons, to companies owned by the same owner or shareholder, to subsidiaries of the same holding company, to any holding company and its subsidiaries, to any natural person and one or more companies of which that natural person is a controller. The term “person or group of related persons” is also clarified in the scenarios stated in paragraph 10 of this Determination.

4.15 **“Segregated deposit”** - means a deposit account, usually savings or time deposit rather than chequing, in the same bank as the lending bank and in some way tagged or frozen or identified as pledged against a loan.

PART II: STATEMENT OF POLICY

5. **Purpose -** This Determination is intended to set certain conditions and limitations on the borrowing of excessive amounts of a bank’s funds by one person or a group of related persons or group of counterparties or one economic sector or industry whose performance is determined by the common or correlated underlying factors. It is also intended to safeguard a bank’s depositors and creditors by diversifying credit risk among several persons engaged in different lines of business.

6. **Scope** - This Determination applies to all exposures held or reflected on a bank’s balance sheet or otherwise held or reflected as off-balance sheet items.

7. **Responsibility -** The Board of Directors of each bank must be responsible for establishing policies and procedures which are adequate to ensure that (a) all exposures fully comply with the determined limits set forth in the Act and in this Determination; (b) all exposures are made and administered in accordance with prudent lending practices, and (c) the bank’s framework for managing concentration risk is clearly documented and shall include a definition of risk concentrations relevant to the bank and how these concentrations and their corresponding limits are calculated. (d) all internal limitations are defined in relation to bank’s capital, total assets or, where adequate measures exist, its overall risk level.

PART III: IMPLEMENTATION AND SPECIFIC LIMITATIONS

8. **General Limitations -** The following limits shall apply to the approved limit for the credit facilities or the amount outstanding, whichever is higher:

8.1 **General**: The total of all exposures outstanding at any time to a single person, or a group of related persons must not exceed 25 per cent of a bank’s capital funds.

8.2 **Aggregate of large exposures**: The aggregate of all large exposures (i.e. an exposure which individually equals or exceeds 10 per cent of a bank’s capital funds) must not exceed 800 per cent of a bank’s capital funds.

8.3 **Exemption by Bank of Namibia:** Approval to exceed the limits in paragraphs 8.1 and 8.2 above, if requested by a bank pursuant to section 34(1) of the Act may only be granted by the Bank subject to the following conditions:

(i) The total exposure to a person or a group of related persons or counterparties in a specific economic or industry sector must not exceed the amount stated in the exemption request submitted to the Bank;

(ii) The exposure must comply in all respects with a written lending policy that has been adopted and approved by the Board of Directors of the bank;

(iii) Before requesting the Bank's approval, the exposure must be reviewed and approved by a majority of the entire Board of Directors of the bank, and so documented in the minutes of the Board; and

(iv) Before requesting the Bank's approval, the bank must have made a request to at least three other banks, at least two of which are not affiliated with the bank, to participate in the loan by (a) joining in a syndication of the exposure, or (b) purchasing the portion that exceeds the single borrower limit and have been denied by all three, and written documentation of such requests and denials must be maintained.

(v) The exemption so granted will be for a determined period of time within which the concerned bank would have to bring its exposure back to threshold limits determined by the Bank.

(vi) Prior to requesting exemption, the banking institution must conduct a comprehensive credit analysis or delegate such task to a qualified third party to ensure that such an exposure is reasonably expected to perform over the life time of the loan. Such analysis should be readily available to the Bank for inspection should the Bank so require.

9. **Exemptions -** The following exemptions apply to the limits in paragraph 8 above:

9.1 **Discounted paper.** Exposures arising from the discount of commercial paper negotiated with full recourse to the issuer shall not count against the purchasing bank discounting the commercial paper.

9.2 **Bankers' acceptances.** The aggregate amount of bankers' acceptances (including participations therein) which have been issued or accepted by another bank must not exceed more than 200 per cent of the purchasing bank's capital funds.

9.3 **Marketable commodities.** A bank may lend up to 50 per cent of its capital funds so long as the total of all exposures, which exceed the 25 per cent limits in paragraph 8 above, is secured by marketable commodities traded on a recognised stock exchange. For this exception to apply, the current marketable commodities held as security must: (i) have a current value that is at least 125 per cent at all times of the exposures that exceed 25 per cent of the bank's capital funds, and (ii) be fully insured.

9.4 **Government and Bank of Namibia.** Exposures granted to or fully secured by obligations of the Government of Namibia or the Bank of Namibia or fully secured by the explicit guarantee issued by the Government of Namibia must be exempted from the above limits.

9.5 **Segregated deposits.** Exposures which are fully or partly secured at all times by a segregated deposit account in the lending bank must be exempt, to the extent they are covered by such deposit account, from the lending limits set forth in paragraph 8 above. For this exception to apply, the bank must have the legal right of offset for the deposit. Also, if the deposit is in a different currency than the secured exposure, then the deposit must be revalued at least daily based on applicable exchange rates and must: (i) have a current value that is at least 125 per cent at all times of the exposures that exceed 25 per cent of the bank's capital funds, and (ii) be fully insured.

Finally, if the value of the pledged deposit declines and results in an unsecured exposure exceeding the lending limits, then the exposure must be brought into conformance within five (5) working days.

9.6 **Bank guaranteed debts.** A bank may lend up to 50 per cent of its capital funds so long as the total of all exposures which exceed the lending limits in paragraph 8 above is guaranteed by another bank as to both principal and interest.

