S.I. 113 of 2023

FINANCIAL INSTITUTIONS ACT, 2004

(Act 14 of 2004)

Financial Institutions (Capital Adequacy) (Amendment) Regulations, 2023

Arrangement of Regulations

Regulations

S.I. 113 of 2023

FINANCIAL INSTITUTIONS ACT, 2004

(Act 14 of 2004)

Financial Institutions (Capital Adequacy) (Amendment) Regulations, 2023

In exercise of the powers conferred by section 23 read with section 32 of the Financial Institutions Act, 2004 the Central Bank of Seychelles, in consultation with the Minister of Finance, makes the following regulations —

Citation

1. These regulations may be cited as the Financial Institutions (Capital Adequacy) (Amendment) Regulations, 2023.

Amendment of regulation 2

2. Regulation 2 of the Financial Institutions (Capital Adequacy) Regulations, 2010 (S.I. 73 of 2010) in these Regulations referred to as "principal Regulations" is amended as follows —

(a) by inserting after the definition of "core capital" the following definition —

"public enterprises" means an organisation listed under the Public Enterprise Act, 2023;

(b) by repealing the definition of "risk-adjusted assets";

Amendment of regulation 3

3. Regulation 3 of the principal Regulations is amended by repealing in sub-regulation (1) the words "or offshore banking business";

Amendment of regulation 4

4. The principal Regulations is amended by repealing regulation 4(2).

Amendment of regulation 5

5. The principal Regulations are amended by repealing regulation 5 and substituting it with the following —

"Minimum Capital Ratios

5.(1) Each bank, shall maintain the following capital ratios —

(a) Capital Adequacy Ratio shall not be less than 12% where Capital Adequacy Ratio is equal to capital base divided by risk-weighted assets, expressed in percent: (capital base/risk-weighted assets)*100;

(b) Core Capital Ratio shall not be less than 6% where Core Capital Ratio is equal to tier 1 capital divided by risk-weighted assets, expressed in percent: (tier 1 capital/risk-weighted assets)*100.

(2) Risk-weighted assets shall be calculated as the sum of credit risk component, market risk component and operational risk component.

(3) In the calculation of market risk component, under sub regulation 2, the Central Bank may exempt certain components in the determination of the overall foreign currency risk exposure.

(4) In these regulations —

(a) credit risk component —

(i) shall be calculated using the following four steps —

(A) to assign risk weights to on-balance sheet assets post credit risk mitigation where applicable, in line with instructions under Schedule 2;

(B) to convert the bank's off-balance sheet items to credit equivalents by using credit conversion factors specified under Schedule 3 and to apply risk weights to the credit equivalents post credit risk mitigation where applicable;

(C) to calculate the risk-weighted value of on-balance sheet assets and off-balance sheet items by multiplying the amount of each on-balance sheet asset and off-balance sheet items by the percentage risk weight to which it was assigned; and

(D) to sum the risk-weighted values of the bank's on-balance sheet assets and off-balance sheet items.

(ii) may for, any eligible collateral or guarantee specified under Schedule 4 which secures an on-balance sheet or off-balance sheet exposure, use the credit risk mitigation requirements under schedule 4 to reduce the regulatory capital charge of the exposure.

(b) market risk component, where market risk refers to foreign currency risk, shall be calculated using the following three steps —

(i) determine the overall foreign currency risk exposure~~;~~ using the following four steps —

(A) Calculate the domestic currency equivalent of the net open position in each individual foreign currency;

(B) Calculate the sum of all short positions;

(C) Calculate the sum of all long positions;

(D) Determine the overall foreign currency risk exposure as the higher of (2) and (3); and

(ii) multiply the overall foreign currency risk exposure computed at paragraph (i) by 0.12;

(iii) multiply the result obtained in paragraph (ii) by 8.33;

(c) operational risk component shall be calculated using the following two steps —

(i) derive the bank's average annual gross income for the preceding three years using only the years with positive gross income and base the average on that number of years; and

