Banking Supervision Dept.

مؤسسة النقد العربي السعودي
الرقم: 361000067330
التاريخ: 1436/05/07
المرفقات: ٢٢

From	:	Saudi Arabian Monetary Agency
To	:	All Banks
Attention	:	Managing Directors, Chief Executive Officers and General Managers
Subject	:	**Rules on Large Exposures of Banks**

These Rules are aimed at diversification of the credit portfolio of banks, containing the maximum loss emanating from large exposures to single counterparties or groups of connected counterparties and ensuring broader access to credit for the economic development of the Kingdom. These Rules are being issued by SAMA under its Charter issued by the Royal Decree No.23 on 23-05-1377H (15 December 1957G) and the Banking Control Law issued by the Royal Decree No. M/5 on 22-02-1386H (11 June 1966G) and the rules for Enforcing its Provisions issued by Ministerial Decision No 3/2149 on 14/10/1406H.

These Rules shall come into force with effect from 1st July 2015 and shall supersede the existing SAMA rules regarding Limits on Credit Exposures issued vide SAMA Circular of June 1994.

Abdulaziz S. Alfuraih
Vice Governor

Encl: As above.

P. O. Box 2992 - Riyadh 11169, Saudi Arabia - Tel.: 01-463 3000 - Telex 404390 SJ - Fax 01-466 2119

Saudi Arabian Monetary Agency

Rules on Large Exposures of Banks

February 2015

Table of Contents

Contents **Page No.**

Rules on Large Exposures of Banks

1. General Requirements:

1.1. Introduction:

These Rules are issued by Saudi Arabian Monetary Agency (SAMA) in exercise of the powers vested upon it under its Charter issued by the Royal Decree No.23 on 23-05-1377H (15 December 1957G) and the Banking Control Law issued by the Royal Decree No. M/5 on 22-02-1386H (11 June 1966G) and the rules for Enforcing its Provisions issued by Ministerial Decision No 3/2149 on 14/10/1406H.

These Rules set out the minimum requirements on large exposures including the limits on a bank's exposures to single counterparties, groups of connected counterparties and related counterparties as well as the types of exposures to be included in or excluded from those limits, and the regulatory reporting requirements for large and connected exposures.

These Rules shall supersede the existing SAMA rules regarding Limits on Credit Exposures issued vide SAMA Circular of June 1994.

1.2. Definitions:

The following terms and phrases, where used in these Rules, shall have the corresponding meanings, unless the context requires otherwise:

i. ***SAMA:*** the Saudi Arabian Monetary Agency.

ii. ***Rules:*** Rules for Large Exposures of banks.

iii. ***Subsidiary:*** includes a subsidiary where a bank owns more than 50% of its shareholding.

iv. ***Exposure:*** includes both on and off-balance sheet exposures included in either the banking or trading books, and instruments with counterparty credit risk under the Basel risk-based capital framework. Banking and trading books have the same meaning as under the Basel risk-based capital framework.

v. ***Large Exposure:*** if the sum of all exposure values of a bank to a counterparty or to a *Group of Connected Counterparties* is equal to or above 10% of the bank's eligible capital base. The exposure values have to be measured and eligible capital base calculated as per requirements set out under these Rules.

vi. ***Eligible Capital Base:*** is the effective amount of Common Equity Tier 1 capital fulfilling the criteria defined in Part 1 of the Basel III framework.

vii. ***Control Relationship:*** the ability to influence the actions or decisions of another person whether directly or indirectly. Control relationship will be deemed to exist automatically if one entity owns more than 50% of the voting rights of another entity. In addition, banks must assess the connectedness between counterparties based on control or beneficial ownership, using the following criteria:

a. Voting agreements (e.g. control of a majority of voting rights pursuant to an agreement with other shareholders);

b. Significant influence on the appointment or dismissal of an entity's administrative, management or supervisory body, such as the right to appoint or remove a majority of members in those bodies, or a majority of members have been appointed solely as a result of the exercise of an individual entity's voting rights;

c. Significant influence on senior management, e.g. an entity has the power, pursuant to a contract or otherwise, to exercise a controlling influence over the management or policies of another person (e.g. through consent rights over key decisions);

