

GOVERNMENT NOTICE NO. 9

FINANCIAL SERVICES ACT

(CAP. 44: 05)

FINANCIAL SERVICES (PROMPT CORRECTIVE ACTION FOR DEPOSIT TAKING MICROFINANCE INSTITUTIONS) DIRECTIVE, 2018

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IN EXERCISE of the powers conferred by section 34 (1) (a) and (2) (a) of the Financial Services Act, I, DR. DALITSO KABAMBE, Registrar of Financial Institutions, issue the following Directive—

PART I—PRELIMINARY

1. This Directive may be cited as the Financial Services (Prompt Corrective Action for Deposit Taking Microfinance Institutions) Directive, 2018.

Citation

2. In this Directive unless the context otherwise requires—

Interpretation

“core capital” has the meaning ascribed to that term in the Financial Services (Capital Adequacy Requirement for Deposit Taking Microfinance Institutions) Directive, 2014;

GN. 38/2014

“institution” means a deposit taking microfinance institution under the Microfinance Act; and

Cap. 46:08

“Registrar” means the Registrar of Financial Institutions appointed under the Act.

3. The powers specified in this Directive are in addition to the general powers of the Registrar under the Act and the Microfinance Act and other Directives.

Scope of application  
Cap. 46:08

## PART II—OBJECTIVES

- Objectives 4. The objectives of this Directive are to—
- (a) establish corrective actions that the Registrar may take or impose on an institution; and
  - (b) prescribe circumstances under which the Registrar or his agent may exercise powers under the existing legal framework to resolve an institution while—
    - (i) the institution is still under the control of its owners; and
    - (ii) suspending the rights of the owners and management before an institution becomes insolvency.

## PART III—PROMPT CORRECTIVE ACTION

- Prompt corrective actions 5. The Registrar shall take prompt corrective actions on an institution that falls in each of the categories set out in the Schedule.
- General Enforcement Actions 6. The Registrar shall, in addition to the supervisory actions outlined in the Schedule, impose the directions and administrative penalties prescribed in section 39 and 75 of the Act.

## SCHEDULE

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## SUMMARY OF PROMPT CORRECTIVE ACTIONS

<i>Category</i>	<i>Institution Condition</i>	<i>Mandatory Supervisory Action</i>
Capital Adequacy Ratio	A. Marginally Capitalised Institution: An institution with core capital ratio which is greater than 10% but less than 15% which, given its financial developments, for example, worsening asset quality, is expected to breach the minimum capital requirement prescribed by the Registrar.	The Registrar shall take the following measures— (a) caution management to proactively monitor the ratio; (b) put the institution under the Registrar's watch list for increased monitoring; and (c) restrict dividend payment.
	B. Undercapitalised Institution: An institution with core capital ratio which is greater than 8% but less than the prescribed minimum of 10%.	The Registrar shall take the following measures in addition to the measures prescribed for a marginally capitalised institution—

- (a) engage the management, board or shareholders of the institution to discuss ways to resolve the undercapitalization;
- (b) restrict investment in new branches;
- (c) restrict investment in fixed assets;
- (d) request the institution to submit a financial recovery plan to the Registrar;
- (e) conduct targeted on-site examination;
- (f) conclude an enforceable undertaking with the institution; and
- (g) request an institution to recapitalize to meet the regulatory minimum capital requirement.

C. Significantly Undercapitalised Microfinance Institution:

An institution with core capital ratio which is equal to, or greater than, 5.0% but less than 8.0%.

The Registrar shall take the following measures in addition to the measures prescribed for a marginally capitalised and undercapitalised institution—

- (a) restrict lending;
- (b) direct the institution to replace management, board, or both management and board, in addition to the Registrar's power to remove relevant persons that do not meet the fit and proper requirements prescribed by the Registrar;
- (c) restrict the undertaking of any material transaction without Registrar's approval;
- (d) prohibit changes in the institution's accounting methods;
- (e) direct immediate new recapitalisation or capital restoration plan;

- (f) review the institution's capital plan within fourteen days and communicate to the institution its acceptability or otherwise;
- (g) take over management and control of the institution within six months after final capital call;
- (h) immediately after issuance of final capital call, start compiling all critical information in readiness for implementation of any resolution option, prescribed for a critically undercapitalised institution; and
- (i) if the institution's capital plan is unacceptable or if the institution's shareholders fail to recapitalise within the period specified by the Registrar, implement any of the resolution options prescribed for a critically undercapitalised institution.