(ii) multiply the bank's average annual gross income under paragraph (i) by 1.25;

Amendment of regulation 7

6. The principal Regulations are amended in regulations 7 by repealing in regulation 7 the words "risk-adjusted assets" and substituting them with the words "risk-weighted assets"

Insertion of a new regulation 8

7. The principal Regulations are amended by inserting after regulation 7 the following regulation —

"Power to request higher capital ratios

8. The Central Bank may require a bank to maintain higher capital ratios based on the risk profile of the bank.";

Amendment of Schedule 2

8. The principal Regulations are amended by repealing Schedule 2 and substituting it with the following new Schedule —

"SCHEDULE 2

[regulation 5(4)(a)(i) (A)]

Instructions

1. The amount of each on-balance sheet asset shall be reported net of specific provisions and interest-in-suspense.

2. Banks shall apply credit risk mitigation to an on-balance sheet asset where applicable as per Schedule 4.

3. The on-balance sheet assets after taking into account credit risk mitigation where applicable shall be assigned to the appropriate risk weights in Table 1.

4. All assets shall be assigned except for those assets which are required to be deducted from capital as per Schedule 1.

5. Where the ratings of External Credit Assessment Institutions and scores of Export Credit Agencies are to be used to determine the risk weights as per Table 1, the scores of Export Credit Agencies are only to be used if ratings of External Credit Assessment Institutions are not available. Additionally, banks will need to obtain the Central Bank's approval for use of ratings of External Credit Assessment Institutions that are not included in the Regulations. Central Bank will communicate the appropriate risk weight to the banks in relation to the ratings of such External Credit Assessment Institutions.

Table 1 - ————————————————————

Risk weight categories on-balance sheet

Description of Item	Risk Weight
1. Cash and Similar items	
(a) Cash (in domestic currency).	0%
(b) Foreign notes and coins.	0%
(c) Claims collateralised by cash deposits.	0%
(d) Cash items in the course of collection.	20%
2. Claims on Sovereigns	
(a) Claims on the Government of Seychelles and Central Bank of Seychelles denominated and funded in domestic currency	0%
(b) Minimum Reserve Requirements including excess funds above the Minimum Reserve Requirement denominated in foreign currency	0%
(c) Claims on or guaranteed by the Government of Seychelles and Central Bank of Seychelles denominated in foreign currency excluding the Minimum Reserve Requirements and excess funds above the Minimum Reserve Requirement denominated in foreign currency.	— The risk weight is determined by the external credit rating of the jurisdiction in accordance with Table 2.

(d) Claims on other sovereigns.	The risk weight is determined by the external credit rating of the jurisdiction in accordance with Table 2. Notwithstanding this, where a regulator permits banks in its jurisdiction to allocate a lower risk weight to claims on that jurisdiction's sovereign denominated in the domestic currency of that jurisdiction and funded in that currency, the same, lower risk weight may be allocated to such claims, subject to the prior written approval of the Central Bank.
3. Claims on international organisations	
(a) Claims on eligible Multilateral Development Banks. The Central Bank may provide guidance on eligibility criteria for Multilateral Development Banks to be attributed the risk weight and provide a list of eligible Multilateral Development Banks.	0%
(b) Claims on other Multilateral Development Banks.	The risk weight is determined by the external credit rating of the Multilateral Development Bank in accordance with Table 3.
(c) Claims on the Bank for International Settlements, International Monetary Fund and European Central Bank.	0%

