BANK OF MAURITIUS

Guidelines on
Capital Adequacy Ratio
for
Non-Bank Deposit Taking Institutions

October 2009

Guidelines on Capital Adequacy Ratio

1. Introduction

These Guidelines take into account the provisions of the Banking Act 2004.

2. Purpose

The Bank of Mauritius enunciates through these Guidelines the minimum capital adequacy ratio that non-bank deposit taking institutions shall maintain at all times.

3. Authority

These Guidelines are issued in terms of section 100 of the Banking Act 2004, and section 50 of the Bank of Mauritius Act 2004.

4. Scope of Application

These Guidelines shall apply to all non-bank deposit taking institutions (hereinafter referred to as NBDTIs) licensed under the Banking Act 2004.

5. Terms and Conditions

The Terms and Conditions issued to NBDTIs under the Banking Act 1988, are hereby repealed and replaced by the new Terms and Conditions specified in Annexure 1.

6. Effective Date

These Guidelines shall come into effect as from 1 October 2009.

7. Capital Adequacy Ratio

NBDTIs shall be required to risk weight the credit risks which form part of their balance sheet assets and shall maintain a capital adequacy ratio of 10 per cent.

For the purpose of assessing capital adequacy, the capital shall be split into two tiers - Tier 1 core capital, also referred to as Tier 1 Capital, and Tier 2 supplementary capital, also referred to as Tier 2 Capital. While Tier 1 capital provides the most permanent and readily available support to a NBDTI against unexpected losses, Tier 2 capital contains elements that are less permanent in nature or are less readily available. However, Tier 2 capital shall not exceed a maximum of 100 per cent of Tier 1 core capital.

The broad details of the capital framework shall be as indicated in the following paragraphs.

8. Tier 1 - Core Capital

Tier 1 core capital shall consist of stated capital, statutory reserve, surplus arising from sale of fixed assets, general reserve, other free reserves created by appropriations from post-tax retained earnings and undistributed balance in profit and loss account attributable to previous years. Accumulated losses, current year's interim losses, goodwill and other intangible assets shall have to be deducted from Tier 1 capital. Other intangible assets shall include, inter alia, investments made in software.

The current year's interim retained profits may be included in Tier 1 core capital only if they have been certified by the NBDTIs' external auditors. In the absence of such verification, current year's interim profits shall not be included in the capital base. The verification by external auditors shall entail at least the following:

(a) Satisfying themselves that the figures forming the basis of the interim profits have been properly extracted from the underlying accounting records;

(b) Reviewing the accounting policies used in calculating the interim profits so as to obtain comfort that they are consistent with those normally adopted by the NBDTIs in drawing up its annual financial statements;

(c) Performing analytical procedures on the result to date, including comparisons of actual performance to date with budget and with the results of prior period(s);

(d) Discussing with management the overall performance and financial position of the NBDTIs;

(e) Obtaining adequate comfort that the implications of current and prospective litigation, all known claims and commitments, changes in business activities and provisioning for bad and doubtful debts have been properly taken into account in arriving at the interim profits; and

(f) Following up problem areas of which the external auditors come across during the course of an audit of the NBDTIs' financial statements.

The external auditors must submit an opinion to the NBDTIs on whether the interim results are fairly stated. The required report, set out in Annexure II, shall be attached to the Quarterly Capital Adequacy Ratio Return.

9. Tier 2 - Supplementary Capital

Tier 2 supplementary capital shall consist of:

(a) **Fixed assets revaluation reserves;**

(b) **General and Portfolio Provisions or reserves; and**

(c) **Subordinated debt.**

(a) <u>Fixed assets revaluation reserves</u>

These reserves arise from revaluation of NBDTIs' own premises to reflect their current value, or something closer to their current value than historic cost. The extent to which the revaluation reserves can be relied upon as a cushion for unexpected losses depends mainly on the level of certainty that can be placed on estimates of the market values of the relevant assets. The assets must, therefore, be prudently valued.

Revaluation of premises shall be carried out by independent professional valuers, on a basis satisfactory to both the external auditors and the Bank of Mauritius. The reserves arising from revaluation of fixed assets shall be explicitly reported in the balance sheet or by way of notes to the audited accounts.

Only 45 per cent of the amount of reserves, explicitly reported in the balance sheet or by way of notes, arising from the revaluation of tangible fixed assets will be eligible for inclusion in Tier 2 capital.

(b) <u>General and Portfolio Provisions or reserves</u>

General and Portfolio Provisions or reserves held against unidentified and unforeseen losses qualify for inclusion in Tier 2 capital subject to an amount not exceeding 1.25 per cent of total weighted risk assets. They shall not be ascribed to a particular asset or group of assets and shall be freely available to meet or absorb any losses which are identified after the reporting date.

