CENTRAL BANK OF SOMALIA

Financial Institution Law, 2012

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Regulation on Capital Adequacy, 2014

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1. INTRODUCTION

1.1. Authority

This regulation is made by the Central Bank pursuant to its authority set forth in Sections 14(1)-(2), 15(1), and 34 of the Financial Institution Law, 2012 ("FIL"), and Sections 38(1) and 52(1) of the Central Bank of Somalia Law, 2011, for the purpose of implementing Sections 14 (Minimum Capital Requirements), 15 (Minimum Ongoing Capital Requirements), and 18 (Submission of Forms for Capital Adequacy Computation) of the FIL.

1.2. Applicability

This regulation applies to all persons licensed by the Central Bank to engage in banking business in Somalia. The requirements of this regulation apply to each bank individually, and on a fully consolidated basis to each bank, its holding company, and members of its group, if applicable.[1]

2. CAPITAL REQUIREMENTS

2.1. Minimum Amount of Capital[2]

Unless the Central Bank notifies a bank in writing of a higher capital requirement pursuant to Sections 14(6) and 15(2) of the FIL, banks shall at all times maintain in Somalia unimpaired paid-up capital, or assigned capital in the case of a branch of a foreign bank, in an amount which exceeds USD 5,000,000.

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[1] Section 14(1), FIL; ¶20-23, "Introduction," *International Convergence of Capital Measurement and Standards*, Basel II-Comprehensive Version, Basel Committee on Banking Supervision, 2006.
[2] Sections 14(1), 14(2)(a) and 15(1)(b), FIL; Principle 6 "Capital Adequacy;" Essential criterion 7 of Principle 3 "Licensing Criteria," *Core Principles for Effective Banking Supervision*, Basel Committee, 2006.

2.2. Minimum Capital Ratios[3]

2.2.1. Capital Adequacy Ratio

(Total Capital / Total Net Assets) x 100

Each bank shall at all times maintain a Capital Adequacy Ratio which equals or exceeds twelve percent (12%).

2.2.2. Core Capital Ratio

(Core Capital / Total Net Assets) x 100

Each bank shall at all times maintain a Core Capital Ratio which equals or exceeds eight percent (8%).

3. CALCULATIONS[4]

3.1. Total Capital[5]

Total Capital = Core Capital + Supplemental Capital.

3.2. Core Capital[6]

Core Capital = The sum of the qualifying capital accounts listed in 3.2.1
– */minus/less* the accounts listed in 3.2.

[3] Section 14(1), FIL; ¶49-50, "Definition of Capital," *Basel III: A Global Framework for More Resilient Banks and Banking System*, Basel Committee, December 2010 (revised June 2011); Principle 6 "Capital Adequacy," Essential Criteria 1, 2, 4 & 5, and Additional Criterion 2, *Core Principles Methodology*, Basel Committee, 2006.
[4] Section 15(1)(c), FIL.
[5] Section 15(1)(c), FIL; ¶49, "Components of Capital," *Basel III: A Global Framework for More Resilient Banks and Banking System*, Basel Committee, December 2010 (revised June 2011).
[6] Section 15(1)(a),(c), FIL.

3.2.1. Elements of Core Capital[7]

(i) Unimpaired ordinary paid-up share capital or assigned capital in the case of a foreign bank;

(ii) Unimpaired paid-up non-cumulative perpetual preference shares;

(iii) Share premium; and

(iv) Accumulated retained earnings in the amount reported in the most recent audited accounts approved by the Central Bank[8], less any accumulated losses in the current year.

3.2.2. Deductions[9]

(i) Goodwill;

(ii) The amount of the bank's investments in the capital of other banks, financial institutions and insurance companies; and

(iii) The amount of the bank's investment in its own shares (treasury stock).

3.3. Supplemental Capital[10]

Supplemental Capital = The sum of the following listed qualifying accounts.

(i) Current year-to-date net profit after tax, unaudited;[11]

(ii) Financial market instruments that are unsecured and subordinate to the interests of shareholders and creditors and that have been deemed satisfactory by the Central Bank.[12]

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[7] Core Capital is also referred to as Tier 1 Capital in Basel III. ¶52-56, "Common Equity Tier 1" and "Additional Tier 1 Capital", *Basel III: A Global Framework for More Resilient Banks and Banking System*, Basel Committee, December 2010 (revised June 2011).

[8] Sections 20(1) and 20(5)(a), FIL.

[9] ¶66-86, "Regulatory Adjustments," *Basel III: A Global Framework for More Resilient Banks and Banking System*, Basel Committee, December 2010 (revised June 2011).

[10] Section 15(1)(d), FIL; ¶57, "Tier 2 Capital," *Basel III: A Global Framework for More Resilient Banks and Banking System*, Basel Committee, December 2010 (revised June 2011).