D. Critically undercapitalised institution: An institution with core capital ratio which is less than 5.0%

The Registrar shall take the following measures in addition to the measures prescribed for a marginally capitalised, undercapitalised and significantly undercapitalised institution—

- (a) immediately take over management of the institution or appoint a statutory manager to exercise any or all of the resolution powers available under the Act and the Microfinance Act; and
- (b) immediately initiate procedures for liquidation of the institution in accordance with the provisions of the Act and the Microfinance Act.

Cap. 46:08

Cap. 46:08

Liquidity	<p>A. Marginally liquid Microfinance Institution: An institution with a liquidity ratio which is greater than 20% but less than 25 %</p>	<p>The Registrar shall engage management to closely monitor the institution's liquidity ratio.</p>
	<p>B. Institution with weak liquidity position. An institution with liquidity ratio which is between 15% and 20%</p>	<p>The Registrar shall take the following measures in addition to the measures prescribed for a marginally liquid institution—</p> <ul style="list-style-type: none"> <li>(a) engage management for discussion on its plans to improve liquidity;</li> <li>(b) direct the institution to submit a plan for restoring liquidity to the Registrar;</li> <li>(c) review the plan within fourteen days and communicate to the institution its acceptability or otherwise; and</li> <li>(d) impose administrative penalty.</li> </ul>
	<p>C. Significantly Illiquid Institution: A Microfinance Institution that records a liquidity ratio of between 10% and 15%</p>	<p>The Registrar shall take the following measures in addition to the measures prescribed for a marginally liquid institution and an institution with a weak liquidity position—</p> <ul style="list-style-type: none"> <li>(a) conduct a spot-check to investigate the problem of the institution including compliance with its own liquidity management practices and contingency plan;</li> <li>(b) invite the institution's board and management for discussion on efforts being pursued to address the problem;</li> <li>(c) direct the institution to realise illiquid assets in order to improve liquidity;</li> </ul>

(d) direct the institution to intensify debt recovery; and

(e) direct the institution to divest its equity in subsidiaries or related entities.

D. Critically illiquid institution: An institution that persistently registers liquidity ratio which is below 10%.

The Registrar shall take the following measures in addition to the measures prescribed for a marginally liquid institution, an institution with a weak liquidity position and a significantly illiquid institution—

(a) change management or directors; and

(b) place the institution under statutory management if unable or unlikely to meet maturing obligations for five days.

Made this 24th day of January, 2018.

FILE NO. FIN/PFSPD/03/04

DR. D. KABAMBE  
*Registrar of Financial Institutions*

GOVERNMENT NOTICE NO. 10

FINANCIAL SERVICES ACT

(CAP. 44: 05)

FINANCIAL SERVICES (TRANSACTIONS OF BANKS WITH RELATED PARTIES)  
DIRECTIVE, 2018

ARRANGMENT OF PARAGRAPHS

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## SCHEDULE-Policy on transactions with insiders and related parties

IN EXERCISE of the powers conferred by section 34 (2) (z) of the Financial Services Act, 1, Dr. DALITSO KABAMBE, Registrar of Financial Institutions, make the following Directive—

