

# **Saudi Arabian Monetary Authority (SAMA)**

## **Related Parties Rules for Banks**

February 2020



Contents

1. Introduction ..... 3

2. Definitions ..... 3

3. Scope and Level of Application ..... 6

4. Governance and Risk Management..... 7

5. Exposure Limits ..... 8

    5.1 Maximum Exposure Limits ..... 8

    5.2 Exposures Exempted from Related Parties Limits..... 8

6. Security for Related Party Transactions..... 9

7. Reporting..... 9

8. Effective Date ..... 9

## **Related Parties Rules for Banks**

### **1. Introduction**

These Rules are issued by 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 14/10/1406AH.

These rules define related parties, provide additional requirements in regards to exposures to related counterparties and reinforce and provide further guidance to Article 9 of the Banking Control Law.

Banks should also adhere to the related party requirements as prescribed in SAMA Principles of Corporate Governance and any relevant policies as applicable.

These Rules shall supersede the Related Parties Rules for Banks issued vide SAMA circular no. 1607/67 dated 09/01/1441AH. The changes from the previous version are underlined.

### **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 Authority.
- ii.* **Rules:** Related Parties Rules for Banks.
- iii.* **Exposure:** 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.

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

v. **Control Relationship:** 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 determine whether a control relationship exists 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 governing 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 entity (e.g. through consent rights over key decisions);

Banks are also expected to refer to criteria specified in appropriate internationally recognized accounting standards (The International Financial Reporting Standards - IFRS are applied to all banks in KSA) for further qualitatively based guidance when determining control.

vi. **Related Party:**

- a. Substantial Shareholders of the bank.
- b. Board members of the bank or any of its subsidiaries/ affiliates (Associates and joint venture as per the definitions giving by the accounting standards) and their relatives.
- c. Senior Executives of the bank or any of its subsidiaries/ affiliates and their relatives.

- d. Board members and Senior Executives of Substantial Shareholders of the bank.
- e. Entities other than companies owned by a Board member or any Senior Executive of the bank or their relatives, or owned by the external auditor of the bank.
- f. Non-joint stock companies in which a Board member or a Senior Executive of the bank or any of their relatives, or the external auditor of the bank, is a partner.
- g. Companies in which a Board member or a Senior Executive of the bank or any of their relatives is a member of its Board of directors or is one of its Senior Executives.
- h. Joint stock companies in which a member of the Board or a Senior Executive of the bank or any of their relatives owns (5%) or more.
- i. Companies in which a Board member or a Senior Executive of the bank or any of their relatives has a financial interest, is a guarantor of, or has influence on the companies' decisions even if only by giving advice or guidance.
- j. Subsidiary/ affiliate.
- k. External auditors of the bank.

Advice or guidance that is provided on a professional basis by a person licensed to provide such advice shall be excluded from the provisions of paragraphs (i).

**vii. Relatives:**

- a. Fathers, mothers, grandfathers and grandmothers.
- b. Children, grandchildren.
- c. Siblings, maternal and paternal half-siblings.
- d. Husbands and wives.

Where dependence criteria for relatives/ family members has been identified based on the Related Party definition, a bank may still demonstrate to SAMA in exceptional cases, that the family members clearly operate all business activities

independent of each other with no economic interdependence, financial support or shareholding from the other family member.

- viii. **Substantial Shareholders:** any person who owns 5% or more of the shares of the bank or voting rights therein.
- ix. **Security:** means such security as would, in the opinion of the SAMA, be acceptable to a prudent banker and satisfies the following criteria:
- a. The market value of the asset is readily determinable or can be reasonably established and verified;
  - b. The asset is marketable and there exists a readily available secondary market for disposing of the asset;
  - c. The bank's right to repossess the asset is legally enforceable and without impediment;
  - d. The bank is able to secure control over the asset if necessary.
  - e. The bank has the expertise and systems to manage the asset concerned.
- x. **Senior Executive:** the Managing Director, Chief Executive Officer, General Manager, their deputies, Chief Financial Officer, Managers of key departments, officers of risk management, internal audit, and compliance functions, and similar positions in the Financial Institution, in addition to incumbents of any other positions determined by SAMA.

### **3. Scope and Level of Application**

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 foreign branches and subsidiaries of locally incorporated banks operating outside the Kingdom of Saudi Arabia.
- iii. All foreign banks operating in the Kingdom of Saudi Arabia.