[11] Current year's interim profits are included in Supplemental Capital. National authorities are permitted to require that interim profit or loss be audited, verified, or subject to review procedures before being included in *Core Capital* instead of in Supplemental Capital; ¶52, *Basel III: A Global Framework for More Resilient Banks and Banking System*, Basel Committee, December 2010 (revised June 2011).

[12] Subordinated debt, ¶58, "Criteria for Inclusion in Tier 2 Capital," *Basel III: A Global Framework for More Resilient Banks and Banking System*, Basel Committee, December 2010 (revised June 2011).

4. CAPITAL PLANNING POLICY[13]

The board of directors of each bank will ensure that executive officers develop, implement, maintain, and regularly update a Capital Planning Policy. To be considered adequate, the Capital Planning Policy must meet the following minimum requirements:

4.1. Be in writing;

4.2. Be reviewed, updated, and approved by the board of directors at least annually;

4.3. Identify the material risks to which the bank is subject;

4.4. Account for the bank's material risks in its targeted capital levels and ratios;

4.5. Explain the process by which the board of directors expects management to establish capital targets, capital levels and ratios that exceed the minimum requirements of this regulation.

4.6. Include measures to ensure that the capital targets will support the bank's current operations and future capital needs based on its business plan;

4.7. Specify the principles that management is to follow when making decisions about how to deploy the bank's capital;

4.8. Require effective coordination and clear communication between those persons who are responsible for capital and liquidity monitoring and management; and

4.9. Establish protocols for management to follow to preserve capital during economic downturns and other events which threaten the bank's capital.

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[13] Section 15(1)(d), FIL; *A Sound Capital Planning Process: Fundamental Elements*, Basel Committee, 2014; and Additional Criterion 3 of Principle 6, "Capital Adequacy," *Core Principles for Effective Banking Supervision*, Basel Committee, 2006.

5. RESTRICTIONS ON CAPITAL DISTRIBUTIONS[14]

5.1. No bank shall make a voluntary capital distribution unless the bank exceeds, and will continue to exceed after making the distribution, the minimum required amount of capital and the minimum Capital Adequacy Ratios.

5.2. A bank that holds capital in excess of the minimum required amount and exceeding the minimum Capital Adequacy Ratios, may make voluntary capital distributions in accordance with the following guidelines:

Core Capital Ratio	Maximum Annual Earnings[15] Payout Ratio Permitted
8.0 – 10.0%	25%
10.1 – 12.0%	50%
12.1 – 14.0 %	75%
14.1% +	100%

6. REPORTING[16]

No later than the close of business on the last day of the month following a calendar-quarter-end and in the format prescribed by the Central Bank, each bank shall submit to the Central Bank a report showing the calculation of Total Capital, Core Capital, Supplemental Capital, Total Net Assets, the Capital Adequacy Ratio, and the Core Capital Ratio in accordance with this regulation.

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[14] Section 14(3), FIL; ¶122-150, "Capital Conservation Buffer," *Basel III: A Global Framework for More Resilient Banks and Banking System*, Basel Committee, December 2010 (revised June 2011); Essential Criterion 6 of Principle 6, "Capital Adequacy," *Core Principles for Effective Banking Supervision*, Basel Committee, 2006.

[15] Earnings are defined as distributable profits, calculated prior to the deduction of distributions and after the tax which would have been reported had none of the distributable items been paid, pursuant to ¶132(b), *Basel III: A Global Framework for More Resilient Banks and Banking System*, Basel Committee, December 2010 (revised June 2011).

[16] Section 18, FIL; and Essential Criterion 1 of Principle 21, "Supervisory Reporting," *Core Principles for Effective Banking Supervision*, Basel Committee, 2006.

CENTRAL BANK OF SOMALIA

Report on Capital Adequacy

Line No.	Description	Amount
	Elements of Core Capital	
10	Unimpaired paid-up ordinary share capital and premium (or assigned capital in the case of a foreign bank)	
20	Unimpaired paid-up non-cumulative perpetual preference shares and premium	
30	Accumulated retained earnings - Audited	
	Deductions	
40	Current year loss, if applicable	
50	Goodwill	
60	Investments in other banks, financial institutions and insurance companies	
70	Treasury stock	
80	**CORE CAPITAL** (10 + 20 + 30) – (40 + 50 + 60 + 70)	
	Elements of Supplemental Capital	
90	Current year net profit after tax - Unaudited	
100	Eligible subordinated debt	
110	**SUPPLEMENTAL CAPITAL** (90 + 100)	
120	**TOTAL CAPITAL** (80 + 110)	
130	**TOTAL NET ASSETS** (from balance sheet of same reporting date)	
Line No.	**Ratio**	**%**
140	**Capital Adequacy Ratio** (120 / 130) x 100	
150	**Core Capital Ratio** (80 / 130) x 100	