



PRUDENTIAL REGULATIONS FOR CORPORATE / COMMERCIAL BANKING

(Updated on January 31, 2011)

BANKING POLICY & REGULATIONS DEPARTMENT
STATE BANK OF PAKISTAN

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State Bank of Pakistan compiles a booklet of Prudential Regulations from time to time for convenience of users. Updated version of such a booklet containing amendments in the regulations made through circulars/Circular letters to date is being issued. Due care has been taken while incorporating amendments, however, errors and omission may be expected. In case of any ambiguity, users are advised to refer to the original circulars/circular letters on the relevant subject(s), which are available on SBP's website (www.sbp.org.pk).

THE TEAM

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Inayat Hussain	Executive Director (BPRG)
Syed Irfan Ali	Director (BPRD)
Muhammad Saleem	Additional Director (BPRD)
Kazi Sarfraz	Joint Director (BPRD)
Amjad Ali	Joint Director (BPRD)
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The amendments made in the Prudential Regulations for Corporate/Commercial Banking during January 31, 2009 to January 31, 2011 have been incorporated in this updated version for ease of reference of the users.

The Prudential Regulations for Corporate/Commercial Banking cover four categories viz. Risk Management (R), Corporate Governance (G), Customer Due Diligence and Anti Money Laundering (M), and Operations (O). It may further be noted that any financing facility, other than the one defined under the SMEs, Consumer, Agriculture and Micro Financing, shall be governed by the Prudential Regulations for Corporate/Commercial Banking. However, in case of international operations, the Prudential Regulations of host country shall prevail.

The Prudential Regulations for Corporate/Commercial Banking do not supersede other directives issued by State Bank of Pakistan in respect of areas not covered here. Any violation or circumvention of these regulations shall render the bank/DFI/officer(s) concerned liable for penalties under the Banking Companies Ordinance, 1962.

SYED IRFAN ALI
Director
Banking Policy & Regulation Department

PART – A
DEFINITIONS

For the purpose of these regulations: -

1. Account Holder means a person who has opened any account with a bank or is a holder of deposit/deposit certificate or any instrument representing deposit/placing of money with a bank/DFI or has borrowed money from the bank/DFI.
2. Alternate Director means a person who has been designated by a director during his absence, as per provisions of the sub-section (2) of section 192 of Companies Ordinance, 1984.
3. Bank means a banking company as defined in the Banking Companies Ordinance, 1962.
4. Borrower means a person on whom a bank/DFI has taken any exposure during the course of business.
5. Chief Executive Officer (CEO), in relation to bank/DFI means an individual who, subject to the control and directions of the directors, is entrusted with the whole, or substantially the whole, of the powers of management of the affairs of the bank/DFI occupying the position of Chief Executive Officer and include President, acting President, Managing Director, Country Head of Foreign bank, Executive assuming charge of the bank for interim period or by whatever name called, and whether under a contract of service or otherwise.
6. Contingent Liability means:
 - a) a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non- occurrence of one or more uncertain future events not wholly within the control of the enterprise; or
 - b) a present obligation that arises from past events but is not recognized because:
 - i) it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or
 - ii) the amount of the obligation cannot be measured with sufficient reliability;and includes letters of credit, letters of guarantee, bid bonds/performance bonds, advance payment guarantees and underwriting commitments.
7. Corporate Card means credit card issued to the employees of an entity where the repayment is to be made by the said entity.
8. DFI means Development Financial Institution and includes the Pakistan Industrial Credit and Investment Corporation (PICIC), the Saudi Pak Industrial and Agricultural Investment Company Limited, the Pak Kuwait Investment Company Limited, the Pak Libya Holding Company Limited, the Pak Oman Investment Company (Pvt.) Limited, Investment Corporation of Pakistan, House

Building Finance Corporation, Pak Brunei Investment Company Limited¹, Pak-Iran Joint Investment Company Limited², Pak-China Investment Company Limited³, and any other financial institution notified under Section 3-A of the Banking Companies Ordinance, 1962.

9. Documents include vouchers, cheques, bills, pay-orders, promissory notes, securities for leases/advances and claims by or against the bank/DFI or other papers supporting entries in the books of a bank/DFI.
10. Director includes any person occupying the position of a director on the Board of a bank/DFI and includes sponsor, nominee and alternate director or by whatever name called.
11. Executive Director means a paid employee or executive in the concerned bank/DFI or employee or executive in a company/group where sponsor shareholders of the bank/DFI have substantial interest.
12. Equity of the Bank/DFI means Tier-I Capital or Core Capital and includes paid-up capital, general reserves, balance in share premium account, reserve for issue of bonus shares and retained earnings/accumulated losses as disclosed in latest annual audited financial statements. In case of branches of foreign banks operating in Pakistan, equity will mean capital maintained, free of losses and provisions, under Section 13 of the Banking Companies Ordinance, 1962.

For the purpose of Regulation R-1, reserve shall also include revaluation reserves on account of fixed assets to the extent of 50% of their value. However, for this purpose assets must be prudently valued by valuers on the panel of Pakistan Bank Association (PBA), fully taking into account the possibility of price fluctuations and forced sale value. Revaluation reserves reflecting the difference between the book value and the market value will be eligible up to 50%.

13. Equity of the Borrower includes paid-up capital, general reserves, balance in share premium account, reserve for issue of bonus shares and retained earnings/accumulated losses, revaluation reserves on account of fixed assets and subordinated loans.

The Preference Shares, only with the following features, will also be included in the equity of the borrower:

- There should not be any provision for redemption or the redemption should be at the option of the issuer.
- In case the issuer is given an option to redeem the preference shares, as per agreed terms and conditions, the issuer will redeem the share only through a sinking fund created out of the profits of the company. Further, the sinking fund created for this purpose would not be calculated towards the equity of the issuer.
- The terms and conditions should not give rise to a contractual obligation on the part of the issuer to deliver another financial asset or exchange another

¹ Specified vide GoP Notification No.F.1(4)-BKG(R&S)/2002 dated December 21, 2006.

² Specified vide GoP Notification No.F.1(4)-BKG(R&S)/2002 dated July 21, 2007.

³ Specified vide GoP Notification No.F.1(4)-BKG(R&S)/2002 dated November 29, 2007.

financial instrument under conditions that are or can be potentially unfavorable to the issuer. However, an option to convert preference shares into common shares may be included in the features of the preference shares.

- The terms and conditions of the preference shares should not be such as to compel the issuer economically, financially or otherwise to redeem the shares.
- Payment and distribution of dividend to the holders of preferred shares, whether cumulative or non-cumulative, should be at the discretion of the issuer.

Revaluation reserves will remain part of the equity for first three years only, from the date of asset revaluation, during which time the borrower will strengthen its equity base to enable it to avail facilities without the benefit of revaluation reserves. However, if a borrower gets revaluation during the three years period, the borrower will be allowed the benefit from fresh revaluation, to the extent of increase in revaluation reserves, but restricting the benefit of such incremental value to 3 years only. Similarly, if after 3 years, the borrower again gets revaluation of the assets with resultant addition in their value, the benefit of such revaluation may also be allowed for the next 3 years, again to the extent of increase in revaluation reserves.

The revaluation reserves to be eligible for benefit should be calculated by the valuers on the approved panel of the PBA. If the bank/DFI obtains copy of accounts as per requirement in Prudential Regulation R-3, then such revaluation reserves should appear in the said accounts, and in such case, no parallel calculation by the banks/DFIs for amortization purposes will be required. In case of no requirement of copy of accounts, the borrower may still be given the benefit of revaluation reserves in the way mentioned above, but the bank/DFI will calculate the amortization of the same independently.

14. Exposure means financing facilities whether fund based and/or non-fund based and include:
- i) Any form of financing facility extended or bills purchased/discounted except ones drawn against the L/Cs of banks/DFIs rated at least 'A' by Standard & Poor, Moody's, Fitch-Ibca, Japan Credit Rating Agency (JCRA) or credit rating agency on the approved panel of State Bank of Pakistan and duly accepted by such L/C issuing banks/DFIs:
 - ii) Any financing facility extended or bills purchased/discounted on the guarantee of the person.
 - iii) Subscription to or investment in shares, Participation Term Certificates, Term Finance Certificates or any other Commercial Paper by whatever name called (at book value) issued or guaranteed by the persons.
 - iv) Credit facilities extended through corporate cards.
 - v) Any financing obligation undertaken on behalf of the person under a letter of credit including a stand-by letter of credit, or similar instrument.
 - vi) Loan repayment financial guarantees issued on behalf of the person.
 - vii) Any obligations undertaken on behalf of the person under any other guarantees including underwriting commitments.
 - viii) Acceptance/endorsements made on account.
 - ix) Any other liability assumed on behalf of the client to advance funds pursuant to a contractual commitment.

15. Family Member as defined in sub-section (ff) of section 5 of Banking Companies Ordinance 1962.¹
16. Financial Institutions mean banks, Development Financial Institutions (DFIs) and NBFCs.
17. Forced Sale Value (FSV) means the value which fully reflects the possibility of price fluctuations and can currently be obtained by selling the mortgaged/pledged assets in a forced/distressed sale conditions.
18. Government Securities shall include such types of Pak. Rupee obligations of the Federal Government or a Provincial Government or of a Corporation wholly owned or controlled, directly or indirectly, by the Federal Government or a Provincial Government and guaranteed by the Federal Government as the Federal Government may, by notification in the Official Gazette, declare, to the extent determined from time to time, to be Government Securities.
19. Group means persons, whether natural or juridical, if one of them or his dependent family members or its subsidiary, have control or hold substantial ownership interest over the other. For the purpose of this:
 - a) Subsidiary will have the same meaning as defined in sub-section 3(2) of the Companies Ordinance, 1984 i.e. a company or a body corporate shall deemed to be a subsidiary of another company if that other company or body corporate directly or indirectly controls, beneficially owns or holds more than 50% of its voting securities or otherwise has power to elect and appoint more than 50% of its directors.
 - b) Control refers to an ownership directly or indirectly through subsidiaries, of more than one half of voting power of an enterprise.
 - c) Substantial ownership/affiliation means beneficial shareholding of more than 25%² by a person and/or by his dependent family members, which will include his/her spouse, dependent lineal ascendants and descendants and dependent brothers and sisters. However, shareholding in or by the Government owned entities and financial institutions will not constitute substantial ownership/affiliation, for the purpose of these regulations.
20. Independent Director means such a person who is not linked directly or indirectly with bank/DFI or its sponsor or strategic shareholders. For the purpose of such determination, an "independent director" is a director who:
 - Has not been employed by Bank /DFI within the last five years;
 - Has not been an employee or affiliate of any present or former external auditor/consultant/legal advisor of Bank/DFI within the last three years;
 - Has not been an executive officer or employee of a subsidiary or associate company of the bank/DFI or where Directors of the bank/DFI has substantial beneficial interest (20% or more shareholding of director's own or combined with family members);

¹ Inserted vide BPRD Circular No. 04 of 2007 dated April 23, 2007.

² In update as of January 31, 2009, erroneously written as 20%.

- Has not been employed by a company of which an executive officer of Bank/DFI has been a director within the last three years;
- Is not affiliated with a not-for-profit entity that received contributions from Bank/DFI exceeding the greater of 10 million or 2 percent of such charitable organization's consolidated gross revenues during the current fiscal year or any of the last three completed fiscal years.

(Note: An independent director shall submit a declaration for his/her independence to SBP at the time of his/her appointment.)

21. Key Executive¹ means key executives of banks/DFIs and includes the following functional responsibilities for the present:

- a) Any executive, acting as second to CEO including Chief Operating Officer, Deputy Managing Director or by whatever name called
- b) Chief Financial Officer/Head of Finance/Head of Accounts
- c) Head of Internal Audit
- d) Country Treasurer
- e) Head of Credit/Risk Management
- f) Head of Operations
- g) Head of Compliance
- h) Head of Human Resource
- i) Head of Information Technology
- j) Head of Islamic Banking
- k) Head of overseas operations of a bank at head office level
- l) Country Head/Regional Head (where a region is consisting of more than one foreign countries)
- m) CEO/Head of subsidiary banking company outside Pakistan
- n) CEO of Joint Venture (where majority stake is with the bank incorporated in Pakistan & authority to appoint CEO)²

The above list will be reviewed from time to time by SBP.

22. Liquid Assets are the assets which are readily convertible into cash without recourse to a court of law and mean encashment/realizable value of government securities, bank deposits, certificates of deposit, shares of listed companies which are actively traded on the stock exchange, NIT Units, certificates of mutual funds, Certificates of Investment (COIs) issued by DFIs/NBFCs rated at least 'A' by a credit rating agency on the approved panel of State Bank of Pakistan, listed TFCs rated at least 'A' by a credit rating agency on the approved panel of State Bank of Pakistan and certificates of asset management companies for which there is a book maker quoting daily offer and bid rates and there is active secondary market trading. These assets with appropriate margins should be in possession of the banks/DFIs with perfected lien.

Guarantees issued by domestic banks/DFIs when received as collateral by banks/DFIs will be treated at par with liquid assets whereas, for guarantees issued by foreign banks, the issuing banks' rating, assigned either by Standard & Poors, Moody's or Fitch-Ibca, should be 'A' and above or equivalent.

¹ Definition of 'Key Executive' shifted from Part-B, Regulation G-1.

² k) to n) inserted vide BPRD Circular No. 05 of 2009 dated March 05, 2009.

The inter-branch indemnity/guarantee issued by the bank's overseas branch in favor of its sister branch in Pakistan, would also be treated at par with liquid assets, provided the bank is rated 'A' and above or equivalent either by Standard & Poors, Moody's, Fitch-Ibca or Japan Credit Rating Agency (JCRA). The indemnity for this purpose should be similar to a guarantee i.e. unconditional and demand in nature.

23. Major Shareholder of a bank/DFI means any person holding 5% or more of the share capital of a bank/DFI either individually or in concert with family members. Family members have the same meaning as defined in the Banking Companies Ordinance, 1962.
24. Medium and Long Term Facilities mean facilities with maturities of more than one year and Short Term Facilities mean facilities with maturities up to one year.
25. NBFC means Non-Banking Finance Company and includes a Modaraba, Leasing Company, Housing Finance Company, Investment Bank, Discount House, Asset Management Company and a Venture Capital Company.
26. Nominee Director means a person nominated on the board of a bank/DFI by sponsor(s), persons, company, institution etc. by virtue of his/their shareholding in a bank/DFI.
27. Other Form of Security means hypothecation of stock (inventory), assignment of receivables, lease rentals, contract receivables, etc.
28. PBA means Pakistan Banks Association.
29. Person means and includes an individual, a Hindu undivided family, a firm, an association or body of individuals whether incorporated or not, a company and every other juridical person.
30. Readily Realizable Assets mean and include liquid assets and stocks pledged to the banks/DFIs in possession, with 'perfected lien' duly supported with complete documentation.
31. Secured means exposure backed by tangible security and any other form of security with appropriate margins (in cases where margin has been prescribed by State Bank, appropriate margin shall at least be equal to the prescribed margin). Exposure without any security or collateral is defined as clean.

The banks/DFIs may also take exposure against Trust Receipt. They are, however, free to take collateral/securities, to secure their risks/exposure, in addition to the Trust Receipt.

Banks/DFIs will be free to decide about obtaining security/collateral against the L/C facilities for the interim period, i.e. from the date of opening of L/C till the receipt of title documents to the goods.

32. Sponsor Shares¹ mean 5% or more paid-up shares of a bank, acquired by a person(s) individually or in concert with his family members (including his spouse, lineal ascendants and descendants and dependent brothers and sisters),

¹ Introduced vide BPRD Circular 4 of 2008 dated May 22, 2008.

group companies, subsidiaries, and affiliates/associates. Such acquisition of shareholding will include all the shares acquired by aforesaid person(s) including, inter alia, through (a) as original subscriber/promoter of the bank; (b) subsequent right/bonus issues; (c) market based acquisition deal; (d) reconstruction/restructuring of a bank carried out by SBP; (e) strategic sale through privatization (f) amalgamation of banking companies; or (g) any other mode of acquisition. All shares acquired by common shareholders, who are also sponsor shareholders, of amalgamating banking companies in amalgamation transaction shall be considered Sponsor Shares.

33. Sponsor Shareholders¹ mean all those shareholders of a bank holding sponsor shares.
34. Sponsor Director¹ means the member of the Board of Directors of a bank holding sponsor shares.
35. Strategic Investment is an investment which a bank/DFI makes with the intention to hold it for a period of minimum 5 years.