4. **Claims on Public Enterprises**	
(a) Claims on Public Enterprises funded and denominated in domestic currency where the Public Enterprise is established by individual statute in Seychelles and has revenue raising powers.	20%
(b) Claims on Public Enterprises in Seychelles funded and denominated in domestic currency.	100%
(c) Claims on Public Enterprises denominated in foreign currency.	The risk weight is determined by the external credit rating of the jurisdiction in accordance with Table 4.
5. **Claims on banks and credit unions**	
(a) Claims on banks and credit unions funded and denominated in domestic currency.	20%
(b) Claims on banks and credit unions denominated in foreign currency.	The risk weight is determined by the external credit rating of the bank or credit union in accordance with Table 5.
6. **Claims on corporates**	
(a) Claims on corporates.	100%
7. **Retail exposures**	
(a) Claims in regulatory retail portfolio, shall be claims that meet the following criteria: (i) Orientation criterion – the exposure is to an individual person or persons;	75%

(ii) Product criterion – the exposure shall take the form of any of the following: revolving credits and lines of credit, personal term loans and leases. Mortgage loans are excluded to the extent that they qualify for treatment as claims secured by residential property; (iii) Low value of individual exposures criterion – the maximum aggregated retail exposure to one counterpart shall not exceed an absolute threshold of SCR750, 000.	
(iv) Claims falling outside the regulatory retail portfolio.	100%
8. Claims secured by residential property	
(a) Claims secured by residential property that meet the following criteria – (i) Lending is fully secured by mortgages on residential property; (ii) Residential property is occupied by the borrower or rented from the borrower; and (iii) The residential property shall be valuated in accordance to the valuation rules listed under this Schedule.	35%

(iv) The bank shall be satisfied that the risk of the borrower is not solely dependent on the performance of the underlying property serving as collateral but rather the capacity of the borrower to repay the debt from other sources.	
(b) Other claims secured by residential property.	50%
9. Claims secured by commercial real estate	
(a) Claims secured by commercial real estate.	100%
10. **Claims on securities firms**	
(a) Claims funded and denominated in domestic currency on securities firms that are subject to supervisory and regulatory arrangements comparable to that applicable to banks.	20%
(b) Claims denominated in foreign currency on securities firms that are subject to supervisory and regulatory arrangements comparable to that applicable to banks.	The risk weight is determined by the external credit rating assigned to the securities firm in accordance with Table 5.
(c) Claims on securities firms that are not subject to supervisory and regulatory arrangements comparable to that applicable to banks.	100%
11. **Past-due loans**	
(a) The secured portion of a past due loan.	The risk weight is determined in accordance with the risk weight attributed to the recognised credit risk mitigant.

(b) The unsecured portion of a past-due loan when specific provisions are no less than 20% of the outstanding amount of the loan, except for qualifying residential mortgages.	100%
(c) The unsecured portion of a past-due loan, when specific provisions are less than 20% of the outstanding amount of the loan, except for qualifying residential mortgages.	150%
(d) A qualifying residential mortgage that is past due for more than 90 days net of specific provisions.	100%
12. **Other balance sheet exposures**	
(a) Tangible fixed assets.	100%
(b) High risk assets.	150%
(c) Other assets.	100%

Valuation Rules

(Item 8(a)(iii)-)

(1) The bank shall have appropriate governance arrangement to ensure that valuations are reliable and carried out regularly.

(2) The valuation shall be carried out by a person who possesses the necessary qualifications, ability and experience and who is independent from the credit decision process.

(3) Where the Central Bank of Seychelles finds that the valuation is not reliable, the Central Bank may instruct the bank to appoint an independent expert to conduct the revaluation the cost of which shall be borne by that bank.

(4) Notwithstanding paragraph 3 the Central Bank of Seychelles may in specific circumstances instruct the bank to do a revaluation.

