

MALDIVES MONETARY AUTHORITY

PRUDENTIAL REGULATION

No. 02-2009

SINGLE BORROWER and LARGE EXPOSURE LIMITS

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PART I: PRELIMINARY

- 1: Short Title** – Single borrower limits.
- 2: Authorization** – The Maldives Monetary Authority (MMA) is authorized to issue regulations under Art. 36 read with Art. 29-34 of the MMA Act 1981 (MMA Act) in relation to prudential matters to be complied with by all banks and deposit-taking institutions (collectively 'banks'), or other persons as the regulation may specify.
- 3: Application** – All banks and deposit-taking institutions licensed by the MMA to conduct banking business in the Maldives.
- 4: Definitions** – Terms used within this regulation are as defined in the Act, as defined below, or as reasonably implied by contextual usage:
- (1) "**associate**" – means any person over whom another person exerts or has the ability to exert significant influence and who is not a subsidiary of the first person; also referred to as an "affiliate" or "affiliated person". (See also International Accounting Standard IAS-28 or successor standards).
- (2) "**bank**" – means all banks and deposit-taking institutions licensed by the MMA to conduct banking business in the Maldives.
- (3) "**bankers' acceptances**" – means drafts or bills of exchange drawn upon a bank for a term not exceeding six months inclusive of days of grace and which arise out of transactions involving (i) the importation or exportation of goods; (ii) the domestic shipment of goods or financing of operations; or (iii) which are secured at the time of acceptance by a receipt issued by a bonded warehouse or such other document that conveys or secures title over readily marketable commodities.
- (4) "**capital base**" – means Total Capital defined in the Capital Adequacy Regulation issued by the MMA.
- (5) "**commercial paper**" – means short term unsecured money market obligations issued by commercial and financial companies for terms not exceeding six months where the proceeds are used to finance current operations, the instrument is negotiable and may be issued either on a discounted basis or as an interest-bearing obligation.
- (6) "**common enterprise**" – a common enterprise exists when (i) the expected source of repayment is the same or substantially the same for advances made to different but related borrowers, or (ii) exposures are made to persons related by common control where the persons are engaged in inter-dependent businesses or there is substantial financial inter-dependence among them.
- (7) "**control**" – for purposes of this regulation, "control" is presumed to exist when:
- (i) one or more persons acting together directly or indirectly own, control, or have power to vote 50% or more of any class of voting shares of another person; or
- (ii) one 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
- (iii) any other circumstances exist which indicate that one or more persons acting together exercise a controlling influence, directly or indirectly, over the activities, management, practices or policies of another person.

(8) "**corporate group**" – means a corporation plus its subsidiaries and associates or affiliates; an enterprise is a subsidiary or an associate of a corporation which exerts, or has the power to exert, control or significant influence over a subsidiary or an associate (see International Accounting Standards IAS 27-28 or successor standards).

(9) "**current market value**" – means that value determined by using valuation methods appropriate to the type of property being evaluated. For commercial and multi-use properties (combined residential/rental/commercial), current market value is the average of values determined using the (i) comparable sales approach, (ii) cost approach and (iii) income (discounted cash flows) approach; for residential property (mainly owner-occupied/non-rental) the value is the average of values determined by using the comparable sales and cost approaches. The insured/insurable amount of property held as collateral is not acceptable as a substitute for current market value. The determination of current market value must be documented in writing, show assumptions, analyses and conclusions used, and be available for review by the MMA. As used herein, the term "current" means within a period of 12 months.

(10) "**exposure**" – means any loan, advance or credit exposure, whether direct or indirect, funded or unfunded, including obligations as maker or endorser arising from the discounting of commercial paper, given to a person on the basis of an obligation to repay or which is repayable from specific property pledged by or on behalf of a person; funded exposures are those for which loan proceeds have been provided to the borrower or to a third party on behalf of the borrower; unfunded exposures are those for which loan proceeds have not yet been provided but the bank is legally obligated to do so on a specified future date or event.

(10.1) "**direct exposure**" – means an exposure created when the person applying for a loan is the initial recipient or beneficiary of the loan proceeds or credit facility, is the primary signatory or a co-maker to the loan, and is the person to whom the bank and the courts will look first for repayment of the obligation.