## PART I – PRELIMINARY

1. This Directive may be cited as the Financial Services (Transactions of Banks with Related Parties) Directive, 2018. Citation
2. In this Directive unless the context otherwise requires— Interpretation
  - “arms length basis” means where a transaction between related parties is conducted upon terms no more favourable than those which would be offered under prevailing conditions to persons other than related parties;
  - “bank” has the meaning ascribed to that term in the Banking Act; Cap.44:01
  - “banking business” has the meaning ascribed to that term in the Banking Act; Cap.44:01
  - “banking group” means a group of two or more companies at least one of which is a bank domiciled in Malawi where the holding company is a bank or a non-financial company domiciled in Malawi;
  - “board” means the highest body of authority in a financial institution responsible for strategically guiding the institution, effectively monitoring management and properly accounting to shareholders;
  - “core or Tier 1 capital” has the meaning ascribed to that term in the Financial Services (Capital Adequacy for Banks) Directive 2012; G.N. 31/2012
  - “credit facility” has the meaning ascribed to that term in the Banking Act. Cap.44:01
  - “eligible guarantee” means a guarantee that is issued by —
    - (a) the Government of Malawi in compliance with section 63 of the Public Finance Management Act; Cap.37:02
    - (b) any sovereign country with a sovereign rating approved by the Registrar;
    - (c) an international bank with an external credit assessment of AAA to AA- issued by an external credit assessment institution acceptable to the Registrar;
    - (d) a multilateral development bank or institution; or
    - (e) a third party entity that—
      - (i) represents a direct claim on the guarantor;
      - (ii) is denominated in the same domestic currency as the exposure or strong convertible currency;

(iii) clearly and incontrovertibly defines the extent of the guarantee's cover of a specific exposure;

(iv) is irrevocable and non-cancelable by the guarantor, except for non-payment of the credit protection contract;

(v) has no clause in the contract that would allow the guarantor to unilaterally cancel the guarantee, increase the effective cost of the guarantee, or delay payment under the guarantee for any reason including the need to be funded in the budget;

(vi) has, as the only condition for its enforcement the obligor's failure to meet an obligation to the bank; and

(vii) is 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;

"exposure to an insider or related party" means the amount of the insider's or related party's obligation to a bank calculated as the sum of the following—

- (a) credit facilities;
- (b) equity securities;
- (c) debt securities;
- (d) securitized assets and other transactions with recourse; and
- (e) contingent liabilities, such as commitments to extend credit;

"group of related parties" means two or more persons holding exposures from a bank, whether on a joint or separate basis, which are mutually associated and meet any of the following criteria—

- (a) the parties are a "group of related debtors" as defined in the Banking Act;
- (b) the persons have common management or common directors;
- (c) cross guarantees exist; or
- (d) a direct or indirect financial interdependency exists between the persons which cannot be substituted in the short term.

Cap.44:01

Cap.44:01

Cap.44:01

"insider" has the meaning ascribed to that term in the Banking Act;

"related party" has the meaning ascribed to that term in the Banking Act;

"senior management official" means—

- (a) an executive officer;
- (b) head of department or function;
- (c) an official who reports either directly to the board of directors, to a committee of the board of directors or to an executive officer;
- (d) a branch manager of a bank that the Registrar declares as a senior management official; and

Act No. 15  
of 2013

"subsidiary" has the meaning ascribed to that term in the Companies Act.

## PART II – OBJECTIVES

3. The objectives of this Directive are to—
- (a) promote sound practices with regard to the granting of credit to related parties;
  - (b) ensure that transactions between a bank and its insiders and related parties are done on an arm's-length basis; and
  - (c) promote public confidence in banks by ensuring that no undue favouritism is extended to insiders or related parties of banks.

Objectives

## PART III – REGULATORY REQUIREMENTS

4.—(1) A credit facility to an insider or to a related party shall be on arm's length basis.

Restrictions on insider lending and related parties

(2) A bank's exposure to an insider or to a related party shall not exceed ten percent (10%) of its core capital.

(3) The aggregate of a bank's exposures to insiders and related parties shall not exceed twenty five percent (25%) of the bank's core capital, unless the bank obtains written permission of the Registrar.

(4) A credit facility to an insider or to a related party shall be secured by collateral which is enforceable.

(5) Subparagraphs (1) and (4) shall not apply to a credit facility that a bank may grant to its employees as part of their terms and conditions of employment that equally apply to all officers and employees.

(6) A bank shall not grant any credit facility to an insider or to a related party while another credit facility to that person is non-performing.