Table 2-Risk weights for claims on sovereigns in currency other than their local currency

(1) Credit assessment of Standard and Poor's Ratings/Fitch Ratings	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	Below B-	Unrated
(2) Credit assessment of Moodys Investors Service .	Aaa to Aa3	A1 to A3	Baa1 to Baa3	Ba1 to B3	Below B3	Unrated
(3) Consensus risk scores of Export Credit Agencies (Arrangement of Officially Supported Exports Credits).	0-1	2	3	4-6	7	
(4) Risk weights.	0%	20%	50%	100%	150%	100%

Table 3: Risk weights for claims on Multilateral Development Banks

(1) Credit assessment of Standard and Poor's Ratings/Fitch Ratings.	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	Below B-	Unrated
(2) Credit assessment of Moodys Investors Service.	Aaa to Aa3	A1 to A3	Baa1 to Baa3	Ba1 to B3	Below B3	Unrated
(3) Risk weights.	20%	50%	50%	100%	150%	50%

Table 4: Risk weights for foreign currency denominated exposures to Public Enterprises

(1) Credit assessment of Standard and Poor's Ratings/Fitch Ratings.	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	Below B-	Unrated
(2) Credit assessment of Moody's Investor's Service.	Aaa to Aa3	A1 to A3	Baa1 to Baa3	Ba1 to B3	Below B3	Unrated
(3) Risk weights.	20%	50%	100%	100%	150%	100%;

Table 5: Risk weights for foreign currency denominated exposures to banks, credit unions and securities firms subject to the same regulatory and supervisory arrangement as banks

(1) **Credit assessment of - Standard and Poor's Ratings/Fitc h Ratings**	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	Below B-	Unrated
(2) Credit assessment of Moody's Investor's Service.	Aaa to Aa3	A1 to A3	Baa1 to Baa3	Ba1 to B3	Below B3	Unrated
(3) Risk weight	20%	50%	50%	100%	150%	50%
(4) Risk weights for short-term claims	20%	20%	20%	50%	150%	20% ;

Note:

1. ***Short-term claims are defined as having an original maturity of three months or less.***
2. ***Claims with (contractual) original maturity under 3 months which are expected to be rolled over (that is where the effective maturity is longer than 3 months) shall not qualify for this preferential treatment for capital adequacy purposes.***
3. ***No claim on an unrated bank, unrated credit union or unrated securities firm subject to supervisory and regulatory arrangements comparable to that applicable to banks, may receive a risk weight lower than that applied to claims on its sovereign of incorporation.***

Amendment of Schedule 3

9. The principal Regulations are amended by repealing Schedule 3 and substituting it with the following new Schedule —

"SCHEDULE 3

[regulation 5(4)(a)(i) (B)]

CREDIT CONVERSION FACTOR FOR OFF-BALANCE SHEET ITEMS

Instructions

(1) Banks shall assign their off-balance sheet risks to one of the credit conversion categories in Table 1.

(2) The amount of each off-balance sheet risk is multiplied by the credit conversion factor for the category to which it was assigned.

(3) Banks shall apply credit risk mitigation to the resulting credit equivalent where applicable as per Schedule 4.

(4) The resulting credit equivalents, after taking into account credit risk mitigation where applicable, shall be assigned to the appropriate risk weight as per Table 1 under Schedule 2.

(5) The appropriate risk weight for instruments under Table 1, are determined by reference to the risk weight allocated to the counterparty of the exposure, with the exception of the following —

(a) Sale and repurchase agreements;

(b) Asset sales with recourse;

(c) Forward asset purchases;

(d) Forward deposits placed;

(e) The unpaid part of partly paid-up shares and securities.

The risk weights for instruments (a) to (e) are to be determined by reference to the risk weights of the underlying assets.

Table 1: Credit Conversion Factor for Off Balance Sheets Items

Instruments	Credit conversion factor
(1) Direct credit substitutes, including general guarantees of indebtedness, standby letters of credit serving as financial guarantees, acceptances and endorsements.	100%
(2) Sale and repurchase agreements and assets sales with recourse where the credit risk remains with the bank	100%
(3) Forward asset purchases, forward deposits placed and the unpaid part of partly-paid shares and securities any other commitments with a certain drawdown.	100%
(4) Transaction-related contingent items not having the character of direct credit substitutes (for example performances bonds, bid bonds, warranties and standby letters of credit related to particular transactions).	50%