(10.2) "**indirect exposure**" – means an exposure created when a person other than the recipient of a loan agrees or is otherwise legally obligated to repay the debt in the event that the primary obligor/s defaults or is unable to repay the debt; an example of indirect debt is the exposure created when one person guarantees loans advanced to another person; the recipient of the loan proceeds is the 'primary' obligor and the person guaranteeing the loan is the 'secondary' obligor although both persons may be equally liable under the law to repay the obligation.

(10.3) "**large exposure**" – means any exposure to a single borrower or to a group of related borrowers which, in total, equals or exceeds 10% of a bank's capital base.

(11) "**loans**" – means the same as direct exposures unless defined otherwise in text.

(12) "**readily marketable commodities**" – means commercial products and other commodities such as agricultural or fish products, minerals, ores and petroleum products, etc. which are traded on established international markets and for which recognized daily price quotations are commonly available.

(13) "**money market instruments**" – means financial instruments that can be sold and negotiated within three business days on a willing buyer/willing seller basis at a fair value based on actual transactions or readily available daily bid/ask market prices. Money market instruments include stocks, notes, bonds, and debentures traded on a recognized securities exchange, commercial paper and bankers' acceptances.

(14) "**net realizable value**" – means that amount which a bank can reasonably expect to realize after discounting the value of collateral to current market conditions and deducting the reasonable and estimable costs of recovery and sale. Costs of recovery and sale typically include, but are not limited to: legal fees, appraisal costs, sales fees, insurance cover, maintenance, security, and any other expenses necessary to put the collateral in a saleable condition. Net realizable value must be documented in writing, show assumptions, analyses and conclusions, and be available for review by MMA.

(15) "**person**" – means a natural person, company, corporation, associate, trust, joint venture, partnership or other business enterprise.

(16) "**related persons**" – two or more persons will be considered to be related if one person has the ability, directly or indirectly, to control the other person/s or to exercise significant influence over the financial and operating decisions of the other person/s, or if both persons are subject to common control or common significant influence.

(16.1) "**group of closely related persons**" – means two or more persons, companies, corporations, partnerships or other business enterprises which are closely related through common ownership, control, management, financial inter-dependence or cross-guarantees. The definition also includes persons who are family members that are financially dependent upon one or more persons within the group.

(17) "**significant influence**" – means the ability to materially participate in or apply implicit or explicit pressure to the financial and operating policies and decisions of another person; the absence of absolute control does not preclude the ability to exert significant influence over the policies and decisions of another person. If one person holds, directly or indirectly through subsidiaries, 10% or more of the voting power over another person, it will be presumed that the first person exerts or has the ability to exert significant influence over the second person. Conversely, if a person holds, directly or indirectly through subsidiaries, less than 10% of the voting power over another person, it will be presumed that the first person does not exert or have ability to exert significant influence unless there are compelling circumstances to the contrary. The fact that one person holds a substantial or majority ownership in a second person does not preclude a third person from also having the ability to exert significant influence over that second person.

(18) "**subsidiary**" – means an enterprise that is controlled by another enterprise commonly referred to as the 'parent'. Control means the power to govern, directly or indirectly, the financial and operating policies and decisions of an enterprise so as to gain benefits from its activities. (See also International Accounting Standard IAS-27)

PART II: STATEMENT OF POLICY

- 1: Purpose** – This regulation is intended to limit credit risk, relative to a bank's capital base, for exposures to a single person, a group of closely-related persons, a corporate group, and for large exposures in the aggregate. This regulation also is intended to allow flexibility for banks to provide credit facilities beyond a basic limit for certain kinds of low-risk exposures. Finally, this regulation is intended to promote credit risk diversification and broader access to credit for the economy as a whole.
- 2: Scope** – This regulation applies to all banks licensed and operating in the Maldives and to all exposures held on a bank's balance sheet or reflected as off-balance sheet.

- 3: **Responsibility** – It is the responsibility of the board of directors and managing officers of each bank to adopt policies and procedures which are adequate and which ensure (i) that all exposures fully comply with the limits set forth in the Act and this regulation, and (ii) that all exposures are made and administered in accordance with prudent lending practices.

