

GUIDELINES ON TRANSACTIONS WITH RELATED PERSONS OF A BANK

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1. **AUTHORITY, PURPOSE AND SCOPE**

(a) **Authority**

1.1 These Guidelines are issued by the Bank of Botswana (Bank) pursuant to its authority set forth in Section 4(2) of the Bank of Botswana Act (CAP. 55:01).

(b) **Purpose**

1.2 The purpose of these Guidelines is to provide guidance for the implementation of Sections 17(7)-(8), 18(1) and 31 of the Banking Act (CAP. 46:04) (hereinafter referred to as the “Act”) and Regulation 9(3) of the Banking Regulations, 1995.

(c) **Scope**

1.3 These Guidelines apply to any bank licensed by the Bank under the Act, to statutory banks and other financial institutions established under separate Acts of Parliament, but falling under the purview of the Bank’s supervision in terms of Section 53(2) of the Act and/or their respective statutes.

2. **DEFINITIONS**

(a) **Accommodation** - A loan, advance or other credit facility, financial guarantee or other liability granted or incurred by a bank to or on behalf of any person, physical or juridical.

(b) **Act** - The Banking Act (CAP. 46:04).

(c) **Arm’s length** - Literally at a distance, transacting business with a related person on the same terms as available to members of the general public, rather than on familiar, friendly or preferential terms.

(d) **bank** - A company which is licensed by the Bank, pursuant to the Act, to conduct banking business in Botswana.

(e) **Board of Directors** - The highest body of authority in a bank responsible for strategically guiding a bank, effectively monitoring management and properly accounting to shareholders.

(f) **The Bank** - The Bank of Botswana established under the Bank of Botswana Act (CAP. 55:01).

(g) **Core Capital** - The amount of “Tier 1” capital calculated in accordance with instructions of the Bank on capital adequacy measurement and standard.

(h) **Director** - Any person, by whatever name called, who performs or is empowered to perform, substantially the same functions for a bank as those performed by a director of a company, as defined in the Companies Act (CAP. 42:01).

- (i) **Exposure** - The amount of a bank's exposure is calculated as follows:
- (i) The sum of all loans and credit facilities granted, either directly or indirectly, to a person or group of inter-related persons, such as:
- term loans, overdrafts, credit lines and other credit facilities;
 - trade bills discounted, invoice discounts and factoring;
 - credit substitutes, such as guarantees, acceptances, letters of credit and bills, and finance lease receivables;
 - underwriting of debt and equity securities, and other forms of participations;
 - securitised assets and other transactions with recourse;
 - credit derivatives, futures and forwards, swaps and option contracts such as credit default swaps and other derivatives;
 - contingent liabilities, such as commitments to extend credit, performance bonds and warranties.
- (ii) Less the amount by which the above-listed accommodations are irrevocably secured by:
- collateral in the form of cash deposits placed with a bank that granted the accommodation; or
 - an eligible guarantee by any sovereign with a credit rating of AA- or better, issued by a recognised external credit rating agency.
- (iii) To be considered eligible, the guarantee must: (1) represent a direct claim on the guarantor; (2) be denominated in the same currency as the exposure; (3) be explicit and clearly define the extent of the guarantee's cover of a specific exposure and be incontrovertible; (4) except for non-payment of the credit protection contract, be irrevocable and non-cancelable by the guarantor; (5) have as its only condition for its enforcement the counterparty's failure to meet his/her obligation to the bank; and (6) be executed so that neither the guarantor nor any other person is in a position to challenge the legal rights of the bank in calling the guarantee.
- (j) **Group of Inter-related Persons** - Two or more persons holding exposures from a bank, whether on a joint or separate basis, who are mutually associated and have at least one of the following: (1) a controlling interest; (2) common ownership or control; (3) common management; (4) common directors; (5) cross guarantees; or (6) direct financial interdependence which cannot be substituted in the short-term.

- (k) **Person** - Either a: (1) Natural person - an individual; or (2) juridical person - a company, partnership, association, or group of persons acting in concert, whether or not organised as a formal business entity.
- (l) **Principal Officer** - Chief Executive Officer or other person by whatever name referred to, who is subject to the directions of a board of directors, responsible for the day-to-day management of the affairs of a bank.
- (m) **Regulations** - Banking Regulations, 1995, Statutory Instrument No. 73 of 1995, published October 20, 1995.
- (n) **Related Person** - Includes all of the following without limitations: (1) Significant shareholder; (2) Member of a board of directors or audit committee; (3) Principal Officer and senior management officials; (4) Any person who is related to such significant shareholder, member of the board of directors or audit committee, Principal Officer or senior management official by family or business interest; (5) Subsidiary of a bank; (6) Company or undertaking in which at least a 5 percent interest is held by a bank; (7) Parent company of a bank; (8) Company that is under common control with a bank; and (9) A company that holds at least a 5 percent interest of another company in which a bank holds at least a 5 percent interest.
- (o) **Senior Management Official** - Any person who is an officer of a bank, including the Managing Director or Chief Executive Officer (and deputies), Chief financial or Operations Officer, Chief Lending Officer, Chief Internal Auditor, Chief Treasury Officer (or their equivalents), and other Heads of Department (core banking functions).
- (p) **Subsidiary** - A juridical person in which another person, or group of persons acting in concert, holds the equivalent of 50 percent or more of any class of shares with voting rights; or a shareholding that permits such other person or group of persons to exercise effective strategic control over the management or policies of the entity.
- (q) **Significant Shareholder** - A person who holds (directly or indirectly): (1) 5 percent or more of either the equity or the voting rights of a bank; or (2) Such other interest in a bank that enables a person to exercise significant influence over its strategic management or activity.
- (r) **Supplementary Capital** - Such long term funds and hybrid financial instruments that are approved by the Bank and qualifying as Tier II capital in accordance with the Capital Adequacy Measurement and Standards directive.
- (s) **Audit Committee** - A committee (or equivalent body) established by a board of directors of a bank for the purpose of overseeing the accounting and financial reporting processes and audits of the financial statements of a bank and ensuring the adequacy and effectiveness of the bank's internal control systems.