Where, however, the provisions or reserves have been created against identified losses or in respect of an identified deterioration in the value of any asset or group of assets, they are not freely available to meet unidentified losses which may subsequently arise elsewhere in the portfolio and do not possess an essential characteristic of capital. Such provisions or reserves shall therefore not be included in the capital base.

(c) <u>Subordinated debt</u>

Subordinated debt which is approved by the Bank of Mauritius may be included in Tier 2 supplementary capital. The amount of subordinated debt included in Tier 2 capital shall be limited to a maximum of 50 per cent of Tier 1 core capital.

Broadly, to be eligible for inclusion, it shall satisfy the following conditions:-

(i) The subordinated debt shall be an unsecured debt;
(ii) It shall have an original maturity of over five years;
(iii) It may be redeemed before maturity only at the option of the NBDTIs concerned and with the prior written approval of the Bank of Mauritius;
(iv) In the event of the winding up of the NBDTIs concerned, the subordinated debt shall not be repaid until the claims of depositors and other creditors have been fully satisfied; and
(v) Such further conditions as may be prescribed by the Bank of Mauritius.

During the last five years to maturity, a cumulative discount (or amortisation) factor of 20 per cent per year shall be applied to reflect the diminishing value of the subordinated debt as a continuing source of strength.

10. Associates

IAS 28 defines 'an associate' as an entity, including an unincorporated entity such as a partnership, over which the investor has significant influence and that is neither a subsidiary nor an interest in a joint venture.

If an investor holds, directly or indirectly (eg through subsidiaries), 20 per cent or more of the voting power of the investee, it is presumed that the investor has significant influence, unless it can be clearly demonstrated that this is not the case. A substantial or majority ownership by another investor does not necessarily preclude an investor from having significant influence. The existence of significant influence by an investor is usually evidenced in one or more of the following ways:

(a) Representation on the board of directors or equivalent governing body of the investee;
(b) Participation in policy-making processes, including participation in decisions about dividends or other distributions;
(c) Material transactions between the investor and the investee;
(d) Interchange of managerial personnel; or
(e) Provision of essential technical information.

11. Specific Provisions

Specific provisions for bad and doubtful debts may be deducted from the book value of the relevant exposures before weighting.

Further, portfolio and general provisions for doubtful debts in excess of the amount permitted for inclusion in Tier 2 supplementary capital, may be deducted from the book value of the relevant exposures before weighting.

12. Deductions from capital base

The following deductions should be made from Tier 1 capital:

(a) Accumulated losses;
(b) Current year's interim losses;
(c) Fully paid bonus shares issued by capitalization of property revaluation reserves;
(d) Goodwill and intangibles assets as reported in the latest audited accounts;
(e) Deferred tax assets as shown in the latest audited accounts;
(f) Investments made in subsidiaries and associates;
(g) Investments made in the equity of commercial entities; and
(h) Lending to a subsidiary and associate companies.

13. Risk Weight Assets

		Risk weight
(i)	Cash in hand	0%
(ii)	Balances with the Bank of Mauritius	0%
(iii)	Claims collateralised by cash deposits placed with the company with a legal right of set-off on the credit balances and meeting the conditions set out in these Guidelines	0%
(iv)	Claims on or guaranteed by Government of Mauritius	0%
(v)	Holdings of securities issued or guaranteed by Government of Mauritius, Treasury Bills and Bank of Mauritius Bills	0%
(vi)	Claims collateralised by securities issued or guaranteed by Government of Mauritius, Treasury Bills and Bank of Mauritius Bills and Bonds;	0%
(vii)	Claims on, or claims guaranteed or accepted or endorsed by, banks licensed under the Banking Act 2004	20%
(viii)	Mortgage Loans secured by a fixed charge on the residential property	35%

subject to the following three conditions are met

(a) Aggregate loans to an individual (natural person) (including husband and wife) does not exceed Rs 5.0 million

(b) Loan to Value (LTV) <=80%

(c) Property is subject to valuation from persons who possess the necessary qualifications, ability and experience and who are independent from the credit decision processes