The following must be noted further in respect of strategic investment:

- a. The bank should mark strategic investment as such at the time of investment.
 - b. If there are a series of purchases of stocks of a company, the minimum retention period of 5 years shall be counted from the date of the last purchase.
 - c. The banks/DFIs will report their investment in strategic portfolio to the Banking Policy Department, within 2 working days from the date of such investment.
36. Subordinated Loan means an unsecured loan, extended to the borrower for a minimum original maturity period of 5 years, subordinate to the claim of the bank/DFI taking exposure on the borrower, and documented by a formal subordination agreement between provider of the loan and the bank/DFI. The loan shall be disclosed in the annual audited financial statements of the borrower as subordinated loan.
 37. Substantial ownership/affiliation² means beneficial shareholding of more than 20% by a person and/or by his dependent family members, which will include his/her spouse, dependent lineal ascendants and descendants and dependent brothers and sisters. However, shareholding in or by the Government owned entities and financial institutions will not constitute substantial ownership/affiliation, for the purpose of these regulations.
 38. Tangible Security means readily realizable assets (as defined in these Prudential Regulations), mortgage of land, plant, building, machinery and any other fixed assets.
 39. Underwriting Commitments mean commitments given by commercial banks/DFIs to the limited companies at the time of new issue of equity/debt instrument, that in case the proposed issue of equity/debt instrument is not fully subscribed, the un-subscribed portion will be taken up by them (commercial banks/DFIs).

¹ Introduced vide BPRD Circular 4 of 2008 dated May 22, 2008.

² Introduced vide BPRD Circular No. 04 of 2007 dated April 23, 2007. This is for the purpose of Regulation G-1 only.

PART - B
REGULATIONS

REGULATION R-1

LIMIT ON EXPOSURE TO A SINGLE PERSON/GROUP

The total outstanding exposure (fund based and non-fund based) by a bank/DFI to any single person shall not at any point in time exceed 30% of the bank's/DFI's equity as disclosed in the latest audited financial statements, subject to the condition that the maximum outstanding against fund based exposure does not exceed 20% of the bank's/DFI's equity.

2. The total outstanding exposure (fund based and non-fund based) by a bank/DFI to any group shall not exceed 50% of the bank's/DFI's equity as disclosed in the latest audited financial statements, subject to the condition that the maximum outstanding against fund based exposure does not exceed 35% of the bank's/DFI's equity.

3. Limit on exposure to a single person/Group effective from 31-12-2009 and onward would be as under:

Effective date	Exposure limit as a % of bank's/DFI's equity (as disclosed in the latest audited financial statements)			
	For single person		For group	
	Total outstanding (fund and non-fund based) exposure limit	Fund based outstanding limit	Total outstanding (fund and non-fund based) exposure limit	Fund based outstanding limit
31-12-2009	30	20	45	35
31-12-2010	30	20	40	35
31-12-2011	30	20	35	30
31-12-2012	30	20	30	25
31-12-2013	25	25	25	25

4. The group will cover both corporate entities as well as SMEs, in cases where such entities are owned by the same group.

5. For the purpose of this regulation banks/DFIs are required to follow the guidelines given at Annexure-I.

REGULATION R-2

LIMIT ON EXPOSURE AGAINST CONTINGENT LIABILITIES

Contingent liabilities of a bank/DFI shall not exceed at any point in time 10 times of its equity. Following shall not constitute contingent liabilities for the purpose of this regulation:

a) Bills for collection.

- b) Obligations under Letters of Credit and Letters of Guarantee to the extent of cash margin retained by the bank/DFI.
- c) Letters of credit/guarantee where the payment is guaranteed by the State Bank of Pakistan/Federal Government or banks/DFIs rated at least 'A' by a credit rating agency on the approved panel of State Bank of Pakistan or Standard & Poors, Moody's, Fitch-Ibca or Japan Credit Rating Agency (JCRA).
- d) Non-fund based exposure to the extent covered by liquid assets.
- e) Claims other than those related to provision of facilities (fund based or non-fund based) to the banks'/DFIs' constituents, where the probability of conversion of these claims into liabilities are remote.

2. For the purpose of this regulation, weightage of 50% shall be given to bid/mobilization advance/performance bonds and 10% to forward foreign exchange contracts.

REGULATION R-3

MINIMUM CONDITIONS FOR TAKING EXPOSURE

While considering proposals for any exposure (including renewal, enhancement and rescheduling/restructuring) exceeding such limit as may be prescribed by State Bank of Pakistan from time to time (presently at Rs 500,000), banks/DFIs should give due weightage to the credit report relating to the borrower and his group obtained from Credit Information Bureau (CIB) of State Bank of Pakistan. However, banks/DFIs may take exposure on defaulters keeping in view their risk management policies and criteria, provided they properly record reasons and justifications in the approval form. The condition of obtaining CIB report will apply to exposure exceeding Rs 500,000/- after netting-off the liquid assets held as security.

2. Banks/DFIs shall, as a matter of rule, obtain a copy of financial statements duly audited by a practicing Chartered Accountant, relating to the business of every borrower who is a limited company or where the exposure of a bank/DFI exceeds Rs 10 million, for analysis and record. The banks/DFIs may also accept a copy of financial statements duly audited by a practicing Cost and Management Accountant in case of a borrower other than a public company or a private company which is a subsidiary of a public company. However effective from December 31, 2009, if the borrower is a public limited company and exposure exceeds Rs. 500 million, banks/DFIs should obtain the financial statements duly audited by a firm of Chartered Accountants which has received satisfactory rating under the Quality Control Review (QCR) Program of the Institute of Chartered Accountants of Pakistan. Subsequently, if the firm's rating is downgraded in QCR program, then the financial statements of such borrowers are audited in the subsequent year by a firm having satisfactory rating under QCR.¹ Banks/DFIs may waive the requirement of obtaining copy of financial statements when the exposure net of liquid assets does not exceed the limit of Rs 10 million. Further, financial statements signed by the borrower will suffice where the exposure is fully secured by liquid assets.

3. Banks/DFIs shall not approve and/or provide any exposure (including renewal, enhancement and rescheduling/restructuring) until and unless the Loan Application Form (LAF) prescribed by the banks/DFIs is accompanied by a

¹ Substituted vide BPRD Circular No. 3 of 2009 dated February 11, 2009.

'Borrower's Basic Fact Sheet' under the seal and signature of the borrower as per approved format of the State Bank of Pakistan (Annexure II-A for corporate borrowers and Annexure II-B for individual borrowers).

REGULATION R-4
LIMIT ON EXPOSURE AGAINST
UNSECURED FINANCING FACILITIES

Banks/DFIs shall not provide unsecured/clean financing facility in any form of a sum exceeding Rs 500,000/- (Rupees five hundred thousand only) to any one person. Financing facilities granted without securities including those granted against personal guarantees shall be deemed as 'clean' for the purpose of this regulation. Further, at the time of granting a clean facility, banks/DFIs shall obtain a written declaration to the effect that the borrower in his own name or in the name of his family members, has not availed of such facilities from other banks/DFIs so as to exceed the prescribed limit of Rs 500,000/- in aggregate.

2. For the purpose of this regulation, following shall be excluded/exempted from the per party limit of Rs 500,000/- on the clean facilities:

- a) Facilities provided to finance the export of commodities eligible under Export Finance Scheme.
- b) Financing covered by the guarantee of Pakistan Export Finance Guarantee Agency.
- c) Loans/advances given to the employees of the banks/DFIs in accordance with their entitlement/staff loan policy.
- d) Investment in COIs/inter bank placements with NBFCs, provided the investee NBFC is rated 'A+', 'A' or 'A-' for long-term rating and at least 'A2' for short-term rating or equivalent by a credit rating agency on the approved panel of the State Bank of Pakistan or Standard & Poors, Moody's, Fitch-Ibca or Japan Credit Rating Agency (JCRA).n instructions, will be exempted from the aggregate exposure limit.

3. Banks/DFIs shall ensure that the aggregate exposure against all their clean facilities shall not, at any point in time, exceed the amount of their equity. However, investment of banks/DFIs in subordinated and unsecured TFCs, issued by other banks/DFIs to raise Tier-II Capital as per State Bank of Pakistan's instructions, will be exempted from the aggregate exposure limit.

REGULATION R-5
LINKAGE BETWEEN FINANCIAL INDICATORS
OF THE BORROWER AND TOTAL EXPOSURE
FROM FINANCIAL INSTITUTIONS

While taking any exposure, banks/DFIs shall ensure that the total exposure (fund-based and/or non-fund based) availed by any borrower from financial institutions does not exceed 10 times of borrower's equity as disclosed in its financial statements (obtained in accordance with para 2 of Regulation R-3), subject to the condition that the fund based exposure does not exceed 4 times of its equity as disclosed in its financial statements. However, where the equity of a borrower is negative and the borrower has injected fresh equity during its current accounting year, it will be

eligible to obtain finance up to 4 times of the fresh injected equity (instead of the existing 3 times) provided the borrower shall plough back at least 80% of the net profit each year until such time that it is able to borrow without this relaxation. After 30th June 2009, the borrower will be eligible only upto 3 times of his fresh injected equity.

In exceptional cases, banks/DFIs may allow seasonal financing to borrowers, for a maximum period of six months, not meeting the criteria of 4 times of fund based exposure and 10 times total exposure, subject to the condition that fund based exposure does not exceed 8 times and total exposure does not exceed 12 times of borrower's equity. In case of NBFCs, the total exposure (i.e. fund based and/or non-fund based) availed by any NBFC from financial institutions shall not exceed 10 times of its equity, without the restriction of fund based exposure to be 4 times as in case of other types of borrowers.

2. At the time of allowing fresh exposure/enhancement/renewal, the banks/DFIs should ensure that the current assets to current liabilities ratio of the borrower is not lower than such ratio as may be required under the Credit Policy of the bank/DFI. Banks/DFIs shall prescribe the minimum current ratio under their Credit Policy keeping in view the quality of the current assets, nature of the current liabilities, nature of industry to which borrower belongs to, average size of current ratio of that industry, appropriateness of risk mitigants available to the bank/DFI etc. It is expected that bank/DFI's Credit Policy, duly approved by the Board of Directors, shall emphasize higher credit standards and provide full guidance to the management about the current ratio requirement for various categories of clients and corresponding risk mitigants etc. acceptable to the bank/DFI.¹

3. For the purpose of this regulation, subordinated loans shall be counted as equity of the borrower. Banks/DFIs should specifically include the condition of subordinated loan in their Offer Letter. The subordination agreement to be signed by the provider of the subordinated loan, should confirm that the subordinated loan will be repaid after that bank's/DFI's prior approval.

4. This regulation shall not apply in case of exposure fully secured against liquid assets held as collateral, as well as in cases where the exposure is taken on Units/Projects revived as a consequence of settlement under Committee for Revival of Sick Industrial Units (CRSIU), Corporate & Industrial Restructuring Corporation (CIRC) and the State Bank of Pakistan BPD Circular No. 29 dated October 15, 2002, for a period of five years from the date of such settlement. Export finance and finance provided to ginning and rice husking factories shall also be excluded from the borrowings (exposure) for the purpose of this regulation.

5. Where the banks/DFIs have taken exposure on exceptional basis as provided in para 1 above, they shall record in writing the reasons and justifications for doing so in the approval form and maintain a file in their central credit office containing all such approvals. The Exceptions Approval file shall be made available to the inspection team of State Bank during the inspection.

¹ Amended vide BPRD Circular No. 6 of 2009 dated March 7, 2009

REGULATION R-6
EXPOSURE AGAINST SHARES/TFCs
AND ACQUISITION OF SHARES

1. A) EXPOSURE AGAINST SHARES/TFCs:

Banks/DFIs shall not:

- a) take exposure against the security of shares/TFCs issued by them.
- b) provide unsecured credit to finance subscription towards floatation of share capital and issue of TFCs.
- c) take exposure against the non-listed TFCs or the shares of companies not listed on the Stock Exchange(s). However, banks/DFIs may make direct investment in non-listed TFCs.
- d) take exposure on any person against the shares/TFCs issued by that person or its subsidiary companies. For the purpose of this clause, person shall not include individual.
- e) take exposure against 'sponsor director's shares' (issued in their own name or in the name of their family members) of banks/DFIs.
- f) take exposure on any one person (whether singly or together with other family members or companies owned and controlled by him or his family members) against shares of any commercial bank/DFI in excess of 5% of paid-up capital of the share issuing bank/DFI.
- g) take exposure against the shares/TFCs of listed companies that are not members of the Central Depository System.
- h) take exposure against unsecured TFCs or non-rated TFCs or TFCs rated below 'BBB' or equivalent. Exposure may, however, be taken against unsecured/subordinated TFCs, which are issued by the banks/DFIs for meeting their minimum capital requirements, as per terms and conditions stipulated in BSD Circular No. 12 of August 25, 2004.
- i) take exposure against shares unless the beneficiary of the facility is absolute owner of the shares so pledged or has the necessary mandate to pledge the shares of third party as security for availing financing facility from the bank/ DFI.

B) ACQUISITION OF SHARES:

- a) Banks/DFIs shall not own shares of any company/scripts in excess of 5% of their own equity. Further, the total investments of banks in shares should not exceed 20% of their own equity. DFIs which are not mobilizing funds as deposits/COIs from general public/individuals will be exempt from the requirement of capping their total investment in equities. However, DFIs which are mobilizing funds as deposits/COIs from general public/individuals will be required to contain their investment in shares upto 35% of their equity. The shares will be valued at cost of acquisition for the purpose of calculating bank's/DFI's exposure under this regulation. The investments of the bank/DFI in its subsidiary companies (listed as well as non-listed) and strategic investments of the bank/DFI, shall not be included in these limits. The shares acquired in excess of 5% limit due to the underwriting commitments will be sold off/off loaded within a period of three months.

The condition of capping aggregate exposure shall also be applicable on Islamic banks to the extent of 35% of their equity. For the purpose of this regulation, shares will also include units of all forms of Mutual Funds excluding NIT units till its privatization.

b) Banks/DFIs may also take exposure in future contracts to the extent of 10% of their equity on aggregate basis. In this connection, the 10% exposure limit for future contracts will include both positions taken in futures buying and selling.

c) Banks/DFIs may combine the limits for ready market and future contracts and have the aggregate exposure in shares to the extent of 30% of their equity (in case of Islamic Banks/DFIs upto 45% of their equity) provided that investment in future contracts shall not exceed 10% of their equity. In order to facilitate development of Real Estate Investment Trusts (REIT) in Pakistan, banks/DFIs' investment in units of REIT shall not be counted towards the aggregate investment limits of 30% and 45% of equity of the banks and Islamic banks/DFIs respectively.¹

d) Banks/DFIs will obtain prior approval from the State Bank while purchasing shares of a company in excess of 5% of their paid-up capital or 10% of the capital of investee company, whichever is lower. These limits will be calculated as under:

- In the case of investee company, 10% limit will be calculated by taking 10% of the number of its paid-up shares.
- In the case of investing bank, 5% limit will be calculated by taking 5% of paid-up shares of the bank and then multiplying with their face value.

The bank's/DFI's request will be considered in the light of the nature of relationship of the investing bank and the investee company. Further, other factors, such as financial standing of the investing bank, its aggregate investment portfolio, experience in managing the same, efficacy of internal controls etc. will also be taken into account.

In case, shares in excess of above limit are acquired by the bank/DFI through settlement of a facility or by any other means, the information to this effect will be conveyed to the State Bank of Pakistan within three days of the acquisition of such shares. Furthermore, the shares so acquired should be disposed off within one year to comply with the limits given above.²

e) Regarding strategic investment, the banks/DFIs will exercise proper diligence, as their decision to make strategic investment carries great significance, keeping in view the implications of such investment in terms of liquidity management and long term outlook of the investee companies. In this regard, the banks/DFIs should take into account all relevant factors. Accordingly, the following should be ensured:

¹ Inserted vide BPRD Circular Letter No. 15 of 2010 dated July 5, 2010.

² Instruction at d) introduced vide BPD Circular No.09 of 2006 dated July 29, 2006.

- A committee, clearly designated/empowered by the bank, should take the decision for strategic investment.
- All Record of transactions/decisions, taken by the committee, regarding strategic investment should be properly maintained and kept in a separate file, for provision of the same to the SBP Inspection Team during their visit to the bank.
- The banks/DFIs will report their investment in strategic portfolio to the Banking Policy Department, within 2 working days from the date of such investment.

f) While calculating the maximum limit for investment in shares, the amount of provisions created against permanent diminution by debiting the Profit & Loss account, as instructed vide BSD Circular No.10 dated July 13, 2004, may be deducted from the cost of acquisition of such investments and the maximum limit. Further, investment in preference shares, which fulfill the criteria of equity instrument as laid down in Part-A of these regulations, shall be considered as part of investment in equities. Correspondingly, any investment in preference shares that do not conform to these conditions shall not be included in the limits prescribed under this regulation. However, such investment portfolio will be considered as part of the maximum exposure limit as prescribed under R-1 of these regulations.