- (t) **Unimpaired Capital** - With regard to a capital of a bank, “unimpaired” means the absence of any:
- (i) legal or technical covenant, term, restriction or encumbrance which would otherwise render such capital to be not freely available for distribution to depositors or other creditors in the event of the liquidation or dissolution of the bank; and
 - (ii) condition or arrangement which would, in the opinion of the Bank, diminish the value of the whole or any portion of the capital of a bank.

3. **REQUIREMENTS**

(a) **Arm’s-length Transactions**

3.1 Any transaction between a bank and its related person shall be on an arm’s-length basis. A bank shall not enter into a transaction with or for the benefit of a related person if such transaction would be entered into on less favourable terms and conditions, or not at all, with or for the benefit of persons who are not so related to a bank. However, such a transaction will not be in contravention of these Guidelines if the terms and conditions of the transaction are in line with the conditions of employment.

(b) **Policies and Procedures**

3.2 A board of directors shall establish and ensure that senior management officials implement a written policy covering all transactions, including deposit-taking and credit-granting, between a bank and its related persons. Processes should be established in each bank to allow a board of directors to monitor compliance with policy. A board of directors shall review the policy on at least an annual basis. A policy shall, at a minimum:

- (i) prohibit a bank from providing favourable treatment to related persons and require that all such transactions be on an arm’s-length basis. Prohibited favourable treatment includes, but is not limited to:
 - reduction of credit-granting standards, collateral requirements, collection efforts or any other policies of a bank;
 - providing preferential rates on deposits or credits;
 - covering trading losses; and
 - waiving fees.
- (ii) impose strict and binding limits on exposures to related persons which do not exceed the limitations as set out in these Guidelines.

- (iii) prohibit related persons who have an interest in an accommodation or other transaction with a bank from being involved in the administration, assessment or decision-making process relating to the transaction.
- (iv) require that transactions with related persons, including all deviations from a board approved policy, be reported to a board of directors on a regular basis.
- (v) comply with Sections 17 and 31 of the Act, Section 9(3) of the Regulations and these Guidelines.

(c) **Disclosure**

3.3 A director or senior management official of a bank who is a party to, or has an interest in any credit accommodation or other transactions with a bank, including those proposed shall:

- (i) disclose in writing to a board of directors at the earliest opportunity the nature and extent of his/her interest;
- (ii) rescue himself/herself from any meeting at which the credit accommodation or other transaction is discussed.
- (iii) refrain from voting on any matter related to the credit accommodation or other transaction, provided that such interest, if so disclosed, shall not disqualify a director from constituting a quorum.

(d) **Approval by a Board of Directors**

3.4 A bank must have an approved policy on extension of credit to related persons. Any director who has an interest in a transaction between a bank and its related persons shall abstain from a board's consideration and decision-making process. The official minutes of a board of directors' meeting shall document approval of the transaction, the terms and conditions of the transaction, and the determination by a board of directors that the transaction was at arm's-length. A board of directors shall ensure that transactions with related persons are monitored in a manner independent of the related person.

(e) **Record-keeping**

- (i) Each bank shall maintain records on disclosures made by directors or senior management officials who are a party to, or have an interest in, any credit accommodation or other transaction with a bank.
- (ii) Each bank shall have procedures in place to identify related persons and groups of inter-related persons. A bank's records shall be updated on at least an annual basis.
- (iii) A record shall be maintained of any transaction with a related person.

4. LIMITATIONS

- 4.1 If the interests of two or more persons are such that they are deemed to be a “group of inter-related persons”, then the total exposures of all persons in that group shall be combined for purposes of determining limits on exposures to related persons.
- 4.2 The unsecured amount of a bank’s exposures to a senior management official or employee (other than a director) shall not exceed one-year’s emoluments of such senior management official or employee.
- 4.3 The unsecured amount of a bank’s exposure to any related person other than a senior management official, including a group of inter-related persons, shall not exceed 10 percent of the bank’s core capital.
- 4.4 A bank’s total exposure to any related persons, including groups of inter-related persons, shall not exceed 25 percent of the bank’s unimpaired capital.
- 4.5 A director or senior management official shall not solicit or accept an appointment as executor, administrator or trustee of the estate of any customer of the bank.

5. REPORTING AND SUPERVISORY ACTION

- 5.1 Each bank shall submit to the Bank a quarterly report in the format prescribed by the Bank, showing all exposures to related persons and evidencing compliance with the Guidelines.

Issued this day of, 2008

DIRECTOR
BANKING SUPERVISION DEPARTMENT