Banks are also expected to refer to criteria specified in appropriate internationally recognized accounting standards for further qualitatively based guidance when determining control.

viii. ***Economic Interdependence:*** Connectedness of counterparties based on economic interdependence will be established by banks only in cases where both/all potentially connected exposures are individually in excess of 5% of the bank's eligible capital base and if, one of the following qualitative criteria, is met:

a. Where 50% or more of one counterparty's gross receipts or gross expenditures (on an annual basis) is derived from transactions with the other counterparty (e.g. the owner of a residential/commercial property and the tenant who pays a significant part of the rent);

b. One counterparty has fully or partially guaranteed the exposure of the other counterparty, or is liable by other means, and the exposure is so significant for the guarantor that it is likely to default if a claim occurs. However, the guarantors will only be considered for eceonomic interdependence where the value of the guarantee exceeds 5% of the bank's eligible capital;

c. A significant part of the counterparty's production/output is sold to another counterparty, which cannot easily be replaced by other customers;

d. When the expected source of funds to repay each loan one counterparty makes to another is the same and the counterparty does not have another source of income from which the loan may be fully repaid;

e. Where it is likely that the financial problems of one counterparty would cause difficulties for the other counterparties in terms of full and timely repayment of liabilities;

f. Where the insolvency or default of one of them is likely to be associated with the insolvency or default of the other(s);

g. When two or more counterparties rely on the same source for the majority of their funding and, in the event of the common provider's default, an alternative provider cannot be found. In this case, the funding problems of one counterparty are likely to spread to another due to a one-way or two-way dependence on the same main funding source.

Banks will be required to demonstrate to SAMA that a counterparty who is economically closely related to another counterparty may overcome financial difficulties or even the second counterparty's default by finding alternative business partners or funding sources within an appropriate time period, and thus the bank does not need to combine these counterparties to form a group of connected counterparties despite meeting some of the above criteria.

ix. ***Group of Connected Counterparties:*** Two or more natural or legal persons shall be deemed a group of connected counterparties if at least one of the following criteria is satisfied:

a. *The existence of Control Relationship; or*
b. *The existence of Economic interdependence.*

The bank shall assess the relationship amongst counterparties with reference to (a) and (b) above in order to establish the existence of a group of connected counterparties.

x. ***Related Party:*** any party that the bank exerts control over or that exerts control over the bank, including, inter-alia, the following:

a. Members of Board of Directors, Key Executives/members of Senior Management, Major Shareholders and External Auditors of the Bank and their dependent family members;
b. Un-incorporated establishments in which any Director, External Auditor, Major Shareholder, or Key Executive/member of Senior Management of the Bank or any of their dependent family member is a partner or manager or is a shareholder holding more than 5% of the shares or is a guarantor;

c. Affiliated or Associated companies and partnerships: These include establishments that are connected to the Bank by a common parent or a controlling shareholder.

xi. ***Major Shareholder:*** A person, who directly or indirectly owns, controls or has power to vote more than 5% of the voting shares of the bank granting the facility.

xii. ***Entities Connected with Saudi Government:*** includes public sector entities treated as sovereigns under the Basel risk-based capital framework. However, any commercial undertakings majority owned by Saudi government will be treated as normal commercial entities and therefore be subject to the exposure limits under these Rules.

xiii. ***Dependent Family Members:*** means first-degree relatives including parents, spouse and offspring.

1.3. Objectives of the Rules:

The main objectives of these Rules are to enable banks:

i. To contain the maximum loss a bank could face in the event of a sudden default or failure of a counterparty;
ii. To manage credit concentration risk emanating from concentrated exposures to single counterparties or groups of connected counterparties, through diversification of credit portfolio;
iii. To put in place a large exposures framework which complements and serves as a backstop to the risk-based capital requirements;
iv. To deal effectively with large exposures so as to contribute to the stability of the financial system; and
v. To ensure broader access to credit for the economic development of the Kingdom.