2. Banks/DFIs shall not hold shares in any company whether as pledgee, mortgagee, or absolute owner, of an amount exceeding 30% of the paid-up share capital of that company or 30% of their own paid-up share capital and reserves, whichever is less.

3. Exposure against the shares of listed companies shall be subject to minimum margin of 30% of their current market value, though the banks/DFIs may, if they wish, set higher margin requirements keeping in view other factors. However, banks/DFIs should not give a margin call until the margin reaches to the level of 25%. Banks/DFIs will monitor the margin on at least weekly basis and will take appropriate action for top-up and sell-out on the basis of their Board of Directors' approved credit policy and pre-fact written authorization from the borrower enabling the bank/DFI to do this.

4. Exposure against TFCs rated 'A' (or equivalent) and above by a credit rating agency on the approved panel of State Bank of Pakistan shall be subject to a minimum margin of 10% while the exposure against TFCs rated 'A-' and 'BBB' shall be subject to a minimum margin of 20%.

REGULATION R-7 GUARANTEES

All guarantees issued by the banks/DFIs shall be fully secured, except in the cases mentioned at Annexure-III where it may be waived up to 50% by the banks/DFIs at their own discretion, provided that banks/DFIs hold at least 20% of the guaranteed amount in the form of liquid assets as security.

2. The requirement of security can also be waived by the banks/DFIs in cases of guarantees issued to Pakistani firms and companies functioning in Pakistan against the back to back/counter guarantees of branches of guarantee issuing bank/DFI or banks/DFIs rated at least 'A' or equivalent by a credit rating agency on the approved panel of State Bank of Pakistan or Standard & Poor, Moody's, Fitch-Ibca or Japan Credit Rating Agency (JCRA). Besides, in case the counter-guarantee issuing bank is situated in a foreign country, the rating of at least 'A' or equivalent by a local credit rating agency of the respective country shall also be acceptable, provided the guarantee issuing bank in Pakistan is comfortable with and accepts the counter-guarantee of such foreign bank. However, the prescribed rating requirement for banks situated in foreign countries may be relaxed for transaction amount up to US\$250,000, subject to internal credit controls and approvals of the concerned bank/DFI in Pakistan. For transaction amounts greater than US\$250,000, banks/DFIs may approach the State Bank of Pakistan for specific approvals/exemption, on case by case basis, where the prescribed minimum rating requirement cannot be complied with. The banks/DFIs are encouraged to set limits for acceptance of guarantees issued by other banks/DFIs.

3. In case of back to back letter of credit issued by the banks/DFIs for export oriented goods and services, banks/DFIs are free to decide the security arrangements at their own discretion subject to the condition that the original L/C has been established by branches of guarantee issuing bank or a bank rated at least A by Standard & Poor, Moody's, Fitch-Ibca or Japan Credit Rating Agency (JCRA).

4. The guarantees shall be for a specific amount and expiry date and shall contain claim lodgment date. However, banks/DFIs are allowed to issue open-ended guarantees without clearance from State Bank of Pakistan provided banks/DFIs have secured their interest by adequate collateral or other arrangements acceptable to the bank/DFI for issuance of such guarantees in favour of Government departments, corporations/autonomous bodies owned/controlled by the Government and guarantees required by the courts.

REGULATION R-8

CLASSIFICATION AND PROVISIONING FOR ASSETS

LOANS/ADVANCES:

Banks/DFIs shall observe the prudential guidelines given at Annexure-IV in the matter of classification of their asset portfolio and provisioning there-against.

2. In addition to the time-based criteria prescribed in Annexure-IV, subjective evaluation of performing and non-performing credit portfolio shall be made for risk assessment and, where considered necessary, any account including the performing account will be classified, and the category of classification determined on the basis of time based criteria shall be further downgraded. Such evaluation shall be carried out on the basis of credit worthiness of the borrower, its cash flow, operation in the account, adequacy of the security, inclusive of its realizable value and documentation covering the advances.

3. The rescheduling/restructuring of non-performing loans shall not change the status of classification of a loan/advance etc. unless the terms and conditions of rescheduling/restructuring are fully met for a period of at least one year (excluding grace period, if any) from the date of such rescheduling/restructuring and at least 10% of the outstanding amount is recovered in cash. However, the condition of one year retention period, prescribed for restructured/rescheduled loan account to remain in the classified category, will not apply in case the borrower has repaid or adjusted in cash at least 50% of the total restructured loan amount (principal + mark-up), either at the time of restructuring agreement or later-on during the grace period if any.

The unrealized mark-up on loans (declassified after rescheduling/restructuring) shall not be taken to income account unless at least 50% of the amount is realized in cash. However, any short recovery in this respect will not impact the declassification of this account if all other criteria (meeting the terms and conditions for at least one year and payment of at least 10% of outstanding amount by the borrower) are met. The banks/DFIs are further directed to ensure that status of classification, as well as provisioning, is not changed in relevant reports to the State Bank of Pakistan merely because a loan has been rescheduled or restructured. However, while reporting to the Credit Information Bureau (CIB) of State Bank of Pakistan, such loans/advances may be shown as 'rescheduled/restructured' instead of 'default'.

Where a borrower subsequently defaults (either principal or mark-up) after the rescheduled/restructured loan has been declassified by the bank/DFI as per above guidelines, the loan will again be classified in the same category it was in at the time of rescheduling/restructuring and the unrealized markup on such loans taken to income account shall also be reversed. However, banks/DFIs at their discretion may further downgrade the classification, taking into account the subjective criteria.

At the time of rescheduling/restructuring, banks/DFIs shall consider and examine the requests for working capital strictly on merit, keeping in view the viability of the project/business and appropriately securing their interest etc.

All fresh loans granted by the banks/DFIs to a party after rescheduling/restructuring of its existing facilities may be monitored separately, and will be subject to classification under this Regulation on the strength of their own specific terms and conditions.

4. Banks/DFIs shall classify their loans/advances portfolio and make provisions in accordance with the criteria prescribed above, keeping in view the following:

a) Banks are allowed to take the benefit of 40% of Forced Sale value (FSV) of the pledged stocks and mortgaged residential, commercial and industrial properties (where building is constructed) held as collateral against NPLs for three years from the date of classification for calculating provisioning requirement. However, the banks/DFIs can avail the benefit of 40% of FSV of mortgaged residential, commercial and industrial land (open plot and where building is constructed separate valuation of land must be available) held as collateral against NPLs for four years from the date of classification for calculating provisioning requirement. This benefit would be available in such cases where FSV valuation of land is not more

than four years old. For the purpose of determination of FSV, revised Annexure-V of PR for Corporate/Commercial Banking shall be followed.¹

b) Banks/DFIs may avail the above benefit of FSV subject to compliance with the following conditions:

- i) The additional impact on profitability arising from availing the benefit of FSV against pledged stocks and mortgaged residential, commercial and industrial properties (land and building only) ¹ shall not be available for payment of cash or stock dividend.
- ii) Heads of Credit of respective banks/DFIs shall ensure that FSV used for taking benefit of provisioning is determined accurately as per guidelines contained in PRs and is reflective of market conditions under forced sale situations.
- iii) Party-wise details of all such cases where banks/DFIs have availed the benefit of FSV shall be maintained for verification by State Bank's inspection teams during regular /special inspection.

c) Any misuse of FSV benefit detected during regular /special inspection of SBP shall attract strict punitive action under the relevant provisions of the Banking Companies Ordinance, 1962. Furthermore, SBP may also withdraw the benefit of FSV from banks/DFIs found involved in its misuse.

INVESTMENTS AND OTHER ASSETS:

5. The banks shall classify their investments into three categories viz. 'Held for Trading', 'Available for Sale' and 'Held to Maturity'. However, investments in subsidiaries and associates shall be reported separately in accordance with International Accounting Standards as applicable in Pakistan and shall not be subject to mark to market.

Investment portfolio in 'Held for Trading' and 'Available for Sale' and other assets will be subject to detailed evaluation for the purpose of their classification keeping in view various subjective and objective factors given as under

a) Quoted Securities:

Government Securities will be valued at PKRV (Reuter Page). TFCs, PTCs and shares will be valued at their market value. The difference between the market value and book value will be treated as surplus/deficit.

b) Un-quoted Securities:

PTCs and TFCs will be classified on the evaluation/inspection date on the basis of default in their repayment in line with the criteria prescribed for classification of medium and long-term facilities. Shares will be carried at the cost. However, in cases where the breakup value of such shares is less than the cost, the difference of the cost and breakup value will be classified as loss and provided for accordingly by charging to the Profit and Loss account of the bank/DFI.

c) Treatment of Surplus/deficit:

The measurement of surplus/deficit shall be done on portfolio basis. The surplus/deficit arising as a result of revaluation of 'Held for Trading' securities shall

¹ Amended vide BSD Circular No. 02 of 2010 dated June 3, 2010.

be taken into Profit & Loss Account. The surplus/deficit on revaluation of 'Available for Sale' category shall be taken to "Surplus/Deficit on Revaluation of Securities". Impairment in the value of 'Available for Sale' or 'Held to Maturity' securities will be provided for by charging it to the Profit and Loss Account.

d) Other Assets:

Classification of Other Assets and provision required there-against shall be determined keeping in view the risk involved and the requirements of the International Accounting Standards.

TIMING OF CREATING PROVISIONS:

6. Banks/DFIs shall review, at least on a quarterly basis, the collectibility of their loans/advances portfolio and shall properly document the evaluations so made. Shortfall in provisioning, if any, determined, as a result of quarterly assessment shall be provided for immediately in their books of accounts by the banks/DFIs on quarterly basis.

REVERSAL OF PROVISION:

7. In case of cash recovery, other than rescheduling/restructuring, banks/DFIs may reverse specific provision held against classified assets, subject to the following:

- (a) In case of Loss account, reversal may be made to the extent that the remaining outstanding amount of the classified asset is covered by minimum 100% provision.
- (b) In case of Doubtful account, reversal may be made to the extent that the remaining outstanding amount of the classified asset is covered by minimum 50% provision.
- (c) In case of Substandard account, reversal may be made to the extent that the remaining outstanding amount of the classified asset is covered by minimum 25% provision.

While calculating the remaining provision required to be held after cash recovery and reversal of provision there-against, the banks/DFIs will enjoy the benefit of netting-off the amount of liquid assets from the outstanding amount, in the light of guidelines given in this regulation. However, the provision made on the advice of State Bank of Pakistan will not be reversed without prior approval of State Bank of Pakistan.

VERIFICATION BY THE AUDITORS:

8. The external auditors as a part of their annual audits of banks/DFIs shall verify that all requirements of Regulation R-8 for classification and provisioning for assets have been complied with. The State Bank of Pakistan shall also check the adequacy of provisioning during on-site inspection.

REGULATION R-9

ASSUMING OBLIGATIONS ON BEHALF OF NBFCs

Banks/DFIs shall not issue any guarantee or letter of comfort nor assume any obligation whatsoever in respect of deposits, sale of investment certificates, issue of commercial papers, or borrowings of any non-banking finance company.

Banks/DFIs may, however, underwrite TFCs, commercial papers and other debt instruments issued by NBFCs, and issue guarantees in favor of multilateral agencies for providing credit to NBFCs, provided the banks'/DFIs' such exposure remains within the per party exposure limit as prescribed in Regulation R-1. Banks/DFIs may also allow exposure to any of their client against the guarantee of an NBFC which is rated at least 'A' or equivalent by a credit rating agency on the approved panel of State Bank of Pakistan. The total amount of guarantees issued by an NBFC, and accepted by the banks, on the strength of which the exposure will be allowed by the commercial bank/DFI, will not exceed per party limit of the bank/DFI as mentioned in Regulation R-1. Before taking exposure against the guarantee of NBFC, banks/DFIs shall ensure that total guarantees issued by an NBFC in favour of banks/DFIs do not exceed 2.5 times of capital of the NBFC as evidenced by the latest available audited financial statements of the NBFC and such other means as the banks/DFIs may deem appropriate.

REGULATION R-10

FACILITIES TO PRIVATE LIMITED COMPANY

Banks/DFIs shall formulate a policy, duly approved by their Board of Directors, about obtaining personal guarantees of directors of private limited companies. Banks/DFIs may, at their discretion, link this requirement to the credit rating of the borrower, their past experience with it or its financial strength and operating performance.

REGULATION R-11

PAYMENT OF DIVIDEND

Banks/DFIs shall not pay any dividend on their shares unless and until:

- a) they meet the minimum capital requirements as laid down by the State Bank of Pakistan from time to time;
- b) all their classified assets have been fully and duly provided for in accordance with the Prudential Regulations and to the satisfaction of the State Bank of Pakistan; and
- c) all the requirements laid down in Banking Companies Ordinance, 1962 relating to payment of dividend are fully complied.

REGULATION R-12

MONITORING

While extending fund based facilities to borrowers against hypothecation of stock and/or receivables on pari-passu basis, banks/DFIs shall obtain monthly statements from borrowers that contain a bank-wise break-up of outstanding amounts with the total value of stocks and receivables there-against.

REGULATION R-13

MARGIN REQUIREMENTS

Banks/DFIs are free to determine the margin requirements on facilities provided by them to their clients taking into account the risk profile of the borrower(s) in order to secure their interests. However, this relaxation shall not apply in case of items, import of which are banned by the Government. Banks/DFIs are advised not to

open import letter of credit for these items in any case till such time the lifting of ban on any such item is notified by the State Bank of Pakistan.

2. Banks/DFIs will continue to observe margin restrictions on shares/TFCs as per existing instructions under Prudential Regulations for Corporate/Commercial Banking (R-6). Further, the cash margin requirement of 100% on Caustic Soda (PCT heading 2815.1200) for opening Import Letter of Credit as advised by the Federal Government and notified in terms of BPD Circular Letter No. 5 dated 4th May, 2002, will also continue to remain applicable.

3. State Bank of Pakistan shall continue to exercise its powers for fixation/reinstatement of margin requirements on financing facilities being provided by banks/DFIs for various purposes including Import Letter of Credit on a particular item(s), as and when required.

REGULATION G-1
CORPORATE GOVERNANCE/BOARD
OF DIRECTORS AND MANAGEMENT

The following guidelines are required to be followed by banks/DFIs incorporated in Pakistan. They will also follow 'Code of Corporate Governance' issued by the Securities & Exchange Commission of Pakistan (SECP) so long as any provision thereof does not conflict with any provision of the Banking Companies Ordinance, 1962, Prudential Regulations and the instructions/guidelines issued by the State Bank of Pakistan. Foreign banks are required to adhere to these guidelines wherever feasible and applicable. However, they need not necessarily seek approval of their Board of Directors, as stipulated below in the case of local banks/DFIs:

A. FIT AND PROPER TEST

The "Fit and Proper Test" (FPT) is applicable on the sponsors (both individual & companies) who apply for a commercial banking license, the investors acquiring strategic/controlling stake in the banks/DFIs, major shareholders of the banking companies and for the appointment of Directors, CEO, and Key Executives of the banks/DFIs. The fitness & propriety will be assessed on the following broad elements (Annexure VII-B):

- a) Integrity, Honesty & Reputation
- b) Track Record
- c) Solvency & Integrity
- d) Qualification & Experience
- e) Conflict of Interest
- f) Others

2. First three elements are applicable to all categories of individuals, whereas the last three elements will be considered while assessing the FPT of Directors, CEO & Key Executives of banks/DFIs. In addition to above requirements, sponsors and strategic investors are evaluated respectively in terms of "Guidelines & Criteria for setting up of a Commercial Bank" & "Criteria for Establishment of Islamic Commercial Banks" issued by SBP and Code of Corporate Governance issued by SECP.

3. The sponsors, the strategic investors, and appointment of the Directors and CEO require prior clearance in writing from SBP. The CEO and Key Executives shall be full time employees of the bank/DFI. The Directors and CEO will not assume the charge of their respective offices until their appointments are approved in writing by SBP. All the requests for seeking approval of SBP for appointment of Directors & CEO of the banks/DFIs should be routed through respective banks/DFIs along with information on Annexure-VI-A & VI-B.

4. The appointment of Key Executives will not require prior clearance of SBP. However, the banks/DFIs must themselves ensure while appointing Key Executives that they qualify FPT in letter and spirit. The information on appointment of Key Executive is required to be forwarded to SBP on prescribed format at Annexure-VII-A within seven days of assumption of the charge of the post by the incumbent. The information submitted may be checked on post fact basis by Banking Inspection Department of SBP during inspection.

5. The sponsors are required to seek prior approval of SBP along with the information at Annexure- VI-B and other information as required in the “Guidelines & Criteria for Setting up a Commercial Bank” and” Criteria for Establishment of Islamic Commercial Banks”. The strategic investors contemplating to acquire strategic/controlling stake are required to seek prior approval from SBP either directly or through the concerned department/Ministry of Government executing strategic sale transaction of the bank as required and provided in the transaction structure. The bank should also ensure to give prior intimation to SBP before dealing with any investors/bank/institutions/person for sale/purchase of sponsors/strategic shares and seek approval of SBP for conducting due diligence of bank/DFI in terms of BPD Circular No. 8 of 2003.