(7) A bank shall not purchase a non-performing credit facility or other low quality asset from an insider or a related party.

(8) The Registrar shall consider placements of a bank to any of its affiliated entities in Malawi as insider transactions and they shall be subject to the provisions of this Directive.

(9) An exposure to an insider or related party that exceeds the limitations of this Directive or is made in violation of the requirements of this Directive shall be deducted from the bank's core capital for purposes of determining capital adequacy.

5. The board of directors of a bank shall—

Board responsibilities

(a) adopt and ensure implementation of a written policy on transactions with insiders and related parties that includes the provisions set out in the Schedule to this Directive;

(b) approve all transactions, including credit facilities, between a bank and its insiders and related parties, provided that a director who has an interest in the transaction shall not participate in the board's consideration and decision process; and

(c) ensure that a credit facility or a transaction with an insider or a related party is monitored independent of the insider or related party.

6.—(1) A director or senior management official of a bank who is a party

Disclosure

to or has an interest in an existing or prospective credit facility or other transaction with the bank shall—

(a) disclose in writing to the board of directors at the earliest opportunity the nature and extent of the interest;

(b) leave any meeting at which the credit facility or other transaction is discussed;

(c) refrain from voting on any matter related to the credit facility or other transaction, provided that such interest, if so disclosed, shall not disqualify a director from constituting a quorum.

GN. 4/2011 (2) A bank shall disclose all its credit facilities to insiders and related parties in line with the requirements of the Financial Services (Disclosure of Information by Banks) Directive 2011.

Record keeping 7. A bank shall maintain adequate records with regard to all credit facilities to insiders and related parties.

#### PART IV-ENFORCEMENT

Cap.44:01 8.—(1) The Registrar shall impose the following monetary penalties for violations of this Directive—

(a) for banks, up to fifty million Kwacha (K50, 000,000); and

(b) for natural persons who are members of the board of directors, or senior management, up to ten million Kwacha (K10,000,000).

(2) With respect to banks, the Registrar shall—

(a) debit the penalty in subparagraph 1 (a) from the main account of the bank maintained at the Reserve Bank of Malawi; and

(b) notify the bank in writing prior to debiting the account.

(3) With respect to natural persons or where the bank does not maintain an account with the Reserve Bank of Malawi, the natural person or the bank shall pay the penalty through a bank certified cheque or electronic transfer payable to the Reserve Bank of Malawi within ten working days after being notified by the Registrar.

Administrative penalties  
Cap. 44:01 9. In addition to the monetary penalty imposed in paragraph 8 (1), the Registrar may impose directions, administrative penalties and enforcement action as provided for under the Act and the Banking Act.

Renovation  
GN. 40/2012 10. The Financial Services (Transactions with Related Parties of Banks) Directive, 2012 is revoked.

#### SCHEDULE

(par. 5 (a))

#### POLICY ON TRANSACTIONS WITH INSIDERS AND RELATED PARTIES

1. This policy on transactions with insiders and related parties —

(a) requires a bank to handle all transactions with insiders and related parties on an arm's-length basis. The following preferential treatment is prohibited—

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- (i) altering credit-granting standards, collateral requirements, collection efforts or any other policies of a bank;
  - (ii) providing preferential rates, terms or conditions on deposits or credits;
  - (iii) providing products or services that are not available to the general public;
  - (iv) approving credit facilities without the board of directors approval;
  - (v) covering trading losses; and
  - (vi) waiving fees;
- (b) imposes strict and binding limits on exposures to insiders and related parties which do not exceed the limitations of this Directive;
- (c) prohibits insiders and related parties who have an interest in a credit facility or other transaction with the bank from being involved in the administration, assessment, or decision-making process relating to the transaction; and
- (d) requires the management of a bank to report all transactions with insiders and related parties, and any deviations from the board-approved policy on insiders and related parties, to the board of directors on a regular basis.

Made this 24th day of January, 2018.

(FILE REF. FIN/PFSPD/03/04

DR. D. KABAMBE  
*Registrar of Financial Institutions*