(ix)	Retail Portfolio loans <=Rs 5.0 million[1] *Aggregate loans to an individual (natural person) (including husband and wife) does not exceed Rs5.0 million* Note: Where borrowers are serving/ retired civil servants to whom loans have been granted against deductions from salary/ pensions under a legal provision, a lower risk weight of 50% can be applied.	75%
(x)	Investments in Finance leases and/or Operating leases <=Rs 5.0 million *Aggregate leases to an individual or group of closely related individuals (natural persons) does not exceed Rs5.0 million*	75%
(xi)	Other exposures including loans, mortgages loans, finance and operating leases *(whatever applicable)*	100%
(xii)	Premises, real estate, furniture, fixtures, equipment, vehicles and other fixed assets including capital works in progress *(excluding operational leases)*	100%
(xiii)	All other assets not elsewhere specified *(excluding intangible assets deducted from capital)*	100%

14. Cash Collateral

[1] *For retail portfolio loans, mortgage loans meeting the conditions stipulated at (viii) need not be aggregated.*

To qualify as cash collateral:

i) the cash deposit must either be held and pledged with the reporting NBDTI or with a bank or another NBDTI on the condition that the cash deposit has been pledged in favour of the reporting NBDTI.

ii) the reporting NBDTI shall have a right of set-off over the cash deposit which is legally enforceable in a liquidation of the debtor.

In the case of an exposure partially collateralised by cash deposit only that part of the exposure which is collateralised will qualify for 0% risk-weight.

15. Set-off

Debit balances may only be offset against credit balances where all of the following criteria are met.

(i) There is formal agreement with the customer(s) to do so, or where a legal right of set-off exists. Such arrangements shall, to the best of the reporting NBDTI's knowledge, be enforceable in a bankruptcy or liquidation of the customer(s).
(ii) The debit and credit balances must relate to the same customer(s).
(iii) Both the debit and credit balances must be denominated in the same currency.
(iv) The debit and credit balances must have identical maturities.
(v) The customer(s) and the office(s) of the reporting NBDTI in whose books the debit and credit balances appear must all be domiciled in Mauritius.

16. Reporting

NBDTIs shall submit to the Bank of Mauritius a return on a quarterly basis in the prescribed format as per Annexure III. However, in order to establish the position of each company, the first return shall be as at 31 December 2009. The return shall be signed by two authorised officials of the company and shall be submitted to the Bank of Mauritius not later than 20 working days after the close of the quarter to which it relates.

Bank of MAURITIUS
1st October 2009

ANNEXURE I

Terms and Conditions for
Non-Bank Deposit Taking Institutions to conduct deposit taking business

1. NBDTI shall comply with the provisions of the banking laws when conducting their deposit taking business.

2. NBDTI shall not accept deposits repayable on demand or on notice and shall not accept deposits for original terms to maturity of less than one month and deposits shall be accepted only in a registered form.

3. NBDTI shall, at all times, maintain liquid assets equivalent to not less than 10 per cent of its deposit liabilities or such higher percentage as may be prescribed from time to time by Bank of Mauritius.

4. NBDTI shall display its deposit and lending rates and other applicable charges in a clear and prominent manner at the place(s) where it carries on its business.

ANNEXURE II

External Auditor's Report on Interim Profits

The Board of Directors (in the case of company incorporated in Mauritius)

[Name of company]

Dear Sir(s),

In accordance with your letter of instruction dated [ ], we have reviewed the current year's interim profits of [name of company] for the period [ ] as per the details attached. Our review, which did not constitute an audit, has been carried out having regard to the scope of the work the Bank of Mauritius expects external auditors to do in verifying the current year's interim profits as outlined in the Guidelines on Capital Adequacy Ratio.

On the basis of the results of our review,

(a) the interim profits as per details attached have been calculated on the basis of the accounting policies adopted by the company in preparing its latest statutory accounts for the year to ....;

(b) the specific provisions made are adequate and have been made in accordance with the requirements of the Bank's Guidelines on Impairment and Income Measurement; and

(c) the interim profits amounting to Rs ...... as so reported are reasonably stated.

Yours faithfully,

Chartered Accountants

Current year's profit and loss based on
Management accounts for the period

______________ to __________ 20

		(Rs'000)
1.	Gross earnings on finance leases	
2.	Interest Income received/receivable (including on investments)	
3.	Interest expense paid and payable	( )
4.	**Margin (1 +2-3)**	
5.	Realised profit (loss) from sale of fixed assets	
6.	Other operating income (loss)	
7.	**Gross operating income (4 to 6 inclusive)**	
8.	Staff costs	( )
9.	Depreciation and amortisation	( )
10.	Other operating expenses	( )
11.	**Net operating income (loss) (7- 8 - 9 - 10)**	
13.	Exceptional items	
14.	Bad debts recovered	
15.	Bad debts written off	( )
16.	Provision for bad debts	( )
17.	Provision for taxation	( )
18.	Provision for dividend	( )
19.	**Current year's profit (loss)**	