6. The major shareholders are required to seek prior approval in writing from SBP for acquiring 5% or more shares along-with information on Annexure- VI-B, with proper justification for holding more than 5% shares of the paid up capital. All the banks/DFIs are required to ensure that major shareholders have sought such an approval from SBP and place it on record.

7. Deposit of sponsor shares in blocked account with Central Depository Company of Pakistan (CDC).

- a) All sponsor shares and subsequent right and bonus shares shall be deposited in a blocked account with CDC. The procedure for deposit of sponsor shares in the CDC blocked account is provided at Annexure-XI.
- b) No withdrawal of the sponsor shares from the blocked account would be allowed without prior written permission of SBP.
- c) Blocked account should be opened by the sponsor shareholders of banks exclusively for deposit of the sponsor shares and subsequent right and bonus shares issued thereon.
- d) Charges for opening and operating of the blocked account with CDC will be borne by the sponsor shareholders.
- e) These instructions shall not be applicable to the shareholding of Federal and provincial governments in banks.

8. Fit & Proper Test prescribed in the guideline is continuous in nature. All persons subject to FPT should immediately submit any change in the information already submitted (at the time of clearance) either through Company Secretary or Human Resources Department to Banking Policy and Regulations Department. Violation of the instructions, circumvention, concealment, misreporting and delay in submission of information to SBP may result in withdrawal of SBP approval, besides penal action under the provisions of BCO.

B. RESPONSIBILITIES OF THE BOARD OF DIRECTORS:

The Board of Directors shall assume its role independent of the influence of the Management and should know its responsibilities and powers in clear terms. It should be ensured that the Board of Directors focus on policy making and general direction, oversight and supervision of the affairs and business of the bank/DFI and does not play any role in the day-to-day operations, as that is the role of the Management.

2. The Board shall approve and monitor the objectives, strategies and overall business plans of the institution and shall oversee that the affairs of the institution are carried out prudently within the framework of existing laws & regulations and high business ethics.
3. All the members of the Board should undertake and fulfill their duties & responsibilities keeping in view their legal obligations under all the applicable laws and regulations. All Board members should preferably attend at least 1-2 weeks training program(s) which will enable them to play effective role as a director of bank/DFI, at an institution like Pakistan Institute of Corporate Governance or other similar institution within first year of their directorship on the Board of bank/DFI.
4. The Board shall clearly define the authorities and key responsibilities of both the Directors and the Senior Management without delegating its policy-making powers to the Management and shall ensure that the Management is in the hands of qualified personnel.
5. The Board shall approve and ensure implementation of policies, including but not limited to, in areas of Risk Management, Credit, Treasury & Investment, Internal Control System and Audit, IT Security, Human Resource, Expenditure, Accounting & Disclosure, and any other operational area which the Board and/or the Management may deem appropriate from time to time. The Board shall also be responsible to review and update existing policies periodically and whenever circumstances justify.
6. As regards Internal Audit or Internal Control, a separate department shall be created which shall be manned preferably by professionals responsible to conduct audit of the bank's/DFI's various Divisions, Offices, Units, Branches etc. in accordance with the guidelines of the Audit Manual duly approved by the Board of Directors. The Head of this department will report directly to the Board of Directors or Board Committee on Internal Audit.
7. The business conditions and markets are ever changing and so are their requirements. The Board, therefore, is required to ensure existence of an effective 'Management Information System' to remain fully informed of the activities, operating performance and financial condition of the institution, the environment in which it operates, the various risks it is exposed to and to evaluate performance of the Management at regular intervals.
8. The Board should meet frequently (preferably on monthly basis, but in any event, not less than once every quarter) and the individual directors of an institution should attend at least half of the meetings held in a financial year. The Board should ensure that it receives sufficient information from Management on the agenda items well in advance of each meeting to enable it to effectively participate in and contribute to each meeting. Any advisor, if appointed by the Board member, shall neither attend the Board meeting(s) on behalf of the Board member nor shall regularly sit in the Board meeting(s) as an observer or any other capacity.
9. The Board should carry out its responsibilities in such a way that the external auditors and supervisors can see and form judgment on the quality of Board's work

and its contributions through proper and detailed minutes of the deliberations held and decisions taken during the Board meetings.

10. To share the load of activities, the Board may form specialized committees with well-defined objectives, authorities and tenure. These committees, preferably comprising of 'Non-Executive' Board members, shall oversee areas like audit, risk management, credit, recruitment, compensation etc. These committees of the Board should neither indulge in day-to-day affairs/operations of the bank nor enjoy any credit approval authority for transaction/limits. These committees should apprise the Board of their activities and achievements on regular basis.

11. The Board should ensure that it receives management letter from the external auditors without delay. It should also be ensured that appropriate action is taken in consultation with the Audit Committee of the Board to deal with control or other weaknesses identified in the management letter. A copy of that letter should be submitted to the State Bank of Pakistan so that it can monitor follow-up actions.

12. Whenever the Board of Directors/relevant appointing/removing authority of a bank/DFI considers to remove its President/Chief Executive Officer/Country Head/Country Manager before the expiration of his/her term of office through the defined statutory process, State Bank of Pakistan (SBP) must invariably be informed at least two months ahead of the implementation of such decision along-with the reasons for the same.

The President/CEO/Country Head/Country Manager, wherever, decides to tender resignation before completion of his/her term of office, he/she must inform SBP at least two months before tendering resignation.

The Chairman of the Board of Directors/relevant removing authority of bank/DFI would be responsible for submission of the requisite information to SBP.

C. MANAGEMENT:

No member of the Board of Directors of a bank/DFI holding 5% or more of the paid-up capital of the bank/DFI either individually or in concert with family members or concerns /companies in which he/she has the controlling interest, shall be appointed in the bank /DFI in any capacity except as Chief Executive of the bank/DFI. Further, maximum two members of Board of Directors of a bank/DFI including its CEO can be the Executive Directors.

2. The banks/DFIs during a calendar year may pay a reasonable and appropriate remuneration for attending the Board or its committee (ies) meeting (s), to their non-executive directors and chairman. The scale of remuneration to be paid to the non-executive directors and chairman for attending the Board and/or committee meetings shall be approved by the shareholders on a pre or post facto basis in the Annual General Meeting (AGM). However, no such remuneration shall be paid to the executive directors except usual TA/DA as per bank's/DFI's standard rules and regulations. No consultancy or allied work will be awarded to the non-

executive directors or to the firms/institutions/companies etc. in which they hold substantial interest.¹

3. Chairman of the Board of Directors may, if deemed necessary, appoint one advisor to advise and facilitate him in discharge of his duties/responsibilities. The appointment of such an advisor will be subject to the following conditions:

- a) The advisor must possess the required technical experience relating to banking and finance at a senior level to enable him /her to render a professional advice to the Board.
- b) The terms of reference of the advisor shall be approved by the Board.
- c) A reasonable remuneration may be paid to the advisor with the approval of the Board of Directors.
- d) The advisor may attend the meetings of Board of Directors and Board Committees in which his/her participation is required but he/she will not be a member of the Board and/or its committees.
- e) The advisor shall be required to sign an appropriate confidentiality agreement to ensure confidentiality of documents/information that may come to his/her knowledge, before assuming any such role.²

D. COMPLIANCE OFFICER:

Banks/DFIs shall put in place a Compliance Program to ensure that all relevant laws are complied with, in letter and spirit, and, thus, minimize legal and regulatory risks. For this purpose, the Board of Directors, or Country Manager in case of foreign banks, shall appoint/designate a suitably qualified and experienced person as Compliance Officer on a countrywide basis, who may be assisted by other Compliance Officers down the line. The Head of Compliance will report directly to the President/Chief Executive Officer of the bank/DFI. The Compliance Officers will primarily be responsible for bank's/DFI's effective compliance relating to:

- (a) SBP Prudential Regulations.
- (b) Relevant provisions of existing laws and regulations.
- (c) Guidelines for KYC.
- (d) Anti money laundering laws and regulations.
- (e) Timely submission of accurate data/returns to regulator and other agencies.
- (f) Monitor and report suspicious transactions to President/Chief Executive Officer of the bank/DFI and other related agencies.

2. Banks/DFIs are, however, free to add other areas of compliance under the responsibilities of Compliance Officer and consider setting up a compliance committee under him, as they deem fit to protect the interest of the institution.

3. The Compliance Officers will (i) serve as a contact point between President/Chief Executive Officer and senior management, with regard to functioning of the compliance program (ii) provide assistance in this area to branches and other departments of the bank/DFI, and (iii) act as liaison with State Bank of Pakistan concerning the issues related to compliance.'

¹ Amended vide BPRD Circular No. 14 of 2009 dated August 07, 2009.

² Substituted vide BPRD Circular Letter No. 12 of 2009 dated April 24, 2009.

4. Banks/DFIs are, therefore, advised to put in place, in writing, a complete program of compliance down the line under the supervision of a Compliance Officer.

E. FITNESS AND PROPRIETY OF KEY EXECUTIVES:

Banks/DFIs shall strictly follow the guidelines contained in the 'Fit and Proper Test' (FPT) during the course of appointment of key executives.¹

2. The banks/DFIs should also develop and implement appropriate screening procedures to ensure high standards and integrity at the time of hiring all employees, whether contractual or permanent.

3. In case it is found at subsequent stage/during the course of inspection that guidelines of FPT have not been followed or the incumbent is not a fit and proper person, strict punitive action will be taken under the relevant provisions of Banking Companies Ordinance 1962, in addition to directing the banks/DFIs to dispense with the services of concerned officer if recruited afresh; and in case of existing employee, the same to be transferred from the post immediately.

REGULATION G-2

DEALING WITH DIRECTORS, MAJOR SHARE-HOLDERS AND EMPLOYEES OF THE BANKS/DFIs

Banks/DFIs shall not enter into leasing, renting and sale/purchase of any kind with their directors, officers, employees or such persons who either individually or in concert with family members beneficially own 5% or more of the equity of the bank/DFI. This restriction does not apply in case of purchase of vehicles by the paid directors, officers or employees of the banks/DFIs which remained in their own use, provided such sale is covered under the employees service rules duly approved by the Board of Directors of the banks/DFIs and is effected by the banks/DFIs at least at book value at the date of such transaction.

2. Banks/DFIs shall not:

- a) take unsecured exposure on, or take exposure against the guarantee of:
 - i) any of their directors;
 - ii) any of the family members of any of their directors;
 - iii) any firm or private company in which the bank/DFI or any of the persons referred to in (i) or (ii) are interested as director, proprietor or partner; or
 - iv) any public limited company in which the bank/DFI or any of the persons as aforesaid are substantially interested; and
 - v) their Chief Executive and shareholders holding 5% or more of the share capital of the bank/DFI, including their spouses, parents, and children or to firms and companies in which they are interested as partners, directors or shareholders holding 5% or more of the share capital of that concern.
- b) take any exposure on any of their directors or to individuals, firms or companies in which they or any of their directors, either directly in the borrowing entity or in any of its group companies, hold key management positions, or are interested as partner, director or guarantor, as the case may be, their Chief Executives and

¹ Definition of 'Key Executives' shifted to Part-A.

shareholders holding 5% or more of the share capital of the bank/DFI, including their spouses, parents, and children or to firms and companies in which they are interested as partners, directors or shareholders holding 5% or more of the share capital of that concern, without the approval of the majority of the directors of that bank/DFI excluding the director concerned. The facilities to the persons mentioned above shall be extended at market terms and conditions and be dealt with at arm length basis.

REGULATION G-3

CONTRIBUTIONS AND DONATIONS FOR CHARITABLE, SOCIAL, EDUCATIONAL AND PUBLIC WELFARE PURPOSES

Banks/DFIs shall strictly observe the following rules in the matter of making any donation/contribution for charitable, social, educational or public welfare purposes:

- i) The total donations/contributions made by the bank/DFI during the year shall not exceed such amount as approved by their Board of Directors. It is expected that banks/DFIs making these donations/contributions would have already met provisioning and capital adequacy requirements.
- ii) The banks/DFIs shall develop policy/guidelines duly approved by the Board of Directors for making donations/contributions.

2. All donations or contributions to be made during the year must be specifically approved by the Board of Directors on pre or post facto basis as convenient.

3. Banks/DFIs are further directed to expressly disclose in their annual audited financial statements the total donation/contribution made during the year along with names of donees, to whom total donations/ contributions during the year were made in excess of Rs 100,000/. In the case of donations where any director or his family members have interest in the donee, the names of such directors, their interest in the donee and the names and addresses of all donees, shall also be given.

REGULATION G-4

CREDIT RATING

With a view to safeguard the interest of prospective investors, depositors and creditors, it shall be mandatory for all banks/DFIs to have themselves credit rated by a credit rating agency on the approved panel of the State Bank of Pakistan.

2. Foreign banks which are credit rated by M/s. Standard & Poor, Moody's Fitch-Ibca and Japan Credit Rating Agency (JCRA) are given a minimum rating of A3/A- and above shall be exempt from the application of this requirement. All other foreign banks have to go through credit rating process in Pakistan.

3. The credit rating will be an ongoing process i.e. credit rating should be updated on a continuous basis from year to year, within six months from the date of close of each financial year and the rating report complete in all respects be submitted to the State Bank of Pakistan and made public within a period of seven days of the notification of rating by the credit rating agency. Further, the banks/DFIs will disclose their credit rating prominently in their published annual and quarterly financial statements.

REGULATION M-1
CUSTOMER DUE DILIGENCE (CDD) ¹

With the view to preserve integrity and safety of the financial system, it is expedient to prevent the possible use of the banking sector for money laundering and terrorist financing. To this end, Customer Due Diligence/Know Your Customer (CDD/KYC) requires special attention and concrete implementation. Accordingly, the following minimum guidelines are required to be followed by banks/DFIs to avert the risks posed by the money laundering and terrorist financing. However, banks/DFIs are free to take additional measures in line with Financial Action Task Force Recommendations.

2. Banks/DFIs shall formulate and put in place, a comprehensive CDD/KYC policy duly approved by their Board of Directors and in case of branches of foreign banks, approved by their head office, and cascade the same down the line to each and every business location/concerned officers for strict compliance.

3. CDD/KYC policy of the banks/DFIs shall inter alia include a description of the types of customers that are likely to pose a higher than average risk to the bank/DFI and guidelines for conducting Enhanced Customer Due Diligence depending upon the customers' background, country of origin, public or high profile position, nature of business, etc.

4. Banks/DFIs should undertake customer due diligence measures when:

- a) establishing business relationship;
- b) conducting occasional transactions above rupees one million whether carried out in a single operation or in multiple operations that appear to be linked;
- c) carrying out occasional wire transfers (domestic/cross border) regardless of any threshold;
- d) there is suspicion of money laundering/terrorist financing; and
- e) there is a doubt about the veracity or adequacy of available identification data on the customer.

5. Banks/DFIs shall undertake at least following Customer due diligence measures:

- a) Banks/DFIs should not open and maintain anonymous accounts or accounts in the name of fictitious persons.
- b) All reasonable efforts shall be made to determine identity of every prospective customer. For this purpose, minimum set of documents to be obtained by the banks/DFIs from various types of customers/account holder(s), at the time of opening account, as prescribed in Annexure-VIII of the Prudential Regulations for Corporate/Commercial Banking. While opening bank account of "proprietorships", the requirements laid down for individuals at Serial No. (1) of Annexure-VIII shall apply except the requirement mentioned at No. (3) of the Annexure. Banks/DFIs should exercise extra care in view of the fact that constituent documents are not available in such cases to confirm existence or otherwise of the proprietorships.

¹ Amended vide BPRD Circular Letter No. 07 of 2009 dated March 09, 2009.