2. Scope and Level of Application:

2.1. Institutional Coverage:

These Rules shall be applicable to the following institutions:

i. All Locally incorporated banks licensed and operating in the Kingdom of Saudi Arabia;
ii. All majority owned Subsidiary(ies) of locally incorporated banks operating in the financial sector;
iii. All foreign branches of locally incorporated banks;
iv. Branches of foreign banks operating in the Kingdom

While applying the Rules to their subsidiaries and branches, the banks shall also take into account the legal and regulatory requirements of the concerned regulatory authorities.

When implementing the Rules, Branches of foreign banks operating in the Kingdom are only required to put in place internal policies to ensure a reasonable diversification of their exposures, and to report their 50 largest exposures as per reporting requirements under Section 7 of these Rules.

2.2. Level of Application:

These Rules shall be applicable on a consolidated as well as a standalone basis. While applying the Rules at consolidated level, a bank must consider all exposures to third parties across the relevant regulatory consolidation group and compare the aggregate of those exposures with the group's eligible capital base.

2.3. Scope of Counterparties:

A bank must consider exposures to any counterparty to comply with the exposure limits unless a specific exemption to any exposure is granted under these Rules.

The only exposures to certain counterparties that are exempted from the application of these Rules are exposures to Saudi government, SAMA and *Entities Connected with Saudi Government*, GCC and OECD central governments and their central banks, intra-group and intraday interbank exposures which are exempted to the extent specified under Section 4.3 of these Rules.

3. Maximum Exposure Limits:

3.1. Exposure Limits:

All banks are required to ensure compliance of the following exposure limits:

i. ***Single Counterparty:*** The sum of all the exposures values a bank has to a single non-bank counterparty (excluding individuals and sole proprietorships) must not be higher than 15% of the bank's available eligible capital base at all times. However, the banks will regularize their existing exposures to meet this requirement within the following transition period:

Effective From:	*Existing Exposure to be reduced to:*
1st January 2016	23% of eligible capital base
1st January 2017	21% of eligible capital base
1st January 2018	18% of eligible capital base
1st January 2019	15% of eligible capital base

ii. *Group of Connected Counterparties:* The sum of all the exposures values a bank has to a group of connected non-bank counterparties must not be higher than 15% of the bank's available eligible capital base at all times. where an individual/sole proprietorship/partnership is included within a *Group of Connected Counterparties,* the exposure limit specified under Section 3.1(iii) below shall also be applicable, in addition to the overall group exposure limit. However, the banks will regularize their existing exposures to meet these requirements as per the transition period prescribed under Section 3.1 (i) above and Section 3.1(iii) below. Furthermore, the sum of a bank's exposures to the entities included within a group of connected counterparties will also be subject to the regulatory reporting requirements as specified under Section 7 of these Rules.

iii. ***Individuals/Sole proprietors/Partnerships:*** The sum of all the exposures values a bank has to an individual or a sole proprietorship or a partnership must not be higher than 5% of the bank's available eligible capital base at all times. However, the banks will regularize their existing exposures to meet this requirement within the following transition period:

Effective From:	***Existing Exposure to be reduced to:***
1st January 2016	16% of eligible capital base
1st January 2017	12% of eligible capital base
1st January 2018	8% of eligible capital base
1st January 2019	5% of eligible capital base

iv. ***Banks:*** The sum of all the exposures values a bank has to another bank must not be higher than 25% of the lending bank's available eligible capital base at all times.

v. ***Related Counterparty:*** The sum of all the exposure values a bank has to a non-bank Related Counterparty must not be higher than 10% of the bank's available eligible capital base at all times. However, a bank may have exposure to its non-banking subsidiary in financial sector of upto 25% of the bank's eligible capital. Any existing exposure in excess of this limit of 25% will be proportionately reduced by one-fourth every calendar year over the next four years so as to fully regularize the position by 31st December 2018. Furthermore, a cumulative limit on all exposures to non-bank related counterparties shall be 50% of the bank's eligible capital.

vi. ***Aggregate Large Exposures:*** The aggregate of all Large Exposures shall not exceed 6 times of the bank's eligible capital.

3.2. Measurement of Exposures and Capital Base:

The exposures must be measured as specified in Section 4 of these Rules. The Eligible Capital Base is the effective amount of Common Equity Tier 1 capital fulfilling the criteria defined in Part 1 of the Basel III framework.