PART III: IMPLEMENTATION AND SPECIFIC REQUIREMENTS

- 1: **Limitations** – The following limits shall apply:
- (a) **Single person:** the total exposures outstanding at any time, including both funded and unfunded exposures, to a single person, or to a group of closely-related persons treated as a single person, shall not at any time exceed 15% of the bank's capital base.
 - (b) **Corporate groups:** the total exposures, funded and unfunded, outstanding at any time to a corporate group shall not exceed 40% of the bank's capital base provided that no one member of the group shall exceed 15% of the bank's capital base and further provided that each member of the group must stand alone in respect of (i) capacity to repay from normal operations, (ii) security pledged, and (iii) use of loan proceeds. If loans to one member of the group are combined with loans to one or more other members and treated as a single borrower as provided under paragraph 3 of Part III, then the 15% single borrower limit in paragraph (a) shall apply to the combined exposures.
 - (c) **Large exposures:** the total of all large exposures, as defined in this regulation, shall not at any time exceed 500% of the bank's capital base.
 - (d) **Compliance with policy:** all exposures shall comply with a comprehensive lending policy that is in writing and adequate for the lending activities of the bank and which has been approved and adopted by the board of directors.
- 2: **Exceptions** – In order to allow banks to accommodate prudently the legitimate credit needs of creditworthy borrowers, the following exceptions shall apply to the limits set forth in paragraph 1 above:
- (a) **Discounted paper.** Exposures arising from the discount of commercial paper acquired with full recourse in the ordinary course of business shall not be included in the total exposures of the person who discounts the paper to the purchasing bank.
 - (b) **Bankers' acceptances.** The total of bankers' acceptances issued (i.e. accepted) by another bank shall not exceed 200% of the capital base of the acquiring bank.
 - (c) **Government-backed debts.** Exposures, or portions thereof, which the national government has unconditionally guaranteed as to payment of principal and interest, or that are fully secured by full faith and credit obligations of the national government (e.g. treasury bills), are exempt from the limits in paragraph 1(a,b,c) above. However, exposures of companies (i.e. state-owned enterprises or SOE's) that are owned by the national government, either wholly or in part, but which are separate legal entities shall be subject to the limits in paragraph 1(a,b,c) unless the national government is directly obligated for or has unconditionally guaranteed the debts of such companies in writing as to the repayment of both principal and interest.
 - (d) **Exposures secured by assigned deposits.** Exposures, or portions thereof, that are fully secured at all times by pledged deposits in the lending bank shall be exempt

from the limits set forth in paragraph 1(a,b,c) above. For this exception to apply, the deposit (i) must be specifically assigned to the bank in writing by the customer, (ii) must be segregated and under the sole control of the bank, and (iii) the bank must have the explicit legal right to set off the deposit against the exposure at any time. If a pledged deposit is in a currency different from the currency of the exposure, then the amount of exposure exempt from the limit will be the amount of the deposit converted into the same currency as the exposure using the official mid-rate of exchange.

(e) **Indirect exposures.** A bank may lend up to 30% of its capital base to a single borrower provided that all exposures which exceed 15% of the bank's capital base are indirect exposures as defined in this regulation.

(f) **Marketable commodities.** A bank may lend up to 30% of its capital base to a single borrower provided that all exposures which exceed 15% of the bank's capital base are secured by readily marketable commodities. For this exception to apply, the commodities pledged as security must, at all times: (i) have a current market value at least 150% of the exposures secured thereby, and (ii) be fully insured against loss or damage by a licensed insurance company acceptable to the bank as determined by its board of directors, and the bank must be named as mortgagee or co-insured in the policy. A bank may not require a borrower to use a specific insurance company, and the MMA reserves the right to object, for cause, to any one or more commodities or insurance companies used by a bank in connection with this exception.

(g) **Exposures secured by immovable property.** A bank may lend up to 30% of its capital base to a single borrower on the security of immovable property provided that (i) the net realizable value of the immovable property is, at all times, at least 150% of the exposures secured thereby, (ii) the bank's mortgage is properly registered and superior to all other liens against the property, and (iii) the property is fully insured against loss or damage in an amount at least equal to the debts so secured by an insurance company that is acceptable to the bank as determined by its Board of Directors, and the bank must be named as mortgagee or co-insured in the policy. A bank, however, can not require a borrower to use a specific/particular insurance company. The MMA reserves the right to object, for cause, to any one or more valuers or insurance companies used by the bank in connection with this exception.