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

#### **4. Governance and Risk Management**

- i. The Board of the bank is ultimately responsible for oversight of the bank's associations with its related parties and for approving policies governing the bank's dealings and associations with its related parties. The Board must ensure that these policies are reviewed at least annually and that they remain adequate and appropriate for the bank's risk appetite, risk profile, capital, balance sheet size and the complexity of the bank.
- ii. A bank is required to have policies and procedures on related party exposures.
- iii. A bank is required to have adequate systems and controls in place to identify, measure, monitor and report related party exposures of the bank in a timely basis and ensure related party exposures of the bank are reviewed at least quarterly.
- iv. 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 and policies and procedures on related party exposures;
- v. Any exposure to a related party or any variation of the terms of a related party exposure should be approved at the level of Board of Directors or its delegated authority. While considering any proposal of lending to a board member or any of their connected parties, the Board of Directors shall ensure that the concerned board member would neither participate in the discussion nor influence such a decision;
- vi. A bank should institute procedures to prevent the beneficiaries of any credit exposure being part of the processing or approval of such exposure;
- vii. 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.

## 5. Exposure Limits

### **5.1 Maximum Exposure Limits**

Exposures to related parties are subject to measurement requirements as prescribed in SAMA Rules on Large Exposures of Banks. Subject to the following limits:

- i. The sum of all exposures values a bank has to a non-bank related counterparty that is not a listed company in the Saudi Stock Exchange must not be higher than 5% of the bank's available eligible capital base at all times.
- ii. For those companies listed in the Saudi Stock Exchange, the sum of all exposures values a bank has to the non-bank related counterparty must not be higher than 10% of the Bank's available eligible capital base at all times.
- iii. A bank may have an exposure to its non-banking subsidiary in financial sector of up to 25% of the Bank's available eligible capital base.
- iv. Where a related party is included within a Group of Connected Counterparties, the exposure limit specified under these Rules shall be applicable, in addition to the overall group exposure limit as specified in SAMA Rules on Large Exposures of Banks.
- v. A cumulative limit on all exposures to non-bank related counterparties shall be 50% of the banks eligible capital.

Any breaches of the exposure limits, must be communicated immediately to SAMA. The communication to SAMA must also include the bank's action plan to bring the exposure to within the breached limit. Furthermore, any such breaches may attract punitive supervisory action depending upon their materiality.

### **5.2 Exposures Exempted from Related Parties Limits.**

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

- i. Banks' exposures to the Saudi Government, SAMA, Entities Connected with the Saudi Government, GCC and their central banks.
- ii. Entities that are related to the bank only due to the above sovereign ownership in both the entity and the bank. This also applies if there is a joint Board member



representing and appointed by Saudi Government in both the related party entity and the bank. However, the representative himself or herself in individual capacity is not exempted from the limits specified in these rules.

## **6. Security for Related Party Transactions**

- i. Article 9 of the Banking Control Law requires banks not to grant, without security, a loan or credit facilities, or issue a guarantee or incur any other financial liability in respect to parties specified in the law.
- ii. For loans, credit facilities, guarantees or other financial liabilities to establishments not taking the form of joint-stock companies in which any of its Directors or Auditors is a partner or is a manager or has a direct financial interest, banks are required to ensure such facilities are fully secured where control relationship by the party exists. Where no control relationship exists, security for the borrowing should be on pro rata basis. In other words, only the respective party's effective share of the facility is required to be fully secured.

## **7. Reporting**

Banks are required to submit to SAMA all exposures to related counterparties that exceeded 5% of the banks eligible capital base on the reporting date, on the prescribed format attached as per Appendix-I.

The above information shall be submitted to SAMA each calendar quarter within 30 calendar days of the end of each quarter.

## **8. Effective Date**

These Rules shall come into force with effect from the 1<sup>st</sup> of March 2020. Banks are required to ensure compliance with these Rules while taking any new exposure or renewing existing exposures after the effective date.

Bank are required to submit to SAMA a list of all exposures (if any) that do not meet the requirements of these Rules, and a rectification plan where necessary.

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## Appendix-I

Name of the Bank: \_\_\_\_\_

Statement for the Month ended \_\_\_\_\_

**Q27-5**

**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	In Case if 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 Exposures to Related Parties (Incl. the above Exposures)								
B. Ratio of Aggregate Related Parties Exposures to Bank's Eligible Capital								