- c) Banks/DFIs shall identify the beneficial ownership of accounts/ transactions by taking all reasonable measures.
 - d) For all customers, banks/DFIs should determine whether the customer is acting on behalf of another person, and should then take reasonable steps to obtain sufficient identification data to verify the identity of that other person.
 - e) For customers that are legal persons or for legal arrangements, banks/DFIs are required to take reasonable measures to (i) understand the ownership and control structure of the customer (ii) determine that the natural persons who ultimately own or control the customer. This includes those persons who exercise ultimate effective control over a legal person or arrangement.
 - f) Government accounts should not be opened in the personal names of the government official(s). Any such account, which is to be operated by an officer of the Federal/Provincial/Local Government in his/her official capacity, shall be opened only on production of a special resolution/authority from the concerned administrative department duly endorsed by the Ministry of Finance or Finance Department of the concerned Government.
6. Verification is an integral part of CDD/KYC measures for which banks/DFIs shall ensure that;
- a) copies of CNIC wherever required in Annexure-VIII are invariably verified, before opening the account, from NADRA through utilizing on-line facility or where the banks/DFIs or their branches do not have such facility from the regional office(s) of NADRA.
 - b) the identity of the beneficial owner is verified using reliable information/ satisfactory sources.
 - c) the cost of verification of CNIC from NADRA should not be passed on to their account holder(s) (either existing or prospective).
7. Banks/DFIs shall note that:
- a) For customers/clients whose accounts are either dormant as per bank's own policy or an attested copy of account holder's Computerized National Identity Card (CNIC) is not available in bank's /DFI's record, bank/DFIs may allow credit entries in such accounts. Debit transactions/ withdrawals shall not be allowed until the account holder produces an attested copy of his/her CNIC and fulfills all other formalities for activation of the account. However, transactions e.g. debits under the recovery of loans and markup etc. any permissible bank charges, government duties or levies and instruction issued under any law or from the court will not be subject to debit or withdrawal restriction. ¹
 - b) For all other customers/clients including depositors and borrowers, banks/DFIs shall obtain the attested copies of CNICs. Banks/DFIs shall block accounts without CNIC (after serving one month prior notice) for all debit transactions/withdrawals, irrespective of mode of payment, until

¹ Amended vide BPRD Circular Letter No. 30 of 2009 dated September 30, 2009 & BPRD Circular Letter No. 32 of 2010 dated December 22, 2010.

subject regulatory requirement is fulfilled. However, debit block from the accounts shall be removed upon submission of copy of CNIC. ¹

8. Banks/DFIs are also advised that CDD/KYC is not a onetime exercise to be conducted at the time of entering into a formal relationship with customer/account holder. This is an on-going process for prudent banking practices. To this end, banks/DFIs are required to:

- a) set up a compliance unit with a full time Head.
- b) put in place a system to monitor the accounts and transactions on regular basis.
- c) update customer information and records, if any, at reasonable intervals.
- d) install an effective MIS to monitor the activity of the customers' accounts.
- e) chalk out plan of imparting suitable training to the staff of bank/DFI periodically.
- f) maintain proper records of customer identifications and clearly indicate, in writing, if any exception is made in fulfilling the CDD/KYC measures.

9. Banks/DFIs shall conduct enhanced due diligence when:

- a) dealing with high-risk customers, business relationship or transaction including the following:
 - i) non-resident customers;
 - ii) private banking customers;
 - iii) legal persons or arrangements including non-governmental organizations (NGOs)/not-for-profit organizations (NPOs) and trusts/charities;
 - iv) customers belonging to countries where CDD/KYC and anti-money laundering regulations are lax;
 - v) customers with links to offshore tax havens;
 - vi) customers in cash based businesses;
 - vii) high net worth customers with no clearly identifiable source of income; and
 - viii) customers in high-value items etc.
- b) there is reason to believe that the customer has been refused banking facilities by another bank/DFI.
- c) opening correspondent banks' accounts.
- d) dealing with non-face-to-face/on-line customers. Adequate measures in this regard should be put in place, e.g. independent verification by a reliable third party, client report from the previous bank/DFI of the customer etc.
- e) establishing business relationship or transactions with counterparts from or in countries not sufficiently applying FATF recommendations.
- f) dealing with politically exposed persons or customers holding public or high profile positions.

10. For politically exposed persons or holders of public or high profile positions, enhanced due diligence should include the following:

¹ Amended vide BPRD Circular Letter No. 30 of 2009 dated September 30, 2009.

- a) Relationship should be established and or maintained with the approval of senior management including when an existing customer becomes holder of public or high profile position.
- b) Appropriate risk management systems to determine whether a potential customer, a customer or the beneficial owner is a politically exposed person/ holder of public or high profile position and sources of wealth /funds of customers, beneficial owners for ongoing monitoring on regular basis.

11. Where there are low risks and information on the identity of the customer and the beneficial owner of a customer is publicly available, or where adequate checks and controls exist, banks/DFIs may apply simplified or reduced CDD/KYC measures. Following cases may be considered for application of simplified or reduced CDD/KYC:

- a) Financial institutions provided they are subject to requirements to combat money laundering and terrorist financing consistent with the FATF recommendations and are supervised for compliance with those requirements.
- b) Public companies that are subject to regulatory disclosure requirements and such companies are listed on a stock exchange or similar situations.
- c) Government administrations or entities.

12. Reduced CDD/KYC measures shall not be applied where there is risk of money laundering or terrorist financing or when a customer resides in a country, which does not comply with FATF recommendations.

13. In case banks/DFIs are not able to satisfactorily complete required CDD/KYC measures including identity, beneficial ownership or information on purpose and intended nature of business relationship, account should not be opened or any service provided and instead reporting of suspicious transaction be considered. Similarly, relationship with existing customers should be terminated and reporting of suspicious transaction be considered if CDD/KYC is found unsatisfactory.

14. State Bank of Pakistan, during the course of inspection, would particularly check the efficacy of the CDD/KYC policies and system of the banks/DFIs and its compliance by all the branches and the staff members. Appropriate action shall be taken against the bank/DFI and the concerned staff members for non-compliance and negligence in this area, under the provisions of Banking Companies Ordinance, 1962.

REGULATION M-2 ANTI-MONEY LAUNDERING MEASURES

Banks/DFIs are advised to follow the following guidelines to safeguard themselves against their involvement in money-laundering activities, and other unlawful trades. These will add to or reinforce the precautions, banks/DFIs may have been taking on their own in this regard:

- a) Banks/DFIs shall ensure that their business is conducted in conformity with high ethical standards and that banking laws and regulations are adhered to. It

is accepted that banks/DFIs normally do not have effective means of knowing whether a transaction stems from or forms part of wrongful activity. Similarly, in an international context, it may be difficult to ensure that cross border transactions on behalf of customers are in compliance with the regulations of another country. Nevertheless banks/DFIs should not set out to offer services or provide active assistance in transactions, which in their opinion, are associated with money derived from illegal activities.

- b) Specific procedures be established for ascertaining customer's status and his source of earnings, for monitoring of accounts on a regular basis, for checking identities and bonafides of remitters and beneficiaries, for retaining internal record of transactions for future reference. The transactions, which are out of character/inconsistent with the history, pattern, or normal operation of the account involving heavy deposits/withdrawals/transfers, should be viewed with suspicion and properly investigated.
- c) Banks/ DFIs are required to include accurate and meaningful originator information (name, address and account number) on funds transfers including wire transfers and related messages that are sent, and the information should remain with the transfer or related message throughout the payment chain. However, banks/ DFIs may, if satisfied, substitute the requirement of mentioning address with CNIC, Passport, Driving license or similar identification number for this purpose.
- d) Beneficiary financial institutions shall adopt effective risk-based procedures for identifying and handling wire transfers that are not accompanied by complete originator information. Wire transfers with incomplete originator information may be seen with suspicion which may require reporting to FMU or termination of the transaction. Banks/ DFIs should remain careful from financial institutions which do not comply with aforesaid requirements by limiting or terminating business relationship. ¹
- e) Banks/DFIs shall not allow personal accounts to be used for business purposes except proprietorships, small businesses and professions where constituent documents are not available and the banks/DFIs are satisfied with KYC profile of the account holder, purpose of relationship and expected turnover of the account keeping in view financial status & nature of business of that customer. ¹
- f) For an effective implementation of banks'/DFIs' policy and procedures relating to anti money laundering/other unlawful trades, suitable training be imparted to members of staff and they be informed of their responsibility in this regard.

Keeping in view the above principles, banks/DFIs shall issue necessary instructions for guidance and implementation by all concerned.

REGULATION M-3 RECORD RETENTION

The records of transactions and identification data etc. maintained by banks/DFIs occupy critical importance as for as legal proceedings are concerned. The prudence

¹ Inserted vide BPRD Circular Letter No. 07 of 2009 dated March 09, 2009 & Substituted vide BPRD Circular Letter No. 42 of 2009 dated December 31, 2009.

demands that such records may be maintained in systematic manner with exactness of period of preservation to avoid any set back on legal and reputational fronts. Banks/DFIs shall therefore, maintain, for a minimum period of five years, all necessary records on transactions, both domestic and international. The records so maintained must be sufficient to permit reconstruction of individual transactions (including the amounts and types of currency involved, if any) so as to provide, if necessary, to SBP or law enforcement agencies for investigation or as an evidence in legal proceedings. Banks/DFIs shall, however, retain those records for longer period where transactions relate to litigation or are required by the Court of law or by any other competent authority.

2. The banks/DFIs shall keep records on the identification data obtained through the customer due diligence process (e.g. copies or records of official identification documents like passports, identity cards, driving licenses or similar documents), account files and business correspondence for at least five years after the business relationship is ended.

3. The records relating to the suspicious transactions reported by the bank/DFI will be retained by the bank/DFI, even after the lapse of the period prescribed above, till such time the bank/DFI gets permission from State Bank of Pakistan to destroy such record.

4. The banks/ DFIs should provide timely information related to suspicious transactions to domestic law enforcement agencies (LEAs), sought in terms of legal powers available to them under their respective laws in order to support investigations/ prosecutions.¹

REGULATION M-4 CORRESPONDENT BANKING

The banks/DFIs shall gather sufficient information about their correspondent banks to understand fully the nature of their business. Factors to consider include:

- Know your customer policy (KYC)
- Information about the correspondent bank's management and ownership
- Major business activities
- Their location
- Money laundering prevention and detection measures
- The purpose of the account
- The identity of any third party that will use the correspondent banking services (i.e. in case of payable through accounts)
- Condition of the bank regulation and supervision in the correspondent's country

2. The banks/DFIs should establish correspondent relationships with only those foreign banks that have effective customer acceptance and KYC policies and are effectively supervised by the relevant authorities.

3. The banks/DFIs should refuse to enter into or continue a correspondent banking relationship with a bank incorporated in a jurisdiction in which it (the

¹ Inserted vide BPRD Circular Letter No. 07 of 2010 dated April 05, 2010.

correspondent bank) has no physical presence and which is unaffiliated with a regulated financial group (i.e., shell banks). The banks/DFIs should also guard against establishing relations with correspondent foreign financial institutions that permit their accounts to be used by shell banks.

4. The banks/DFIs should pay particular attention when continuing relationships with correspondent banks located in jurisdictions that have poor KYC standards or have been identified by Financial Action Task Force as being “non-cooperative” in the fight against money laundering.

5. The banks/DFIs should be particularly alert to the risk that correspondent accounts might be used directly by third parties to transact business on their own behalf (e.g., payable-through-accounts). In such circumstances, the banks/DFIs must satisfy themselves that the correspondent bank has verified the identity of and performed on-going due diligence on the customers having direct access to accounts of the correspondent bank/DFI and that it is able to provide relevant customer identification data upon request to the correspondent bank/DFI.

6. Approval should be obtained from senior management, preferably at the level of Executive Vice President or equivalent, before establishing new correspondent banking relationships.

REGULATION M-5 SUSPICIOUS TRANSACTIONS

The banks/DFIs should pay special attention to all complex, unusually large transactions, and all unusual patterns of transactions, which have no apparent economic or visible lawful purpose. Examples of such suspicious transactions are listed at Annexure-IX. However, these are not intended to be exhaustive and only provide examples of the most basic ways in which money may be laundered. The back ground and purpose of such transactions should, as far as possible, be examined, the findings established in writing, and be available to help the relevant authorities in inspection and investigation.

2. If the bank/DFI suspects, or has reasonable grounds to suspect, that funds are the proceeds of a criminal activity or terrorist financing, it should report promptly, its suspicions, through Compliance Officer of the bank/DFI to Director General, Financial Monitoring Unit, Karachi. The report should contain, at a minimum, the following information:

- a) Title, type and number of the accounts.
- b) Amounts involved.
- c) Detail of the transactions.
- d) Reasons for suspicion.

State Bank has been encouraging banks/DFIs to make use of technology and upgrade their systems and procedures in accordance with the changing profile of various risks. Accordingly, all banks/DFIs are advised to implement systems which could flag out of pattern transactions for reporting suspicious transactions.

The existing list of examples of suspicious transactions as Annexure-IX is supplemented with the enclosed list of characteristics of financial transactions that may be a cause for increased scrutiny as Annexure-X.

3. The employees of the banks/DFIs are strictly prohibited to disclose the fact to the customer or any irrelevant quarter that a suspicious transaction or related information is being reported for investigation.

4. In cases of foreign branches of the banks/DFIs and subsidiaries of the banks/DFIs in foreign countries undertaking banking business, the banks/DFIs would ensure compliance with the regulations (relating to Anti Money Laundering and KYC) of State Bank of Pakistan or the relevant regulations of the host country, whichever are more exhaustive.

REGULATION O-1
UNDERTAKING OF CASH PAYMENTS OUTSIDE
THE BANK'S AUTHORIZED PLACE OF BUSINESS

Banks shall not undertake any business of cash payments, other than the authorized place of business, except through the installation of Automated Teller Machine (ATM). Banks desirous of providing the facility of withdrawal through Authorized Merchant Establishments at various Points of Sale (POS) may do so upto a maximum cash limit of Rs 10,000/- For this purpose, adequate and suitable security measures should be put in place for cash feeding and safety of the machines.

2. Banks may do collection and payment of cash for their prime customers through cash carrying companies registered with concerned Government department. This facility should, however, be provided through designated branches of the banks and after the banks have devised procedures including necessary security measures.

REGULATION O-2
WINDOW DRESSING

Banks/DFIs shall refrain from adopting any measures or practices whereby they would either artificially or temporarily show an ostensibly different position of bank's/DFI's accounts as given in their financial statements. Particular care shall be taken in showing their deposits, MCR, non-performing loans/assets, provisioning, profit, inter-branch and inter-bank accounts, etc.

REGULATION O-3
RECONCILIATION OF INTER-BRANCH ACCOUNTS
AND SETTLEMENT OF SUSPENSE ACCOUNT ENTRIES

All entries outstanding in the Inter-Branch Accounts (by whatever name called) and/or Suspense Account must be reconciled/cleared and taken to the proper head of account within a maximum period of 30 days from the date the entry is made in the above-named accounts.

2. Entries made in Suspense Account on account of tax at source, advance tax paid, tax recoverable, advance expense on new branches, advance rent paid, legal expenses, mark-up/service charge recoverable, Qarze Hasna for marriage, and forward cover fee, may be classified as "Other Assets" and the above instructions shall not be applicable to the foregoing items. Besides, entries relating to frauds and forgeries, cash theft and looted, payments against equity, scrips/debt instruments and contributory payments of capital nature to be capitalized at a later stage shall also be excluded from the purview of the said regulation. The exclusion of entries relating to frauds and forgeries, cash theft and looted will, however, be subject to the condition that the same are cleared immediately on receipt of insurance claims. Further, outstanding amount of the premium on Crop Loan Insurance Scheme (CLIS) receivable from Government of Pakistan (GoP) shall also be classified in other assets. The outstanding amount shall, however, be reconciled/cleared immediately on reimbursement of premium amount from the GoP.

3. Banks/DFIs shall institute an effective internal control system for the operations of Inter-Branch and Suspense Accounts, which ensures reconciliation/clearing of the entries in shortest possible time and also clearly fixes the responsibilities on the official(s) for neglecting the timely reconciliation and clearance.

REGULATION O-4
MAINTENANCE OF ASSETS IN PAKISTAN

Every bank/DFI shall maintain in Pakistan not less than 80% of the assets created by it against such time and demand liabilities as specified in Part-A of Form X (prescribed under Rule 17 of the Banking Companies Rules, 1963). Accordingly, assets held abroad by any bank/DFI shall not, at any point in time, exceed 20% of its time and demand liabilities specified in the said Form X. All other assets financed from sources other than time and demand liabilities specified in the said Form X shall be held within Pakistan.

REGULATION O-5
FOREIGN CURRENCY DEPOSITS UNDER FE 25-1998

Banks shall not invest FE 25 deposits in foreign currency/local currency denominated instruments below investment grade. Neither, shall they invest/place such deposits in fund management schemes of other banks/DFIs/NBFCs whether in Pakistan or abroad.

2. Banks shall be required to maintain the prescribed ratio of Cash Reserve/Special Cash Reserve against FE 25 deposits in US Dollars.

3. Placement of funds of FE-25 deposits with any one bank/financial institution, whether in Pakistan or abroad, shall be subject to the following conditions:

- a) The investing bank shall comply with Regulation R-1 (Annexure-1 Para F), which mentions different weightages according to credit ratings of financial institutions.
- b) The investing bank will not place in a single institution an amount exceeding 25% of the total investable funds, available with the investing bank, under the FE-25 Deposit Scheme.