(h) **Bank guaranteed debts.** A bank may lend up to 30% of its capital base to a single person provided that all exposures which exceed 15% of the bank's capital base are guaranteed by another bank as to both principal and interest. For this exception to apply, the guaranteeing bank must not be (i) related to the lending bank or (ii) rated lower than the three highest grades by an internationally recognized rating agency, and the guarantee must be (iii) unconditional and irrevocable, (iv) callable on demand of the MMA, and (v) acceptable MMA in both form and content. Provided further, the total of all exposures backed by guarantees issued by any one bank (individual banks within the same banking group will be aggregated and treated as a single bank) may not exceed 200% of the lending bank's capital base at any time.

If the MMA demands performance under a bank guarantee issued for this exception, then the bank which is the beneficiary of the guarantee will be restricted from (i) declaring or paying cash dividends, (ii) repatriating or distributing profits or capital funds to any shareholder, and (iii) paying amounts to any related person or associate for management or advisory services or other fees related to supervisory, executive, managerial, or policy-making functions until the obligation under the guarantee has been paid in full. This restriction does not, however, apply to reasonable and ordinary

payments for data processing, auditing, or mortgage servicing made pursuant to pre-existing, written contracts unless the MMA specifically restricts such payments.

3: Combining exposures to separate borrowers - (a) **Combination:** Exposures to one person will be combined with exposures to another person and be held subject to the 15% single borrower limit when (i) loan proceeds are subsequently loaned to a second person (i.e. accommodation loans), (ii) loan proceeds are used for the direct benefit of a second person (the 'use' test), (iii) a common enterprise exists between two persons and the common enterprise is being relied upon to generate funds to repay the loan/s (the 'source' test), or (iv) the particular facts and circumstances of the separate borrowers and their inter-relationships indicate, based on applying conservative credit underwriting standards, that the debts should be viewed on a consolidated basis and combined for lending limit purposes.

(b) **Determination:** For purposes of this regulation, the MMA will determine, based upon the facts and circumstances of the particular situation, when an exposure nominally granted to one person will be combined with exposures to another person.

4: Exposures to partnerships - (a) **To the partnership:** For purposes of this regulation, the total exposure of a partnership will include the exposures of each general partner but not the exposures of limited partners unless (i) the proceeds of exposures to limited partners are used for the direct benefit of the partnership or (ii) the exposures of limited partners are repayable primarily from the profits of the partnership.

(b) **To partners:** For purposes of this regulation, the total exposure of each general partner will include the exposures of the partnership but not the exposures of limited partners unless (i) the proceeds of exposures to limited partners are used for the direct benefit of the general partner/s or (ii) the exposures of limited partners are repayable primarily from funds provided by the general partner/s.

(c) **For purchasing interests:** For purposes of this regulation, a loan granted to a member of a partnership for the purpose of purchasing an interest in the partnership will be combined with loans made to the partnership.

(d) **Limited interests:** In the case of limited partnerships where the partnership agreement specifies that limited members are not liable for the debts of the partnership, the rules set forth in paragraphs (a), (b) and (c) above will apply to all general partners or members but not to limited partners. However, if the partnership agreement specifies that limited members are individually liable for a portion of the obligations to the same extent of their proportionate interest in the partnership, then their limited obligations will be combined with other loans to those members for purposes of determining their individual total exposure to the bank

5: Loans written off – The lending limits in paragraph 1(a,b,c) above apply to all loans, including any loans which have been written off in whole or in part. However, loans that have been discharged by a court in bankruptcy or that are no longer legally enforceable will not be included in the total exposure for determining compliance with the lending limits.

6: Loan participations – When a bank sells a participation in a loan to another bank, the portion that has been sold will not count against the lending limits in paragraph 1. However, for this exception to apply, the two banks must have entered into a written participation agreement which specifies that in the event of a default, both banks will

share in recoveries and repayments on a pro rata basis according to their respective participation percentages at the time of default.