3.3. Breaches of Limits:

Any breaches of the exposure limits, which must be regarded as an exceptional events, must be communicated immediately to SAMA and must be rapidly rectified. Furthermore, any such breaches may attract punitive supervisory action depending upon their materiality.

4. <u>Measurement of Exposures Values:</u>

4.1. General Measurement Principles:

Banks shall adhere to the following principles in measuring the values of exposures:

i. The exposure values to be considered for identifying large exposures to a counterparty are all those exposures defined under the risk-based capital framework. Accordingly, banks must consider both on and off-balance sheet exposures included in either the banking or trading books, and instruments with counterparty credit risk under the risk-based capital framework;

ii. In case the counterparty is part of a *Group of Connected Counterparties*, the values of exposures to all individual counterparties within a group of connected counterparties must be aggregated;

iii. The Credit Risk Mitigation(CRM) techniques, except cash margins as allowed under Section 6(iv), are not eligible to reduce exposure values for the purposes of these Rules;

iv. An exposure to a counterparty that is deducted from capital must not be added to other exposures to that counterparty for the purpose of the large exposures limit. This general approach does not apply where an exposure is 1,250% risk-weighted. When this is the case, this exposure must be added to any other exposures to the same counterparty and the sum subject to the large exposures limit, except if this exposure is specifically exempted for other reasons.

4.2. Treatment of Specific Measurement Issues:

While determining the exposures values for the purposes of these Rules, the following specific issues will be dealt with as per the guidance provided in the BCBS Document titled "Supervisory framework for measuring and controlling large exposures" issued in April 2014 (available at www.bis.org):

i. Definition of Exposure values:
   a. Banking book on-balance sheet non-derivative assets;
   b. Banking book and trading book OTC derivatives (and any other instrument with counterparty credit risk);
   c. Securities financing transactions;
   d. Banking book "traditional" off balance sheet commitments;

ii. Trading Book Positions:
   a. Calculation of exposure value for trading book positions;
   b. Offsetting long and short positions in the trading book;

iii. Covered bonds (only if such bonds are issued in any of the GCC or OECD countries);

iv. Collective investment undertakings, securitizations vehicles and other structures;

v. Exposures to central counterparties.

4.3. Exposures Exempted from Exposure Limits:

The following exposures shall be exempt from the large exposure limits specified under these Rules:

i. ***Sovereign exposures and entities connected with Saudi government:*** Banks' exposures to Saudi government, SAMA, *Entities Connected with Saudi Government,* GCC and OECD central governments and their central banks will be exempt from exposure limits, as under:
   a. Any exposure directly taken to Saudi government, SAMA and any of the *Entities Connected with Saudi Government*;
   b. Any portion of an exposure guaranteed, or secured by financial instruments issued by Saudi government or SAMA;
   c. Any exposure to the GCC and OECD central governments and their central banks;
   d. Any entity falling within the scope of the above sovereign exemption will not be taken into account when determining whether two (or more) entities that are in scope must be connected to form a *Group of Connected Counterparties* (i.e. if two entities that are in the scope of the framework, which are otherwise not connected, are controlled by or economically dependent through an exempted entity they need not be connected);
   e. Any exposure to an exempted entity which is hedged by a credit derivative, will be recognized as an exposure to the counterparty providing the credit protection notwithstanding the fact that the original exposure is exempted;
   f. All exposures that are subject to the sovereign exemption under this Section must be reported under the regulatory reporting requirements if these exposures meet the minimum reporting threshold.

ii. ***Interbank exposures*:** All intraday interbank exposures will not be subject to the large exposures limits, neither for reporting purposes nor for application of the large exposure limits. However, all non-intraday interbank exposures will be subject to the large exposure limits;

iii. ***Intra-group exposures:*** All exposures to intra-group entities of the concerned bank, excluding the non-banking subsidiaries in the financial sector, will not be subject to the large exposures limits provided that such entities are included in the scope of accounting consolidation of the bank. However, the non-banking subsidiaries in the financial sector will be subject to the exposure limit of 25% of the bank's eligible capital as specified under Section 3.1(v) of these Rules.