ANNEXURE III
Quarterly Capital Adequacy Ratio Return
as at ....
PART A
Capital Base, Weighted Risk Assets and Capital Adequacy Ratio

I. Capital Base

(Amount Rs'000)

A. Tier 1: Core Capital

(i) Stated capital
(ii) Statutory reserve
(iii) General reserve
(iv) Other disclosed free reserves, including undistributed balance in profit and loss account, created by appropriations of retained earnings (Please specify)
(v) Current year's interim retained profits subject to certification by the company's external auditors

Less: (i) Accumulated losses
(ii) Current year's interim losses
(iii) Fully paid bonus shares issued by capitalising property revaluation reserves[2]
(iv) Goodwill[3]
(v) Other intangible assets (Please specify)
(vi) Deferred tax assets as shown in the latest audited accounts;
(vii) Investments made in subsidiaries and associates*;
(viii) Investments made in the equity of commercial entities*; and
(ix) Lending to a subsidiary and associate companies*.

([2]) To be included in Tier 2 capital.

([3]) To the extent that it is carried in the balance sheet.

(*) Subject to the availability of tier II capital, up to 50% of these exposures can be deducted from tier II capital and the remaining from tier I capital.

Tier 1 capital

B. <u>Tier 2: Supplementary Capital</u>

(i) Reserves arising from revaluation
of tangible fixed assets

(ii) General provisions/Portfolio provisions/
general loan loss reserves
against unidentified losses

(iii) Subordinated debt

Tier 2 capital

C. <u>Total Capital</u>

Tier 1: Core capital

Tier 2: Supplementary capital

Total (gross) capital

Total (net) capital

II. <u>Total Risk Weighted Assets</u>

Weighted amount of on-balance
sheet assets (Part B)

III. <u>Capital Adequacy Ratio</u>[4] **%**

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[4] Divide total (net) capital by total weighted risk assets and multiply the result by 100.

PART B

Risk Weighted On-balance Sheet Assets

		Amount x (Rs'000)	Risk weight %	Weighted Amount (Rs'000)
1.	Cash in hand		0	
2.	Balances with the Bank of Mauritius		0	
3.	Claims collateralised by cash deposits placed with the company with a legal right of set-off on the credit balances and meeting the conditions set out in these Guidelines		0	
4.	Claims on or guaranteed by Government of Mauritius		0	
5.	Holdings of securities issued or guaranteed by Government of Mauritius, Treasury Bills and Bank of Mauritius Bills		0	
6.	Claims collateralised by securities issued or guaranteed by Government of Mauritius, Treasury Bills and Bank of Mauritius Bills and Bonds		0	
7.	Claims on, or claims guaranteed or accepted or endorsed by, banks licensed under the Banking Act 2004		20%	
8.	Mortgage Loans secured by a fixed charge on the residential property *subject to the following three conditions are met* *i) Aggregate loans to an individual (natural person) (including husband and wife) does not exceed Rs 5.0 million* *ii) Loan to Value (LTV) <=80%* *iii) Property is subject to valuation from persons who possess the necessary qualifications, ability and experience and who are independent from the credit decision processes*		35%	
9	Retail Portfolio loans <=Rs 5.0 million		75%	

	Aggregate loans to an individual (natural person) (including husband and wife) does not exceed Rs5.0 million			
	Note: Where borrowers are serving/ retired civil servants to whom loans have been granted against deductions from salary/ pensions under a legal provision, a lower risk weight of 50% can be applied			
10	Investments in Finance leases and/or Operating leases <=Rs 5.0 million		75%	
	Aggregate leases to an individual or group of closely related individuals (natural persons) does not exceed Rs5.0 million			
11	Other exposures including loans, mortgages loans, finance and operating leases		100%	
	(whatever applicable)			
12	Premises, real estate, furniture, fixtures, equipment, vehicles and other fixed assets including capital works in progress		100%	
	(excluding operational leases)			
13	All other assets not elsewhere specified		100%	
	(excluding intangible assets deducted from capital)			
	Total			

Notes:

(1) The risk weighting of 0% will apply only to that portion of a claim which is covered by a cash deposit or a legal right of set-off on credit balances. For example, if a loan is partly secured by a cash deposit, only the secured part of the loan can be weighted at 0%.

(2) Only claims which have been explicitly, irrevocably and unconditionally guaranteed shall be included; such guarantees shall be legally enforceable. Where a claim is partially guaranteed, only the part of the claim which is fully guaranteed shall be reported in the 0% weight.

(3) If the value of the securities held as collateral covers less than the book value of the claim, only that part of the claim which is fully covered shall be reported in the 0% weight. Securities held as collateral shall be marked to market.