The conditions above shall, however, not be applicable on placement of funds by the bank with its own branches overseas. Furthermore, compliance with all other relevant Prudential Regulations shall also be ensured.

4. Banks shall be free to decide the rate of return on deposits mobilized under FE-25.

5. Banks shall be free to use such deposits for their trade-related activities provided the exchange risks are adequately covered and a square position is maintained.

6. Foreign currency deposits mobilized under FE 25 scheme, after netting-off the deposits utilized to finance trade related activities such as financing against Import

and Export documents, should not at any point exceed twenty percent of the local currency deposits of the banks at the close of business on the last working day of the preceding quarter. Banks/DFIs may also exclude FE-25 Deposits in the form of the Foreign Direct Investment and funds received for social and economic uplift through international donor agencies/welfare organizations from the calculation of limit on FE-25 Deposits prescribed in Para 6 of Regulation O-5. This will, however, be subject to the condition that the banks/DFIs will obtain an undertaking from the Account Holder that such funds are remitted from abroad and would be used for poverty alleviation and socio-economic uplift. The genuineness of all such exclusions will be verified by the SBP Inspectors during the subsequent inspections.

7. Banks will report the equivalent Pak Rupee amount (with a foot note on \$ equivalent) of FE 25 deposits utilized for trade related activities under newly created code No.80-05 of their Weekly Statement of Position submitted to the Banking Supervision Department.

GUIDELINES REGARDING LIMIT ON EXPOURE
TO A SINGLE PERSON UNDER REGULATION R-1

1. In arriving at exposure under Regulation R-1:
 - A) 100% of the deposits placed with lending bank/DFI, under perfected lien and in the same currency, as that of the loan, shall be excluded.
 - B) 90% of the following shall be deducted;
 - i) deposits placed with the lending bank/DFI, under perfected lien, in a currency other than that of the loan;
 - ii) deposits with another bank/DFI under perfected lien;
 - iii) encashment value of Federal Investment Bonds, Pakistan Investment Bonds, Treasury Bills and National Saving Scheme securities, lodged by the borrower as collateral; and
 - iv) Pak. Rupee equivalent of face value of Special US Dollar Bonds converted at inter-bank rate, lodged by the borrower as collateral.
 - C) 85% of the unconditional financial guarantees accepted as collateral and payable on demand by banks/DFIs, rated at least 'A' or equivalent by a credit rating agency on the approved panel of State Bank of Pakistan, Standard & Poors, Moody, Fitch Ibcra or Japan Credit Rating Agency (JCRA) shall be deducted. Similar weightage to guarantees issued by the International Finance Corporation (IFC), Commonwealth Development Corporation (CDC) Deutsche Investitions und Entwicklungsgesellschaft mbH (DEG), Netherland Financierings Maatschappij voor Ontwikkelingslanden N.V (FMO) and Asian Development Bank (ADB) shall also apply.
 - D) 50% of listed Term Finance Certificates held as security with duly marked lien shall be deducted. The TFCs to qualify for this purpose should have been rated at least 'A' or equivalent by a credit rating agency on the approved panel of State Bank of Pakistan.
 - E) Weightage of 50% shall be given to;
 - i) documentary credits (except Standby Letter of Credits where 100% exposure would be counted) opened by banks/DFIs;
 - ii) guarantees/bonds other than financial guarantees;
 - iii) underwriting commitments.
 - F) The following different weightages will be applicable to exposure taken against commercial banks/DFIs in respect of placements;
 - i) 10% weightage on exposure to banks/DFIs with 'AAA' rating.
 - ii) 25% weightage on exposure to banks/DFIs rated 'A' and above.
 - iii) 50% weightage on exposure to banks /DFIs rated 'BBB' and above.

The banks/DFIs shall, however, ensure that the overall limit for each financial institution in respect of inter-bank placements is invariably approved by their Board of Directors.

2. For the purpose of this regulation, exposure shall not include the following:
- i) Loans and advances (including bills purchased and discounted) given to the Federal Government or any of their agencies under the commodity operations program of the Federal Government, or guaranteed by the Federal Government.
 - ii) Obligations under letters of credit and letters of guarantee to the extent of cash margin held by the bank/DFI.
 - iii) Letters of credit, which do not create any obligation on the part of the bank/DFI (no liability L/C) to make payments on account of imports.
 - iv) Letters of credit opened on behalf of Federal Government where payment is guaranteed by State Bank of Pakistan/Federal Government.
 - v) Facilities provided to commercial banks/DFIs through REPO transactions with underlying SLR eligible securities.
 - vi) Pre-shipment/post-shipment credit provided to finance exports of goods covered by letter of credit/firm contracts including financing provided from the bank's /DFI's own resources.
 - vii) Letters of credit established for the import of plant and machinery.

**BORROWER'S BASIC FACT SHEET- FOR CORPORATE
PRESCRIBED UNDER REGULATION R-3**

Date of Request. _____

(TO BE COMPLETED IN CAPITAL LETTERS OR TYPEWRITTEN)

1. BORROWER'S PROFILE:

Name										Address									
Phone #					Fax #					E-mail Address									
Office					Res.														
Computerized National Identity Card #										National Tax #					Sales Tax #				
Import Registration #					Export Registration #					Date of Establishment					Date of opening of A/c.				

2. DETAILS OF DIRECTORS/OWNERS/PARTNERS:

Name										Address									
Phone #					Fax #					E-mail Address									
Office					Res.														
Computerized National Identity Card #										National Tax #									
Share-holding					Amount					% of Share-holding									

3. MANAGEMENT:

A) EXECUTIVE DIRECTORS/PARTNERS:												
Name			Address				CNIC #			Phone #		
1.												
2.												
B) NON-EXECUTIVE DIRECTORS/PARTNERS:												
Name			Address				CNIC #			Phone #		
1.												
2.												

4. CORPORATE STATUS:

Sole Proprietorship			Partnership			Public/Private Limited Company		

5. NATURE OF BUSINESS:

Industrial		Commercial		Agricultural		Services		Any other	

6. REQUESTED LIMITS:

		Amount		Tenor	
Fund Based					
Non-Fund Based					

7. BUSINESS HANDLED/EFFECTED WITH ALL FINANCIAL INSTITUTIONS DURING THE LAST ACCOUNTING YEAR:

Imports	Exports	Remittances effected (if any)

8. EXISTING LIMITS AND STATUS:

	Amount	Expiry Date	Status	
			Regular	Amount Overdue(if any)
Fund Based				
Non-Fund Based				

9. ANY WRITE-OFF, RESCHEDULING/ RESTRUCTURING AVOIDED DURING THE LAST THREE YEARS:

Name of Financial Institution	Amount during 1 st Year		Amount during 2 nd Year		Amount during 3 rd Year	
	Write-off	Rescheduled/ Restructured	Write-off	Rescheduled/ Restructured	Write-off	Rescheduled/ Restructured

10. DETAILS OF PRIME SECURITIES MORTGAGED/ PLEDGED:

A) AGAINST EXISTING FACILITIES:				
Name of Financial Institution	Nature of Security	Total Amount	Rank of Charge	Net Realizable Value
1.				
2.				
B) AGAINST REQUESTED/ FRESH/ ADDITIONAL FACILITIES:				
Name of Financial Institution	Nature of Security	Total Amount	Net Realizable Value	
1.				
2.				

11. DETAILS OF SECONDARY COLLATERAL MORTGAGED/ PLEDGED:

A) AGAINST EXISTING FACILITIES:				
Name of Financial Institution	Nature of Security	Total Amount	Rank of Charge	Net Realizable Value
1.				
2.				
B) AGAINST REQUESTED/ FRESH/ ADDITIONAL FACILITIES:				
Name of Financial Institution	Nature of Security	Total Amount	Net Realizable Value	
1.				
2.				

12. CREDIT RATING (WHERE APPLICABLE):

Name of Rating Agency	Rating

13. DETAILS OF ASSOCIATED CONCERNS (AS DEFINED IN COMPANIES ORDINANCE, 1984):

Name of Concern	Name of Directors	Share-holding	% of Total Share Capital

14. FACILITIES TO ASSOCIATED CONCERNS BY THE CONCERNED FI:

Name of Concern	Nature & Amount of Limit	Outstanding as on-----	Nature & Value of Securities	Overdues	Defaults

15. DETAILS OF PERSONAL GUARANTEES PROVIDED BY THE DIRECTORS/PARTNERS ETC. TO FIs TO SECURE CREDIT:

Names of the Guarantors	Institutions/persons to whom Guarantee given	Amount of Guarantee	Validity Period	NIC #	NTN	Net-worth

16. DIVIDEND DECLARED (AMOUNT) DURING THE LAST THREE YEARS:

During 1 st Year	During 2 nd Year	During 3 rd Year

17. SHARE PRICES OF THE BORROWING ENTITY:

Listed Company		Break-up Value of the Shares in case of Private Limited Company
Current Price	Preceding 12 Months Average	

18. NET-WORTH (PARTICULARS OF ASSETS OWNED IN THEIR OWN NAMES BY THE DIRECTORS/PARTNERS/PROPRIETORS):

Owner's Name	Particulars of Assets	Market value	Particulars of Liabilities

19. DETAILS OF ALL OVERDUES (IF OVER 90 DAYS):

Name of Financial Institution	Amount

20. Details of payment schedule if term loan sought.

21. Latest Audited Financial Statements as per requirements of Regulation R-3 to be submitted with the LAF (Loan Application Form).

22. Memorandum and Articles of Association, By-laws etc. to be submitted by the borrower alongwith the request.

I certify and undertake that the information furnished above is true to the best of my knowledge.

CHIEF EXECUTIVE'S/ BORROWER'S
SIGNATURE & STAMP

COUNTER SIGNED BY:

AUTHORISED SIGNATURE & STAMP
(BANK/DFI OFFICIAL)

**BORROWER'S BASIC FACT SHEET - FOR INDIVIDUALS
PRESCRIBED UNDER PRUDENTIAL REGULATION R-3**

Date of Request. _____

(TO BE COMPLETED IN CAPITAL LETTERS OR TYPEWRITTEN)

1. BORROWER'S PROFILE:

Name										Address									
Phone #										Fax #					E-mail Address				
Office					Res.														
Computerized National Identity Card #										National Tax #									
Father's Name										Father's Computerized National Identity Card #									

2. REFERENCES (AT LEAST TWO):

Name										Address									
Phone #										Fax #					E-mail Address				
Office					Res.														
Computerized National Identity Card #										National Tax #									

3. NATURE OF BUSINESS/ PROFESSION:

Industrial	Commercial	Agricultural	Services	Any other

4. EXISTING LIMITS AND STATUS:

	Amount	Expiry Date	Status		
			Regular	Amount Over-due (if any)	Amount Rescheduled/ Restructured (if any)
Fund Based					
Non-Fund Based					

5. REQUESTED LIMITS:

	Amount	Tenor
Fund Based		
Non-Fund Based		

6. Details of payment schedule if term loan sought.

7. Latest Income Tax/Wealth Tax Form to be submitted by the borrower.

I certify and undertake that the information furnished above is true to the best of my knowledge.

APPLICANT'S SIGNATURE &
STAMP

COUNTER SIGNED BY:

AUTHORISED SIGNATURE & STAMP
(BANK/DFI OFFICIAL)

CASES ELIGIBLE FOR RELAXATION UNDER REGULATION R-7

For bid bonds issued on behalf of local consultancy firms bidding for international contracts where the consultancy fees are to be received in foreign exchange, and including Bid Bonds issued on behalf of all contractors of goods and services bidding against International Tenders.

2. For issue of performance bonds on behalf of local construction companies/ contractors of goods and services bidding for international tenders. Provided that the liability of the bank/DFI will be on reducing balance basis after taking into account progressive billing certified by the beneficiary/project owner and payment received against these bills.

3. For issue of guarantees on behalf of local construction companies/ contractors of goods and services bidding for international tenders in respect of mobilization advance.

(i) Guarantees issued should contain clause that the mobilization advance and other proceeds under the contract shall be routed by the beneficiary/project owner through the account of the contractors maintained with the guaranteeing bank/DFI.

(ii) At the time of issuing such guarantee the Construction Company/contractor shall sign an agreement with the bank/DFI that cash proceeds out of mobilization advance will be released as per satisfaction of the bank/DFI about the progress of the contract.

4. While issuing guarantees to the exporters of cotton in terms of F.E. Circular No. 77 dated December 4, 1988, banks/DFIs may settle the type and quantum of security with their customers.

5. Issue of performance bonds/bid bonds and guarantees issued for mobilization advances on behalf of the manufacturers of engineering goods. The term 'engineering goods' shall have the same meanings as are given to locally manufactured machinery in State Bank of Pakistan scheme for financing locally manufactured machinery. Such condition may, however, not be necessary in case of guarantees issued by the International Banks.

**GUIDELINES IN THE MATTER OF CLASSIFICATION
AND PROVISIONING FOR ASSETS (REGULATION R-8)**

All Financing Facilities (including Short, Medium and Long Term)

CLASSIFICATION	DETERMINANT	TREATMENT OF INCOME	PROVISIONS TO BE MADE
(1)	(2)	(3)	(4)
1. Substandard.	Where mark-up/ interest or principal is overdue by 90 days or more from the due date.	Unrealized mark-up /interest to be kept in Memorandum Account and not to be credited to Income Account except when realized in cash. Unrealized mark up/interest already taken to income account to be reversed and kept in Memorandum Account.	Provision of 25% of the difference resulting from the outstanding balance of principal less the amount of liquid assets realizable without recourse to a Court of Law and 40% of the Forced Sale Value (FSV) of pledged stocks and mortgaged residential, commercial and industrial properties (see Note 2 below).
2. Doubtful.	Where mark-up/ interest or principal is overdue by 180 days or more from the due date.	As above.	Provision of 50% of the difference resulting from the outstanding balance of principal less the amount of liquid assets realizable without recourse to a Court of Law and 40% of the Forced Sale Value (FSV) of pledged stocks and mortgaged residential, commercial and industrial properties (see Note 2 below).

¹ Amended vide BSD Circular No. 02 of 2010 dated June 3, 2010

3. Loss.	(a) Where mark-up/ interest or principal is overdue by one year or more from the due date	As above	Provision of 100% of the difference resulting from the outstanding balance of principal less the amount of liquid assets realizable without recourse to a Court of Law and 40% of the Forced Sale Value (FSV) of pledged stocks and mortgaged residential commercial and industrial properties (see Note 2 below). Benefit of FSV against NPLs shall not be available after 3 years from the date of classification of the Loan/Advance. However, the 40% benefit of FSV of land (open plot and separate valuation of land if building is constructed) shall be available for 4 years from the date of classification of loan.
	(b) Where Trade Bills (Import/Export or Inland Bills) are not paid/adjusted within 180 days of the due date.	As above.	As above.

Notes :

- 1) Classified loans/advances that have been guaranteed by the Government would not require provisioning, however, mark up/interest on such accounts to be taken to Memorandum Account instead of Income Account.
- 2) FSV shall be determined in accordance with the guidelines contained in Annexure-V to these Regulations.

PRs FOR CORPORATE AND COMMERCIAL BANKING

UNIFORM CRITERIA FOR DETERMINING THE VALUE OF PLEDGED STOCK AND MORTGAGED PROPERTIES (REGULATION R-8)

Only liquid assets, pledged stock, and property having registered or equitable mortgage shall be considered for taking benefit for provisioning provided no NOC for creating further charge to another bank/DFI /NBFC has been issued by bank/DFI. The aforesaid assets having pari-passu charge shall be considered on proportionate basis of outstanding amount.

2. Plant and machinery, hypothecated assets and assets with second charge and floating charge shall not be considered for taking the benefit for provisioning.

3. Valuations shall be carried out by an independent professional evaluator who should be listed on the panel of evaluators maintained by the Pakistan Banks' Association (PBA) for this purpose. PBA shall lay down the minimum eligibility criteria with the prior approval of the State Bank of Pakistan for placement of evaluators on the panel to be maintained by it. The evaluator while assigning any values to the pledged stock and mortgaged property shall take into account all relevant factors affecting the salability of such assets including any difficulty in obtaining their possession, their location, condition and the prevailing economic conditions in the relevant sector, business or industry. The values of pledged stock and mortgaged property so determined by the evaluators must have to be a reasonably good estimate of the amount that could currently be obtained by selling such assets in a forced/distressed sale condition. The evaluators should also mention in their report the assumptions made, the calculations/formulae /basis used and the method adopted in determination of the values i.e. the forced sales value (FSV).

4. The valuation process will include conducting a 'Full-scope Valuation' of the assets in the first year and then followed by 'Desktop Valuations' in the second and third year (Fourth year only for open plot of land, and where building is constructed, separate valuation of land) . Full scope valuation shall be valid for three years (four years for land only) from the date of last valuation; and, at the time of classification, the Full scope valuation shall not be more than one year old.