9.6.1 However, for this exception to apply, the domestic guaranteeing bank must:

(i) Not be associated with the lending bank;

(ii) Not be rated lower than one notch below the sovereign rating by a credit rating agency fully compliant with the eligibility criteria as outlined in the Basel II regulatory capital framework (International Convergence of Capital Measurement and Capital Standards). Further, Credit rating agencies whose services are utilized by banking institution in Namibia must be registered with the European Security and Market Authority (ESMA); and

9.6.2 The foreign guaranteeing bank, must have credit rating of investment grade as a minimum.

9.6.3 The aggregate of all exposures guaranteed by another bank must not exceed at any time more than 200 percent of the lending bank's capital funds, and (v) the aggregate of all exposures, including guarantee, by the guaranteeing bank to the person or group of related persons must not exceed the lending limits in paragraph 8 above.

9.7 The list of exemptions provided above is not exhaustive and other exemptions may be considered at the Bank's discretion.

10. **Combining loans to separate borrowers** - (a) **Combination**: Exposures made to one person will be combined with exposures made to another person when (i) the exposure proceeds are used for the direct benefit of the other person ('use' test), or (ii) a common enterprise exists between the persons ('source' test). The "source test" shall be deemed to exist when the expected source of income used for repayment of the loan is the same for each person or the "use test" is deemed where separate persons borrow from one banking institution for the purpose of acquiring an entity where those persons own more than 50% of the controlling or voting rights

(b) **Determination**: For purpose of this Determination, the Bank will decide when an exposure nominally made to one person will be combined with exposures to another person. Such decision will be made in the case where there is doubt as to whether or not to combine two or more exposures or where the Bank discovers that two or more exposures that ought to have been combined are treated as separate exposures. The Bank must take the following factors into account in deciding when exposures should be combined: common ownership/control, common directors or management, guarantees or cross guarantees and direct commercial interdependency which cannot be substituted in the short term.

11. Loans to partnerships

11.1 **To the group**: For purposes of this Determination, exposures to a partnership will be considered exposures to each member of the partnership.

11.2 **For purchasing interests**: For purposes of this Determination, exposures made to members of a partnership for the purpose of purchasing an interest in the partnership will be combined with exposures made to the partnership.

12. **Loans written-off** - The lending limits in paragraph 8 above apply to all existing loans, including any loans or portions thereof, which have been written-off in whole or in part. Loans which have been discharged in bankruptcy or which are no longer legally enforceable in a court of law are not subject to the lending limits.

13. **Loan participations** - When a bank sells a participation in a loan, the portion that has been sold will not count against the lending limits in paragraph 8; however, to be excluded, (i) the participation agreement must require that if a default occurs, all participants will share pro rata in repayments and collections relative to their participation percentages at the time of default and (ii) the sale transaction for a portion of a loan shall be a cash transaction. For the purpose of this paragraph, cash transaction is a transaction of which payment is made within a period of not more than seven working days following the conclusion of the transaction.

14. **Loan syndications** - When two or more banks collectively make a loan to a single borrower, only the amount actually loaned or the approved limit allocated by each bank and representing its pro rata share of the syndicated loan will count against the limits set forth in paragraph 8 above.

15. **Interest or discount on loans** - The limits set forth in paragraph 8 above shall not apply to any portion of an exposure which represents accrued interest unless such interest has been capitalized or in any way converted to principal.

16. **Non-conforming exposures -** (a) If an exposure complies with the lending limits in paragraph 8 above when it is made but later fails to comply because (i) the bank's capital funds decline, (ii) the borrower merges or forms a common enterprise with another borrower, (iii) the bank merges with another bank which is also lending to the borrower, (iv) the lending limit or capital funds rules change, or (v) collateral securing the exposure fails to qualify as an exemption under paragraph 9, then the exposure will be treated as 'nonconforming'.

(b) If an exposure becomes 'nonconforming' for reasons (i-iv) above, then the bank must use all reasonable efforts to promptly bring the exposure into compliance with lending limits unless doing so would be inconsistent with safe and sound banking practices.

(c) If an exposure is 'nonconforming' for reason (v) above, then the bank must bring the exposure into compliance within 30 calendar days of the date that the exposure became nonconforming, unless judicial proceedings, regulatory actions, or other circumstances beyond the bank's control prevent the bank from taking action.

17. **Stress-testing -** Banks should conduct regular stress-testing (at least once a year) of large exposures and concentration risk to assess the impact of different scenarios and of the potential losses that may arise from changes in the key risk factors such as economic or industry downturn, interest rate and any other market movements that may adversely have any impact on the bank.

When conducting stress-tests, management of banks should note that during periods of economic calm, concentrations in a bank's portfolio are unlikely to have any noticeable effects on performance or credit quality as usually measured and, as such, can remain latent. Bank management should understand that the real threat arises in an adverse economic scenario, where connected or correlated exposures all show increased risk of default at the same time. The results of stress-tests must be used to prepare for possible real adverse impacts that may affect the bank.

18. Reporting Requirements

The bank shall, at the end of each calendar quarter submit to the Bank returns in terms of this Determination by not later than the 26th day of the following month.

PART IV: REMEDIAL MEASURES

19. **Remedial measures** - If a bank 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 practices.

PART V: EFFECTIVE DATE

20. **Effective date** - The effective date of this Determination shall be 31 December 2019.

21. **Repeal of BID-4** - This Determination repeals and replaces the Determinations on Limits on Exposures to Single Borrowers, Large Exposures and Concentration Risk (BID-4) published, as General Notice No. 290, in Government Gazette No. 4373 of 6 November 2009.

Questions relating to this Determination should be addressed to the -

Director
Bank Supervision Department
Bank of Namibia
Tel: 283-5040