All other exposures of a bank, not specifically listed above as exempted, including covered bonds issued in any of the countries other than GCC and OECD countries, must be fully subject to the large exposure limits.

5. Exposures to Related Counterparties:

Banks shall also ensure compliance of the following requirements, in addition to the exposure limits under Section 3.1(v), while taking any exposure to a related counterparty:

i. Exposures to related parties shall only be considered on arm's length basis and without any preferential treatment. Furthermore, any such credit exposures should also be strictly in line with the bank's credit policy and procedures;

ii. Any exposure to a related party should be approved at the level of Board of Directors. While considering any proposal of lending to a Board member or any of his connected party, the Board of Directors shall ensure that the concerned Board member would neither participate in the discussion nor influence such a decision;

iii. Banks should institute procedures to prevent the beneficiaries of any credit exposure being part of the processing or approval of such exposure;

iv. Any facilities granted by a bank to its key executives/members of senior management as a part of their employment contract/compensation package shall be exempt from the application of these rules.

6. Additional Requirements:

While ensuring compliance with the exposure limits under these Rules, the banks shall also meet the following additional requirements:

i. The exposure limits under these Rules shall be calculated based on the *Eligible Capital Base* as disclosed in the latest published quarterly financial statements of the bank;

ii. The exposure limits specified under these Rules are the maximum and within such limits, each bank can set lower exposure limits as a part of its Credit Policy. Banks are required to introduce adequate internal systems and controls to closely monitor on daily basis all large exposures and ensure compliance with the specified limits;

iii. Banks shall include appropriate clauses in their respective credit Policies on the management and control of large exposures;

iv. Banks shall measure, monitor, and report all exposures at gross values net of cash margins as no netting/reduction is permitted for any other collateral/CRM technique supporting the exposure or for reciprocal exposures with other banks and financial institutions. However, the cash margins for foreign exchange and other derivative transactions shall be taken into account for reducing the related exposures only if such cash margins are maintained in the same currency as the exposure and in the same jurisdiction where the exposure is booked.

7. Regulatory Reporting:

Banks are required to submit to SAMA the following information on their exposures before and after application of the credit risk mitigation techniques, on quarterly basis:

i. All Large Exposures (before application of the credit risk mitigation techniques) along-with the ratio of the aggregate of all such Large Exposures with the bank's eligible capital, on the prescribed format attached as Appendix-I;

ii. All Large Exposures (after application of the credit risk mitigation techniques) along-with the ratio of the aggregate of all such Large Exposures with the bank's eligible capital, on the prescribed format attached as Appendix-II;

iii. All the exempted exposures with values equal to or above 10% of the bank's eligible capital, on the prescribed format attached as Appendix-I & II;

iv. Their largest 50 exposures to counterparties, irrespective of the values of these exposures relative to the bank's eligible capital base, on the prescribed format attached as Appendix-III;

v. All exposures that exceeded the exposure limits specified under these Rules during the reporting quarter even if regularized subsequently, on the prescribed format attached as Appendix-IV;

vi. All exposures to Related counterparties that exceed 5% of its eligible capital base on the reporting date, on the prescribed format attached as Appendix-V.

The above information shall be submitted to the Agency starting from the quarter ending 30th September, 2015 and each calendar quarter thereafter, within 30 calendar days of the end of each quarter.

8. Implementation:

All banks are required to institute necessary policies and procedures to ensure compliance of these Rules. SAMA will monitor compliance of these Rules through its off-site monitoring and on-site inspection processes.

9. Sanctions

Where an offence has occurred, SAMA can impose any one or more of the sanctions stipulated in Article (22) and (23) of the Banking Control Law.

10. Effective Date:

These Rules shall come into force with effect from 1st July 2015. Banks are required to ensure compliance of these Rules while taking any new exposure or renewing existing exposures after the effective date. Furthermore, the information required under Section 7 of these Rules shall be submitted to the Agency starting from the quarter ending 30th September, 2015 and each quarter thereafter, within **30** days of the end of each calendar quarter. In case there are any practical issues in implementation of these Rules, banks should approach SAMA to seek further guidance on addressing such issues.