5. The following may be noted in respect of the Desktop and Full-scope Evaluations:

- Desktop Evaluation is defined as “an Interim Brief Review of Full-scope Evaluation, so that any significant change in the factors, on which the full-scope valuation was based, is accounted for and brought to the notice of the lending bank/DFI.”
- In case the loans exceed Rs 100 million, the Desktop valuation will be done by the same evaluator, who had conducted the full-scope evaluation (the evaluator should be on the approved panel of the PBA) whereas for loans below this threshold, the Desktop evaluation may be done by the banks/DFIs themselves or by the approved evaluators. For conducting

¹ Amended vide BSD Circular No. 02 of 2010 dated June 3, 2010.

Desktop evaluation, the evaluators will pay a short visit to the bank/DFI and the borrower's site. The bank's/DFI's responsibility in this respect will be to ensure that the evaluation is contacted for conducting Desktop Evaluation, and will provide all necessary information to the evaluators, which are materially important for the interim review (Desktop Evaluation).

- The Desktop Evaluation shall be used for determining any additional provisioning requirement and thus the same shall not result in reducing the provisioning requirement, assessed on the basis of full-scope evaluation.
- In cases where the evaluators are not allowed by the borrowers to enter in their premises, the full-scope evaluation, conducted as such, will not be accepted for provisioning benefit.

6. State Bank may check the valuations of the mortgaged assets through an independent evaluator, on random basis, to verify the reasonableness of the valuations. The unjustified differences in the valuations of the banks/DFIs and State Bank of Pakistan shall render the concerned bank/DFI and evaluator to penal actions including, inter alia, withdrawal of FSV benefit.

7. The categories of pledged stock and mortgaged property to be considered for valuation along with discounting factors to be applied would be as under (no other assets shall be taken into consideration):

a) Liquid Assets:

Valuation of Liquid Assets shall be determined by the bank/DFI itself and verified by the external auditors. However, in the case of pledged shares of listed companies, values should be taken at market value as per active list of Stock Exchange(s) on the balance sheet date. Moreover, valuation of shares pledged against loans/advances shall be considered only if these have been routed through Central Depository Company of Pakistan (CDC), otherwise these will not be admissible for deduction as liquid assets while determining required provisions.

b) Mortgaged property:

Valuation of residential, commercial and industrial property (land and building only) would be accepted as determined by the evaluators in accordance with the criteria given above.

c) Pledged Stocks:

In case of pledged stocks of perishable and non-perishable goods, forced sale value should be provided by evaluators, which should not be more than six months old, at each balance sheet date. The goods should be perfectly pledged, the operation of the godown(s) or warehouse(s) should be in the control of the bank/DFI and regular valid insurance and other documents should be available. In case of perishable goods, the evaluator should also give the approximate date when these are expected to be of no value.

PROFORMA - FIT & PROPER TEST

Photo 1 x 1½	Full Name	
	Father's Name	
	Date of Birth	Place of Birth (City and Country)
	Nationality (ies)	NTN Number
	C.N.I.C. No	N.I.C. No (Old)
	Passport Number (for foreign national)	
	Present Residential Address in Full	
	Permanent Residential Address in Full	
	Residential Telephone Number(s)	Mobile Number
	If you have changed your name, state previous name and reason for change	
Academic Education		
Qualification	Name & Address of Degree Awarding Institution	Date of Completion
Professional Education		
Qualification	Name & Address of Institution/ Professional Body	Date of Completion
Training(s); if any		
Existing Employment		
Present Designation	Present Department	
Official Address		
Telephone Number (s)	Email	

Please provide complete and true particulars of all business(es), including proprietary concern/partnership firms, companies, in which you have been associated as a proprietor, partner or a director thereof during the last ten years and the accounts maintained by them:		
Name of the Proprietary Concern/Partnership Firm/ Company	Name of Bank and/or NBFIs Together with Name of Branches	Account Number(s)
Position held during the last ten years (along with name and address of company/institution/body where appointment held, nature of the company/institution/body and dates of appointment)		
Position of the shares held in the bank		Number of shares held as of _____
As a Sponsor Shareholder <ul style="list-style-type: none"> • Own name • In name of your company • In name of your family member Other than Sponsor Shareholder <ul style="list-style-type: none"> • Own name • In name of your company • In name of your family member 		

SIGNATURE OF CONCERNED OFFICIAL

*Additional sheet may be used, if required

Affidavit
(On Non-Judicial Stamp Paper)

I, _____ son/daughter/wife of _____ adult, resident
of _____
and holding CNIC No. _____ do hereby state on solemn
affirmation as under:-

- a. that the deponent hereby confirm that the statement made and the information supplied in the attached questionnaire and the Annexure-VIA and the answers thereof are correct and that there are no other facts that are relevant for “Fit and Proper Test”
- b. that the deponent undertake that the State Bank of Pakistan may seek additional information from any third party it deems necessary in view of assessing “Fit and Proper Test”
- c. that the deponent undertake to bring to the attention of the State Bank of Pakistan any matter which may potentially affect my status as being someone fit and proper as and when it crops up; and
- d. that whatever is stated above is correct to the best of my knowledge and belief and nothing has been concealed therefrom.

DEPONENT

The Deponent is identified by me

Signature _____

ADVOCATE
(Name and Seal)

Solemnly affirmed before me on this _____ day of _____ at _____ by the Deponent above named who is identified to me by _____, Advocate, who is known to me personally.

Signature _____

OATH COMMISSIONER FOR TAKING AFFIDAVIT
(Name and Seal)

QUESTIONNAIRE FOR ACCESSING “FIT & PROPER TEST”

Please answer the following questions by entering a tick (✓) in the appropriate box. If answer of any of these questions in YES and need explanation, use a separate sheet with proper reference to the question.

- | | Yes | No |
|--|--------------------------|--------------------------|
| 1. Have you ever been convicted/involved in any fraud/forgery, financial crime etc, in Pakistan or else where, or is being subject to any pending proceedings leading to any conviction? | <input type="checkbox"/> | <input type="checkbox"/> |
| 2. Have you ever been associated with any illegal activity concerning banking business, deposit taking, financial dealing and other business? | <input type="checkbox"/> | <input type="checkbox"/> |
| 3. Have you ever been subject to any adverse findings or any settlement in civil/criminal proceedings particularly with regard to investments, financial/business, misconduct, fraud, formation or management of a corporate body etc by SBP, other regulators, professional bodies or government bodies/agencies? | <input type="checkbox"/> | <input type="checkbox"/> |
| 4. Have you ever contravened any of the requirements and standards of regulatory system or the equivalent standards or requirements of other regulatory authorities? | <input type="checkbox"/> | <input type="checkbox"/> |
| 5. Have you ever been involved with a company or firm or other organization that has been refused registration/licence to carry out trade, business etc? | <input type="checkbox"/> | <input type="checkbox"/> |
| 6. Have you ever been involved with a company/firm whose registration/licence has been revoked or cancelled or gone into liquidation or other similar proceedings? | <input type="checkbox"/> | <input type="checkbox"/> |
| 7. Have you ever been debarred for being Chief Executive, Chairman, Director or Sponsor/Strategic Investor of a company, especially financial institutions? | <input type="checkbox"/> | <input type="checkbox"/> |
| 8. Have you ever been dismissed/ asked to resign/resigned in Pakistan or elsewhere in order to avoid legal or disciplinary action? | <input type="checkbox"/> | <input type="checkbox"/> |
| 9. Have you ever resigned from a professional or regulatory body in Pakistan or elsewhere in order to avoid legal or disciplinary action? | <input type="checkbox"/> | <input type="checkbox"/> |
| 10. Have you ever been disqualified/ removed by regulators/Government bodies/ agencies? | <input type="checkbox"/> | <input type="checkbox"/> |
| 11. Have you ever been in default of payment of dues owed to any financial institution in individual capacity or as proprietary concern or any partnership firm or in any private unlisted/listed company? | <input type="checkbox"/> | <input type="checkbox"/> |
| 12. Have you ever been in default of taxes in individual capacity or as proprietary concern or any partnership firm or in any private listed/unlisted company? | <input type="checkbox"/> | <input type="checkbox"/> |
| 13. Have you ever been associated as director and/or chief | <input type="checkbox"/> | <input type="checkbox"/> |

executive with the corporate bodies whose corporate and tax record, including custom duties, central excise and sales tax has been unsatisfactory?

14. Have you entered into any agreement with any other person (natural or legal) which will influence the way in which you exercise your voting rights or the way in which you otherwise behave in your relationship with the authorized entity?
15. Are you a director on the Board of Directors of any other Financial Institution(s)?
16. Are you a Chairman, Chief Executive, Chief Financial Office, Chief Internal Auditor, Research Analyst or Trader (by whatever name/designation called) of a Exchange Company (firm or sole proprietorship), member of a Stock Exchange, Corporate Brokerage House?
17. Are you owing/controlling any Exchange Company or Corporate Entity?
18. Have you been or are you working as consultant or adviser of bank/DFI in which you intend to become a director?
19. Are you employee of the bank/DFI?
20. Are you employee of a company/entity/organization where sponsor shareholders of bank/DFI have substantial interest?
21. Are you a member/office bearer of any political party or member of Senate/National/Provincial Assembly/Local Body?
22. If independent director, have you enclosed declaration in this behalf?
23. Any other information that is relevant for the purpose of SBP and needs to be mentioned?

Signature _____
Name _____
Position _____
Date _____

PROFORMA – FITNESS & PROPRIETARY OF KEY EXECUTIVES

Photo 1 x 1½	Position and Grade held by the Executive	
	Date of assumption of current position (dd/mm/yyyy)	
	Full Name	
	Father's Name	
Date of Birth		Place of Birth (City and Country)
Nationality (ies)		NTN Number
C.N.I.C. No		N.I.C. No (Old)
Telephone Number(s)		Mobile Number
Academic Qualification		
Qualification	Name & Address of Degree Awarding Institution	Date of Completion
Professional Qualification		
Qualification	Name & Address of Degree Awarding Institution	Date of Completion
Training(s); if any		
Previous Employment(s) (date-wise)		
Designation	Department	
Official Address		
Telephone Number (s)		
Has ever been convicted of any offence?		Yes No
If yes, nature of offence and penalty imposed		
Has ever been censured or penalized by any financial regulator (local or foreign)?		Yes No
If yes, reasons for adverse findings and amount of penalty imposed (if any)		
Has ever been dismissed from employment?		Yes No
If yes, name of the employer and reason for dismissal		

(Signature of the concerned official) (Signature and Stamp of Employer)

ASSESSMENT OF FITNESS AND PROPRIETY

1. INTEGRITY, HONESTY AND REPUTATION

- i) Has not been convicted/involved in any fraud/forgery, financial crime etc, in Pakistan or elsewhere, or is not being subject to any pending proceedings leading to such a conviction.
- ii) Has not been subject to any adverse findings or any settlement in civil/criminal proceedings particularly with regard to investments, financial matters/business, misconduct, fraud, formation or management of a corporate body etc by SBP, other regulatory authorities (within or outside Pakistan), professional bodies or government bodies/agencies.
- iii) Has not contravened any of the requirements and standards of SBP or the equivalent standards/requirements of other regulatory authorities (outside Pakistan as well), professional bodies or government bodies/agencies.
- iv) Has not been involved with (management or conduct of the affairs of) a company/firm or any other organization that has been refused registration/licence to carry out trade, business etc.
- v) Has not been involved with (management or conduct of the affairs of) a company/firm whose registration/licence has been revoked or cancelled or gone into liquidation or other similar proceedings due to mismanagement of affairs, financial misconduct or mal practices.
- vi) Has not been debarred for being Chief Executive, Chairman, Director, Controlling Shareholder/Sponsor or Key Executive of a company/firm or in similar capacity.

2. TRACK RECORD

- i) The person must have an impeccable track record in the companies served either in the capacity of an employee or director/Chief Executive or as Chairman.
- ii) Has not been demoted, dismissed or forced to resign from employment by the bank/DFI, or has not been removed by any regulator or government body, in the capacity of employee, director, chairman or key executive of the company/firm or any other position of trust.

3. SOLVENCY & FINANCIAL INTEGRITY

- i) Has not been associated with any illegal activity concerning banking business, deposit taking, financial dealing and other business.
- ii) Has not been in default of payment of dues owed to any financial institution and/ or default in payment of any taxes in individual capacity or as

proprietary concern or any partnership firm or in any private unlisted/listed company.

- iii) Has not been associated as director and/or chief executive with the corporate bodies who have defaulted in payment of Government duties/taxes etc.
- iv) Has sufficient means to discharge his/her financial obligations, if any.

4. QUALIFICATION & EXPERIENCE

This section shall apply separately for Directors, CEO and Key Executives of Banks/DFIs as under: -

i) Directors on the Board

- a) Must have management/business experience of at least 5 years at senior level in an active capacity. In case of lawyers, 7 years experience is required, provided that they are not practicing/involved with or acting as legal counsel/adviser or on payroll of a bank where he is proposed to be appointed as director.
- b) Minimum qualification for a person to be appointed as Director on the Board of a bank/DFI is graduation. Higher education accomplished in the discipline of banking and finance may be an added qualification.

ii) Chief Executive Officer

- a) Must be a career banker having at least 5 years of experience at senior level as EVP and above or equivalent i.e. Group Head of Financial/Business Line in a bank and posses expertise and skill set to undertake responsibilities of the position effectively and prudently.
- b) Should be between 40 to 70 years of age.
- c) Should have minimum qualification of graduation or equivalent in the discipline of banking, finance, economics, business administration and related fields. CEO of the Islamic Bank should preferably be having experience/training in Islamic Banking.

iii) Key Executive

- a) Must be a qualified professional possessing relevant experience & degree relating to the job/assignment.

5. CONFLICT OF INTEREST

- i) The CEO is not a Chairman of the Board of Directors of the same bank/DFI .
- ii) The Directors on the Board should avoid conflict of interest in their activities with, and commitments to, other organizations.

- iii) Is not a director (including as a nominee director of the Government) of any other bank/DFI. However, this clause will not be applicable in case of Managing Director and other employees of National Investment Trust (NIT) nominated on the Board of banks/DFIs, till its privatization.
- iv) No person can become a Director of the bank/DFI, if he/she is :
 - a) Holding substantial interest or is working as Chairman, Director, Chief Executive, Chief Financial Officer, Chief Internal Auditor, Research Analyst or Trader (by whatever name/designation called) of a:
 - i) Exchange Company (firm or sole proprietorship)
 - ii) Member of a Stock Exchange
 - iii) Corporate Brokerage House
 - iv) Any company/entity owned and controlled by the person mentioned at i) to iii) above
 - b) Acting, either in personal capacity and/or through firm/ company where he/she has substantial interest, as consultant /advisor to bank/DFI in which he/she intends to become a director.

6. OTHERS

- i) Not more than 25% directors of the same family are permitted to be on the Board of a bank/DFI.
- ii) Maximum two members of Board of Directors of a bank/DFI including its CEO can be the Executive Directors.
- iii) Directors should preferably be professionals from diversified field/industry. However, a minimum of 25% members of Board of Directors of a bank/DFI shall be Independent Directors.
- iv) No member of Senate, National/ Provincial Assembly, Local bodies shall be appointed/ recommended for appointment as Member of Board of Directors and/or Chief Executive Officer/Key Executive of any bank/DFI.
- v) No Key Executive shall head more than one functional area. Furthermore, he/she shall not hold directorship in his /her personal capacity: (a) in a business concern which is also a client of the bank/DFI, and (b) in any other financial institution.