- 7: Loan syndications** – When two or more banks collectively make extended credit to a one borrower under a common loan facility (e.g. a syndicated loan), the loan limits in paragraph 1 above apply only to the funds provided by each bank and representing that bank's pro rata share of the total loan.
- 8: Capitalized interest** – Accrued interest that has been added to the principal balance of the loan (i.e. capitalized) with a corresponding entry to interest income is subject to the lending limits in paragraph 1 above the same as if a separate loan is advanced to pay interest.
- 9: Nonconforming exposures** – Exposures which become nonconforming in respect of the limits set forth in paragraph 1, Part III will be treated as follows:

(a) If an exposure is within the limits when made but subsequently exceeds the limits because (i) the bank's capital base declines, (ii) the borrower merges or forms a common enterprise with another borrower, (iii) the bank merges with another bank which also holds exposures to the borrower, (iv) the lending limits or capital base rules change, or (v) the collateral securing the exposure ceases to qualify as an exception under paragraph 2, then the exposure will be treated as 'nonconforming'.

(b) If an exposure becomes 'nonconforming' for any of reason (i)-(iv) in (a) above, then the board of directors and executive officers are required to act promptly to bring the exposure into compliance unless doing so would be inconsistent with prudent banking practices and adversely affect the ultimate recovery of the exposure. Such nonconforming exposures may be renewed, have their maturity extended or be restructured without violating this regulation provided (i) there is no increase in the amount of the exposure, either direct or indirect; (ii) the renewal, extension or restructure does not exceed more than one year; (iii) security collateral, if any, shall not be released, (iv) there is no change in the borrower with the exception of changes resulting from a merger of the borrower with another person, or (v) the renewal, extension or reschedule is not otherwise designed to evade the requirements of this Regulation as determined by the MMA.

(c) If an exposure becomes 'nonconforming' for reason (v) in (a) above, then the board of directors and executive officers are required to act promptly to bring the exposure into compliance within 30 calendar days from the date the exposure became non-conforming unless judicial proceedings, regulatory actions or other circumstances beyond the bank's control prevent such corrective action.

- 10: Reporting Requirements** – Each bank shall submit returns in respect of exposures in the form and frequency as the MMA may prescribe.

PART IV: CORRECTIVE MEASURES

- 1: Remedial measures and sanctions** – If a bank, its directors or managers violate any provision of this regulation in a willful, negligent or flagrant manner which results, or threatens to result, in an unsafe or unsound condition of the bank or that threatens the interests of depositors, creditors or the general public, or if the bank, its directors or managers fail to comply with the instructions and reporting requirements in this regulation, the MMA may take any one or more of the corrective measures or impose

any administrative penalties as provided in the MMA Act. Such measures and penalties may include, but are not limited to, any or all following –

- (a) Issue a warning to the bank;
- (b) Enter into an informal agreement with the bank for correcting violations and any unsafe and unsound practices and conditions;
- (c) Issue an order to the bank requiring it to cease and desist from particular actions and further to take affirmative actions to correct violations and any unsafe & unsound practices and conditions;
- (d) Require the board of directors to inject additional capital funds;
- (e) Restrict the scope of activities of the bank including imposing limitations on any foreign exchange activities, granting of credit, making of investments, acceptance of deposits, borrowing of money, or other activities as the MMA may deem appropriate;
- (f) Suspend access to the credit facilities of the MMA;
- (g) Suspend or require the removal of any directors, executive officers or managers;
- (h) Appoint an advisor or a conservator;
- (i) Impose an administrative penalty on the bank or any of its directors, executive officers or managers; or
- (j) Hold personally liable and seek restitution from, as the law allows, any directors, executive officers or major shareholders of the bank; or
- (k) Suspend or revoke the bank's license.

PART V: EFFECTIVE DATE

- 1:** **Effective date** – This regulation shall come into effect on 18th May 2009.
- 2:** **Supersedence** – This regulation supersedes paragraphs 9(1)(a) and 9(2) of the MMA Regulations for Banks and Financial Institutions (July 1, 1988) and will remain in effect until superseded or replaced by the Banking Law of the Republic of Maldives. In case of conflicting provisions or interpretations between this regulation and any portion of the earlier regulation, this regulation shall take precedence.

Questions relating to this regulation should be addressed to the Senior Executive Director, Financial Sector Division, Maldives Monetary Authority.