****

Appendix-I

Name of the Bank: _______________

Statement for the Quarter ended ________

M-18A

Statement Showing Large Exposures to Single and Group of Connected Counterparties
(before application of the credit risk mitigation techniques)

(All amounts are in SR thousands)

SR. No.	Name and Location of Borrower	Total value of Gross Exposure			Ratio of Gross Exposure to Bank's Eligible Capital	Whether exempted from Exposure Limits (Yes or No)	In Case of Exempted Exposures, State Reasons for Exemption	Remarks (if any)
		On Bal. Sheet	Off Bal. Sheet	Total				
1	2	3	4	5 (=3+4)	6	7	8	9
A. Aggregate of all Large Exposures								
B. Aggregate of Exempted Large Exposures								
C. Net Large Exposures (A - B)								
D. Ratio of Net Large Exposures to Bank's Eligible Capital								

Appendix-II

Name of the Bank: ______________
Statement for the Quarter ended ________

M-18B

Statement Showing Large Exposures to Single and Group of Connected Counterparties
(after application of the credit risk mitigation techniques)

(All amounts are in SR thousands)

SR. No.	Name and Location of Borrower	Total value of Gross Exposure	Value of Eligible Credit Risk Mitigates(CRM)			Net Value of Exposure	Ratio of Net Exposure to Bank's Eligible Capital	Whether exempted from Exposure Limits (Yes or No)	In Case of Exempted Exposures, State Reasons for Exemption	Remarks (if any)
			Cash Margins	Other Eligible CRM	Total					
1	2	3	4	5	6 (=4+5)		7	8	9	10

A. Aggregate of all Net Large Exposures
B. Aggregate of Exempted Net Large Exposures
C. Aggregate of Large Exposures Net of CRM (A - B)
D. Ratio of Aggregate Large Exposures net of CRM to Bank's Eligible Capital

Appendix-III

Name of the Bank: ______________

Statement for the Quarter ended ________

M-18C

Statement Showing Largest 50 Exposures to Counterparties

(All amounts are in SR thousands)

SR. No.	Name and Location of Borrower	Total Amount of Gross Exposure			Value of Eligible Credit Risk Mitigates(CRM)	Net Exposure	Ratio of Net Exposure to Bank's Eligible Capital	In Case of Exempted Exposures, State Reasons for Exemption
		On Bal. Sheet	Off Bal. Sheet	Total				
1	2	3	4	5 (=3+4)	6	7 (=5-6)	8	9
Total								
A. Aggregate of all Largest 50 Exposures								
B. Ratio of Aggregate Largest 50 Exposures to Bank's Eligible Capital								

Appendix-IV

Name of the Bank: _______________
Statement for the Quarter ended ________

M-19A

Statement Showing Exposures that Exceeded the Specified Exposure Limits during the Reporting Month

(All amounts are in SR thousands)

SR. No.	Name and Location of Borrower	Total Value of Gross Exposure On Reporting Date			Total Value of Exposure on Date of Breach	Original Date of Breach	Date of Regularization	Reasons for Breach	Remarks (if any)
		On Bal. Sheet	Off Bal. Sheet	Total					
1	2	3	4	5 (=3+4)	6	7	8	9	10
Total									

Appendix-V

Name of the Bank: ______________
Statement for the Quarter ended ________

M-19B

Statement Showing Exposures to Related Counterparties that Exceeded 5% of Bank's Eligible Capital Base

(All amounts are in SR thousands)

SR. No.	Name and Location of Borrower	Total Amount of Gross Exposure			Value of Eligible Credit Risk Mitigates(CRM)	Net Exposure	Ratio of Net Exposure to Bank's Eligible Capital	Related Party's Relationship with Bank
		On Bal. Sheet	Off Bal. Sheet	Total				
1	2	3	4	5 (=3+4)	6	7 (=5-6)	8	9
Total								
A. Aggregate of all Exposures to Related Parties (Incl. the above Exposures)								
B. Ratio of Aggregate Related Parties Exposures to Bank's Eligible Capital								