DOCUMENTS TO BE OBTAINED FROM VARIOUS TYPES OF CUSTOMERS/ACCOUNT HOLDER(S) UNDER REGULATION M-1

Sr. No.	Nature of Account	Documents/papers to be obtained
I	Individuals	<ol style="list-style-type: none"> 1. Attested photocopy of Computerized National Identity Card* (CNIC) or passport of the individual by a gazetted officer or an officer of the bank/DFI. 2. In case the CNIC does not contain a photograph, the bank/DFI should also obtain, in addition to CNIC, any other document such as driving license etc. that contains a photograph. However, if the individual does not have any other valid document which bears photograph, following documents should be obtained: <ol style="list-style-type: none"> (i) A copy of the photograph duly attested by gazetted officer/Nazim. (ii) A copy of CNIC without photograph duly attested by the same person who attested the copy of photograph as per Sr. No. (i) above. (iii) A confirmation in writing to the effect that the individual have no other document bearing photograph. <p>Banks/DFIs shall ensure that the CNIC and the photograph are of the same person whose account is being opened with them. The particulars/CNIC of such persons must be confirmed from NADRA in writing or through its "VeriSys" system by the bank/DFI.</p> 3. In case of a salaried person, attested copy of his service card, or any other acceptable evidence of service, including, but not limited to a certificate from the employer. 4. In case of illiterate person, a passport size photograph of the new account holder besides taking his right and left thumb impression on the specimen signature card.
II	Partnership	<ol style="list-style-type: none"> (i) Attested photocopy of identity card of all partners. (ii) Attested copy of 'Partnership Deed' duly signed by all partners of the firm. (iii) Attested copy of Registration Certificate with Registrar of Firms. In case the partnership is unregistered, this fact should be clearly mentioned on the Account Opening Form. (iv) Authority letter, in original, in favor of the person authorized to operate on the account of the firm.
III	**Joint Stock companies	<p>Certified copies of:</p> <ol style="list-style-type: none"> (i) Resolution of Board of Directors for opening of account specifying the person(s) authorized to operate the company account. (ii) Memorandum and Articles of Association. (iii) Certificate of Incorporation. (iv) Certificate of Commencement of Business. (v) Attested photocopies of identity cards of all the directors. (vi) List of Directors on Form 29 issued by the Registrar Joint Stock Company.
IV	Clubs, Societies and Associations	<ol style="list-style-type: none"> (i) Certified copies of <ol style="list-style-type: none"> 6. Certificate of Registration. (b) By-laws/Rules & Regulations. a. Resolution of the Governing Body/Executive Committee for opening of account authorizing the person(s) to operate the

		<p>account and attested copy of the identity card of the authorized person(s).</p> <p>b. An undertaking signed by all the authorized persons on behalf of the institution mentioning that when any change takes place in the persons authorized to operate on the account, the banker will be informed immediately.</p> <p>c. banks should obtain copies of CNICs of all the members of Governing and Executive Bodies of DHA or ask for delegation of power to Administrator under section (7) & (8) of the Pakistan Defence Housing Authority Order, 1980 and accept copy of CNIC of Administrator as well as authorized signatories for the purpose of opening accounts of DHA or similar other authorities subject to the condition that all other requirements laid down under PR-M1 shall be complied with in letter and spirit.</p>
V	Agents Accounts	<p>Certified copy of 'Power of Attorney'.</p> <p>(i) Attested photocopy of identity card of the agent.</p>
VI	Trust Account	<p>(i) Attested photocopy of identity cards of all the trustees.</p> <p>(ii) Certified copy of 'Instrument of Trust' or Trust Deed.</p>
VII	Executors and Administrators	<p>(i) Attested photocopy of identity cards of the Executor/Administrator.</p> <p>(ii) Certified copy of Letter of Administration or Probate.</p>

Note: * In case where the depositor/borrower has not yet obtained Computerized National Identity Card (CNIC), the banks/DFIs may obtain attested copies of Old National Identity Card and receipt of National Database Registration Authority (NADRA) (evidencing that the client has applied for CNIC) alongwith an undertaking in writing that a copy of CNIC will be submitted immediately on receipt of the same. Further, banks/DFIs may accept an attested copy of valid "Alien Registration Card" issued by National Aliens Registration Authority (NARA) instead of CNIC in case of registered aliens who wish to open a bank account in Pakistan in Pak. Rupees only. Likewise, banks/DFIs may also accept attested copy of National Identity Card for Overseas Pakistani (NICOP) and Pakistan Origin Card (POC) issued by NADRA from their holders for opening bank accounts in Pakistan both in local and foreign currency in lieu of CNIC.

** The condition of obtaining Board Resolution and Certificate of Commencement of Business for opening bank account has been relaxed for only such foreign companies/entities belonging to countries where said requirements are not enforced under their laws/regulations. However, such foreign companies will have to furnish the following documents in lieu of resolution passed by BOD for opening of account and Certificate of Commencement of Business to the satisfaction of their banks.

- a. Power of Attorney from the competent authority for opening bank accounts.
- b. A certificate from the company Secretary, duly authorized by the Board, that the entity started its business from certain date and that certificate of Commencement of Business is not issued in that country.

EXAMPLES OF SUSPICIOUS TRANSACTIONS UNDER REGULATION M-5

1. General Comments

The list of situations given below is intended mainly as a means of highlighting the basic ways in which money may be laundered. While each individual situation may not be sufficient to suggest that money laundering is taking place, a combination of such situations may be indicative of such a transaction. Further, the list is by no means complete, and will require constant updating and adaptation to changing circumstances and new methods of laundering money. The list is intended solely as an aid, and must not be applied as a routine instrument in place of common sense.

A customer's declarations regarding the background of such transactions should be checked for plausibility. Not every explanation offered by the customer can be accepted without scrutiny.

It is justifiable to suspect any customer who is reluctant to provide normal information and documents required routinely by the bank in the course of the business relationship. Banks should pay attention to customers who provide minimal, false or misleading information or, when applying to open an account, provide information that is difficult or expensive for the bank to verify.

2. Transactions Which Do Not Make Economic Sense

- i) A customer-relationship with the bank that does not appear to make economic sense, for example, a customer having a large number of accounts with the same bank, frequent transfers between different accounts or exaggeratedly high liquidity;
- ii) Transactions in which assets are withdrawn immediately after being deposited, unless the customer's business activities furnish a plausible reason for immediate withdrawal;
- iii) Transactions that cannot be reconciled with the usual activities of the customer, for example, the use of Letters of Credit and other methods of trade finance to move money between countries where such trade is not consistent with the customer's usual business;
- iv) Transactions which, without plausible reason, result in the intensive use of what was previously a relatively inactive account, such as a customer's account which shows virtually no normal personal or business related activities but is used to receive or disburse unusually large sums which have no obvious purpose or relationship to the customer and/or his business;
- v) Provision of bank guarantees or indemnities as collateral for loans between third parties that are not in conformity with market conditions;
- vi) Unexpected repayment of an overdue credit without any plausible explanation;
- vii) Back-to-back loans without any identifiable and legally admissible purpose.

3. Transactions Involving Large Amounts of Cash

- i) Exchanging an unusually large amount of small-denominated notes for those of higher denomination;
- ii) Purchasing or selling of foreign currencies in substantial amounts by cash settlement despite the customer having an account with the bank;
- iii) Frequent withdrawal of large amounts by means of cheques, including traveller's cheques;
- iv) Frequent withdrawal of large cash amounts that do not appear to be justified by the customer's business activity;

- v) Large cash withdrawals from a previously dormant/inactive account, or from an account which has just received an unexpected large credit from abroad;
- vi) Company transactions, both deposits and withdrawals, that are denominated by unusually large amounts of cash, rather than by way of debits and credits normally associated with the normal commercial operations of the company, e.g. cheques, letters of credit, bills of exchange, etc;
- vii) Depositing cash by means of numerous credit slips by a customer such that the amount of each deposit is not substantial, but the total of which is substantial;
- viii) The deposit of unusually large amounts of cash by a customer to cover requests for bankers' drafts, money transfers or other negotiable and readily marketable money instruments;
- ix) Customers whose deposits contain counterfeit notes or forged instruments;
- x) Large cash deposits using night safe facilities, thereby avoiding direct contact with the bank;
- xi) Customers making large and frequent cash deposits but cheques drawn on the accounts are mostly to individuals and firms not normally associated with their business;
- xii) Customers who together, and simultaneously, use separate tellers to conduct large cash transactions or foreign exchange transactions.

4. Transactions Involving Bank Accounts

- i) Matching of payments out with credits paid in by cash on the same or previous day;
- ii) Paying in large third party cheques endorsed in favour of the customer;
- iii) Substantial increases in deposits of cash or negotiable instruments by a professional firm or company, using client accounts or in-house company or trust accounts, especially if the deposits are promptly transferred between other client company and trust accounts;
- iv) High velocity of funds through an account, i.e., low beginning and ending daily balances, which do not reflect the large volume of funds flowing through an account;
- v) Multiple depositors using a single bank account;
- vi) An account opened in the name of a moneychanger that receives structured deposits;
- vii) An account operated in the name of an offshore company with structured movement of funds.

5. Transactions Involving Transfers Abroad

- i) Transfer of money abroad by an interim customer¹ in the absence of any legitimate reason;
- ii) A customer which appears to have accounts with several banks in the same locality, especially when the bank is aware of a regular consolidated process from such accounts prior to a request for onward transmission of the funds elsewhere;
- iii) Repeated transfers of large amounts of money abroad accompanied by the instruction to pay the beneficiary in cash;
- iv) Large and regular payments that cannot be clearly identified as bona fide transactions, from and to countries associated with (i) the production, processing or marketing of narcotics or other illegal drugs or (ii) criminal conduct;
- v) Substantial increase in cash deposits by a customer without apparent cause, especially if such deposits are subsequently transferred within a short period out of the account and/or to a destination not normally associated with the customer;
- vi) Building up large balances, not consistent with the known turnover of the customer's business, and subsequent transfer to account(s) held overseas;

- vii) Cash payments remitted to a single account by a large number of different persons without an adequate explanation.

6. Investment Related Transactions

- i) Purchasing of securities to be held by the bank in safe custody, where this does not appear appropriate, given the customer's apparent standing;
- ii) Requests by a customer for investment management services where the source of funds is unclear or not consistent with the customer's apparent standing;
- iii) Larger or unusual settlements of securities transactions in cash form;
- iv) Buying and selling of a security with no discernible purpose or in circumstances which appear unusual.

7. Transactions Involving Unidentified Parties

- i) Provision of collateral by way of pledge or guarantee without any discernible plausible reason by third parties unknown to the bank and who have no identifiable close relationship with the customer;
- ii) Transfer of money to another bank without indication of the beneficiary;
- iii) Payment orders with inaccurate information concerning the person placing the orders;
- iv) Use of pseudonyms or numbered accounts for effecting commercial transactions by enterprises active in trade and industry;
- v) Holding in trust of shares in an unlisted company whose activities cannot be ascertained by the bank;
- vi) Customers who wish to maintain a number of trustee or clients' accounts that do not appear consistent with their type of business, including transactions that involve nominee names.

8. Miscellaneous Transactions

- i) Purchase or sale of large amounts of precious metals by an interim customer;
- ii) Purchase of bank cheques on a large scale by an interim customer;
- iii) Extensive or increased use of safe deposit facilities that do not appear to be justified by the customer's personal or business activities.

CHARACTERISTICS OF FINANCIAL TRANSACTIONS THAT MAY
BE A CAUSE FOR INCREASED SCRUTINY UNDER REGULATION M-5

A. Accounts:

- 1) Accounts that receive relevant periodical deposits and are dormant at other periods. These accounts are then used in creating a legitimate appearing financial background through which additional fraudulent activities may be carried out.
- 2) A dormant account containing a minimal sum suddenly receives a deposit or series of deposits followed by daily cash withdrawals that continue until the sum so received has been removed.
- 3) When opening an account, the customer refuses to provide information required by the financial institution, attempts to reduce the level of information provided to the minimum or provides information that is misleading or difficult to verify.
- 4) An account for which several persons have signature authority, yet these persons appear to have no relation among each other (either family ties or business relationship).
- 5) An account opened by a legal entity or an organization that has the same address as other legal entities or organizations but for which the same person or persons have signature authority, when there is no apparent economic or legal reason for such an arrangement (for example, individuals serving as company directors for multiple companies headquartered at the same location, etc.).
- 6) An account opened in the name of a recently formed legal entity and in which a higher than expected level of deposits are made in comparison with the income of the promoter of the entity.
- 7) The opening by the same person of multiple accounts into which numerous small deposits are made that in aggregate are not commensurate with the expected income of the customer.
- 8) An account opened in the name of a legal entity that is involved in the activities of an association or foundation whose aims are related to the claims or demands of a terrorist organization.
- 9) An account opened in the name of a legal entity, a foundation or an association, which may be linked to a terrorist organization and that shows movements of funds above the expected level of income.

B. Deposits and Withdrawals:

- 1) Deposits for a business entity in combinations of monetary instruments that are a typical of the activity normally associated with such a business.
- 2) Large cash withdrawals made from a business account not normally associated with cash transactions.
- 3) Large cash deposits made to the account of an individual or legal entity when the apparent business activity of the individual or entity would normally be conducted in cheques or other payment instruments.

- 4) Mixing of cash deposits and monetary instruments in an account in which such transactions do not appear to have any relation to the normal use of the account.
- 5) Multiple transactions carried out on the same day at the same branch of a financial institution but with an apparent attempt to use different tellers.
- 6) The structuring of deposits through multiple branches of the same financial institution or by groups of individuals who enter a single branch at the same time.
- 7) The deposit or withdrawal of cash in amounts which fall consistently just below identification or reporting thresholds.
- 8) The presentation of uncounted funds for a transaction. Upon counting, the transaction is reduced to an amount just below that which would trigger reporting or identification requirements.
- 9) The deposit or withdrawal of multiple monetary instruments at amounts which fall consistently just below identification or reporting thresholds, if any, particularly if the instruments are sequentially numbered.

C. Wire Transfers:

- 1) Wire transfers ordered in small amounts in an apparent effort to avoid triggering identification or reporting requirements.
- 2) Wire transfers to or for an individual where information on the originator, or the person on whose behalf the transaction is conducted, is not provided with the wire transfer, when the inclusion of such information would be expected.
- 3) Use of multiple personal and business accounts or the accounts of non-profit organizations or charities to collect and then funnel funds immediately or after a short time to a small number of foreign beneficiaries.
- 4) Foreign exchange transactions that are performed on behalf of a customer by a third party followed by wire transfers of the funds to locations having no apparent business connection with the customer or to countries of specific concern.

D. Characteristics of the Customer or His/Her Business Activity:

- 1) Funds generated by a business owned by individuals of the same origin or involvement of multiple individuals of the same origin from countries of specific concern acting on behalf of similar business types.
- 2) Shared address for individuals involved in cash transactions, particularly when the address is also a business location and/or does not seem to correspond to the stated occupation (for example student, unemployed, self-employed, etc.).
- 3) Stated occupation of the transactor is not commensurate with the level or type of activity (for example, a student or an unemployed individual who receives or sends large numbers of wire transfers, or who makes daily maximum cash withdrawals at multiple locations over a wide geographic area).
- 4) Regarding non-profit or charitable organizations, financial transactions for which there appears to be no logical economic purpose or in which there appears to be no link between the stated activity of the organization and the other parties in the transaction.

- 5) A safe deposit box is opened on behalf of a commercial entity when the business activity of the customer is unknown or such activity does not appear to justify the use of a safe deposit box.
- 6) Unexplained inconsistencies arising from the process of identifying or verifying the customer (for example, regarding previous or current country of residence, country of issue of the passport, countries visited according to the passport, and documents furnished to confirm name, address and date of birth).

E. Transactions Linked to Locations of Concern:

- 1) Transactions involving foreign currency exchanges that are followed within a short time by wire transfers to locations of specific concern (for example, countries designated by national authorities, FATF non-cooperative countries and territories, etc.).
- 2) Deposits are followed within a short time by wire transfers of funds, particularly to or through a location of specific concern (for example, countries designated by national authorities, FATF non-cooperative countries and territories, etc.).
- 3) A business account through which a large number of incoming or outgoing wire transfers take place and for which there appears to be no logical business or other economic purpose, particularly when this activity is to, through or from locations of specific concern.
- 4) The use of multiple accounts to collect and then funnel funds to a small number of foreign beneficiaries, both individuals and businesses, particularly when these are in locations of specific concern.
- 5) A customer obtains a credit instrument or engages in commercial financial transactions involving movement of funds to or from locations of specific concern when there appears to be no logical business reasons for dealing with those locations.
- 6) The opening of accounts of financial institutions from locations of specific concern.
- 7) Sending or receiving funds by international transfers from and/or to locations of specific concern.

PROCEDURE FOR DEPOSIT OF SPONSOR SHARES INTO
A BLOCKED ACCOUNT WITH CDC

Following procedure shall be followed by banks for deposit/transfer of sponsor shares into CDC account:

1. The existing sponsor shareholders who have already deposited their shares with SBP BSC shall :
 - a) Open account (sub-participant account or investor account) at CDC exclusively for depositing sponsor shares and subsequent bonus and right shares.
 - b) Confirm the account number to SBP through company secretary of the bank.
 - c) On receipt of above confirmation, SBP will allow the withdrawal of shares deposited with SBP BSC for deposit with CDC.
 - d) The bank shall confirm the deposit of sponsor shares in the CDC account within 15 days of release of shares by SBP.
2. The prospective sponsor shareholders shall open CDC account (sub participant account or investor account) and confirm the account number to SBP through Company Secretary of the bank at least 15 days prior to issuance/transfer of shares. Further, they shall arrange for confirmation of submission of shares in CDC account within 3 days of issuance of shares.
3. For those sponsor shareholders who are yet to deposit their sponsor shares in a blocked account with CDC, shall either open a new account or identify an existing account.