(5)	Note issuance facilities and revolving underwriting facilities to be applied to the total amount of the institution's underwriting obligations of any maturity. Where the facility has been drawn down by the borrower and the notes are held by anyone other than the reporting institution, its underwriting obligations shall continue to be reported as the full nominal amount. (Own holdings of notes underwritten are, however, deducted from the overall value of the commitment, because they are weighted as an on-balance sheet item).	50%
(6)	Other commitments (example formal standby facilities and credit lines) with an original maturity of over 1 year.	50%
(7)	Short-term self-liquidating trade-related contingent items (for example documentary credits collateralised by the underlying shipments).	20%
(8)	Commitments with an original maturity of up to 1 year.	20%
(9)	Uncommitted and cancellable credit lines. Commitments that are unconditionally cancellable by the bank without any prior notice and that provide for automatic cancellation due to deterioration of the borrower's credit-worthiness.	0%";

Inserting a new Schedule 4

10. The principal Regulations are amended by inserting immediately after Schedule 3 the following new Schedule 4 —

“SCHEDULE 4

[regulation 5(4)(a)(ii)]

Credit risk mitigation requirements

The credit risk mitigation techniques that shall be recognised are use of collaterals (the simple approach) and guarantees.

1. **General requirements**

Transactions in which the credit risk mitigation techniques are used shall not receive a higher capital requirement than an otherwise identical transaction where such techniques are not used.

2. **Minimum requirements relating to legal certainty for recognition of credit risk mitigation techniques**

Banks shall meet the following minimum standards for legal documentation to qualify for capital relief for any use of credit risk mitigation techniques —

(a) All legal documents relating to credit risk mitigation shall be binding on all relevant parties and legally enforceable in all relevant jurisdictions;

(b) Banks shall conduct sufficient legal reviews to verify and ensure that all documentation used in collateralised transactions and for documenting guarantees are binding on all relevant parties and legally enforceable in all jurisdictions and shall ensure that they have a well-founded legal basis to reach this conclusion and undertake such further review as necessary to ensure continuing enforceability.

3. **Guarantees**

(1) A guarantee is an undertaking by a third party (the guarantor) to meet the obligation in event of the default of the party primarily (the bank's obligor) responsible for that obligation.

(2) The amount of the bank's exposure, on a risk-weighted basis, may be reduced if the guarantor's credit quality is higher than the obligation being guaranteed.

(a) ***Requirements for recognition of guarantor***

The following requirements shall be met for recognition of guarantor as a credit risk mitigant in addition to the minimum requirements for legal certainty —

(i) The credit protection shall represent a direct claim on the guarantor and shall be explicitly referenced to exposures or a pool of exposures, so that the extent of the cover is clearly defined and incontrovertible.

(ii) The credit protection contract shall be irrevocable, that is, shall not contain any clause that may allow the guarantor to unilaterally cancel the protection.

(iii) The credit protection contract shall not contain any clause, fulfillment of which is outside the direct control of the lending bank, which may have one of the following effects —

(A) increase the effective cost of the protection as a result of deteriorating credit quality of the protected exposure; or

(B) prevent the guarantor from being obliged to pay out in a timely manner in the event the original borrower fails to make any payment due (unconditional).

(C) Where there is a default of the counterparty, the bank shall have the right to recoup, in a timely manner, any claim due under the guarantee. The lending bank shall have the right to receive any such payment from the guarantor without first having to take legal actions in order to pursue the guarantor for payment.

(D) The guarantee shall cover all payments the borrower is required to make in respect to the claim. Where certain types of payments are excluded from the guarantee, the recognised value of the guarantee shall be adjusted to reflect the limited coverage.

(iv) The guarantee shall be an explicitly documented obligation assumed by the guarantor.

(b) ***Eligible guarantors***

(i) Sovereign entities, multilateral development banks, Public Enterprises, banks and securities firms with a lower risk weight than the counterparty.

(ii) Other entities rated A- or better. This would include credit protection provided by parent, subsidiary and affiliate companies when they have a lower risk weight than the obligor.

(c) ***Treatment of guarantees***

The portion of the claim that is supported by the eligible guarantee, shall be weighted according to the risk weight of the guarantor (unless the risk weight of the original counterparty is lower). The unsecured portion of the claim shall be weighted according to the risk weight applicable to the original counterparty.

4. **Collaterals**

(1) A collateralised transaction is one in which banks have a credit exposure or potential credit exposure and that credit exposure or potential credit exposure is hedged in whole or in part by

collateral posted by a counterparty or by a third party on behalf of the counterparty.

(2) Where banks take eligible financial collateral, they are allowed to reduce their credit exposure to a counterparty when calculating their capital requirements to take account of the risk mitigating effect of the collateral.

(3) Requirements for recognition of collateral

The following requirements shall be met for recognition of collateral as a credit risk mitigant in addition to the minimum requirements for legal certainty —

(a) The collateral shall be pledged for the life of the exposure and it shall be marked to market and revalued with a minimum frequency of 6 months. The Central Bank may exempt banks from this requirement in relation to certain collaterals as specified in guidelines.

(b) The credit quality of the counterparty and the value of the collateral shall not have a material positive correlation.

(c) The legal mechanism by which collateral is pledged or transferred shall ensure that the bank has the right to liquidate or take legal possession of the collateral, in a timely manner, in the event of the default, insolvency or bankruptcy of the counterparty (or defined credit events set out in the transaction documentation).

(d) Banks shall have clear and robust procedures for the timely liquidation of collateral to ensure that any legal conditions required for declaring the default of the counterparty and liquidating the collateral are observed, and that collateral can be liquidated promptly.

(e) Where the collateral is held by a custodian, the bank shall take reasonable steps to ensure that the custodian segregates the collateral from its own assets.

(4) Eligible collateral

(a) Cash on deposit with the bank which is incurring the counterparty exposure.

(b) Debt securities issued and guaranteed by the Government of Seychelles and the Central Bank of Seychelles.

(c) Debt securities rated by an External Credit Assessment Institution where these are either:

(i) at least BB-when issued by Sovereigns or Public Enterprises that are treated as Sovereigns by the national supervisor;

(ii) at least BBB-when issued by other entities (including banks and securities firms); or

(d) Debt securities not rated by an External Credit Assessment Institution where these are:

(i) issued by a bank;

(ii) listed on a recognised exchange;

(iii) classified as senior debt;

(iv) all rated issues of the same seniority by the issuing bank shall be rated at least BBB- by a recognised External Credit Assessment Institution;

(v) the bank holding the securities as collateral has no information to suggest that the issue justifies a rating below BBB; and

(vi) the supervisor is sufficiently confident about the market liquidity of the debt securities.

(5) Treatment of collateral

(a) The portion of claims collaterised by the market value of eligible collateral shall receive the risk weight attributable to the collateral, subject to a floor of 20% except under certain conditions. The remainder of the claim shall be assigned the risk weight appropriate to the counterparty.

(b) For the exception to the 20% floor, risk weight of 0% may be assigned to collateralised transactions where the exposure and the collateral are denominated and funded in the same currency, and either —

(i) the collateral is cash on deposit; or

(ii) the collateral is in the form of sovereign securities and central bank's securities eligible for a risk weight of 0% and the market value of the collateral has been discounted by 20%.

5. **Treatment of pools of credit risk mitigation techniques**

Where a bank has multiple credit risk mitigation techniques covering a single exposure, (for example a bank has both collateral and guarantee partially covering an exposure), the bank shall be required to subdivide the exposure into portions covered by each type of credit risk mitigation technique (for example portion covered by collateral, portion covered by guarantee) and the risk-weighted assets of each portion shall be calculated separately."

MADE this 27th day of December, 2023.

CAROLINE ABEL
GOVERNOR
CENTRAL BANK OF SEYCHELLES