

**Consultation on the Proposed Amendments to Licensing Requirements Module (Module LR)-  
Minimum Capital Requirement-Volumes 1 & 2**  
Industry Comments and Feedback  
April 2017

Specific Comments:			
Reference to the draft Directive:	Comments	REF	CBB's Response
Volume 1: LR- 2.5.2CB All <del>Bahrain</del> retail <del>branches</del> of <del>foreign</del> overseas <u>conventional</u> <u>retail banks</u> must maintain a minimum capital of BD 20 million, including general reserves and retained earnings. Such minimum must be maintained within a period of 5 years ending on 31 <sup>st</sup> December, 2021.	<p><b>A legal firm</b> noted the following:</p> <ol style="list-style-type: none"> <li>1. As <u>we believe that the Bahraini legal system does not support the separate entity doctrine for local branches of foreign entities (i.e. Bahrain law contemplates that a branch is not a separate person with an autonomous legal personality), we think that the requirement for a minimum capital of the branch would be legally ineffective.</u> Based upon the single entity doctrine, the assets of the branch would not be ring-fenced from the assets of the parent undertaking to which the branch belongs in case of insolvency such that all creditors of the combined parent undertaking and all its legally indistinct branches (and not only creditors of the branch) would have recourse against the “capital” of the branch. Similarly, creditors of the branch would have recourse against the assets of the parent undertaking and other legally indistinct branches.</li> <li>2. To the extent that, however, the intention is to introduce such requirement for minimum local liquidity (or initial local liquidity), <u>we would suggest naming it as “dotation capital” or “endowment capital” as these represent common terms of art for the purpose of referring to the capital of a legally indistinct branch and would avoid any confusion with “share capital”.</u> We would also <u>suggest eliminating any reference to reserves and retained earnings, as the branch does not technically maintain distinct shareholder equity or pay dividends (and therefore does not have retained earnings)</u> and is not otherwise subject to capital maintenance rules under the Commercial Companies Law since its legal status is as a “foreign company incorporated abroad and undertaking its activities in Bahrain” (Commercial Companies Law, Article 346).</li> </ol>	SP-1	This comment is not applicable as according to the CBB's regulatory framework an overseas bank is treated as a separate legal entity.

**Consultation on the Proposed Amendments to Licensing Requirements Module (Module LR)-  
Minimum Capital Requirement-Volumes 1 & 2**  
Industry Comments and Feedback  
April 2017

<p><b>Volume 2: LR-2.5.2C All overseas Islamic retail banks must maintain a minimum capital of BD 20 million, including general reserves and retained earnings. Such minimum must be maintained within a period of 5 years ending on 31<sup>st</sup> December, 2021.</b></p>	<p><b>A Bank noted the following:</b> Our group structure is designed to deploy capital to support business and / or branches in all circumstances. In addition, capital requirements from home supervisors ensure that the financial institution is adequately capitalized. While issuing the directive under discussion, <u>CBB may take into account that the capital requirements of a foreign bank branch commensurate to the size and scope of business of branches.</u> If CBB is considering absolute amount of minimum capital, these could be based on business scope with incremental increases linked to growth of business.</p>	SP-2	Noted, but this recommended approach does not address competition issues.
	<p><b>A Bank noted the following:</b> While we maintain our strong belief that enhancing the regulatory framework of GCC Central Banks is very important to the future of the GCC economies, we view the proposed minimum capital of BHD 20 million within 5 years, to <u>be very challenging for retail branches of Foreign Banks.</u> This opinion is based on the recent economic country outlook where Moody's expects real GDP growth over the next four years to be only 2.2% on average, in addition to the looming risk of further interest rate hikes affecting the borrowing costs, which could exert negative effect on the economic activity and the banking sector growth. Therefore, <u>we kindly seek the CBB consideration to reduce the capital requirement to BHD 15 million.</u> Such increase would mean doubling our current paid up capital of BHD 7.5 million, to be maintained within, or beyond the proposed 5 year period ending on December 31, 2021, noting that the bank – Bahrain has retained all the profits generated over the past 10 years, since its inception in 2007. We seize this opportunity to inform you that the Capital Levels of the Parent Bank, the bank, are well in line with the local Lebanese minimum regulatory ratios and the Basel III requirements, with a Common Equity Tier 1 Ratio of 12.08% and a Total Capital Adequacy Ratio of 14.74% as at December 31, 2016.</p>	SP-3	Given that it is required over 5 years period, a regular assessment shall be done.
	<p><b>A Bank noted the following:</b> 1. We respectfully submit that this capital increase would be restrictive to mid-sized and niche banks who may find it challenging to achieve this level in the time frame indicated. <u>Therefore we suggest that CBB view such cases with some leniency, and if banks are retaining profits, then allow them beyond December 31, 2021 until by doing so they achieve the desired level.</u> In our case in the meantime HBL Bahrain branches will continue to be supported by our parent. A <u>letter of comfort</u> in this respect is already with the CBB. Please note, we will require the approval of our regulator, the State Bank of Pakistan, to retain earnings to the desired level.  2. The CBB may also consider an alternative approach by <u>linking capital &amp; retained earnings to a CAR ratio.</u>  3. In addition to the above, currently we are maintaining retained earnings both in BHD and USD. This is because we have an asset book both in BHD and USD. Since the peg between BHD and USD is fixed and stable, we suggest that this structure should be maintained and banks be permitted to building up retained earnings both in USD and BHD. This would assist all banks in this market.</p>	SP-4	See SP-3 above.

**Consultation on the Proposed Amendments to Licensing Requirements Module (Module LR)-  
Minimum Capital Requirement-Volumes 1 & 2**  
Industry Comments and Feedback  
April 2017

<p>A</p>	<p><b>A Bank noted the following:</b> We are of the opinion that regulatory requirements <u>be aligned to the Basel III framework</u> on a forward looking basis.</p> <p>Ultimately we would like to foresee Capital on a Parent/Solo basis and whereby branches that operate under a full Basel III framework are exempt from holding specific regulatory capital and whereby the Central Bank of Bahrain instead principally considers the total capital resources of the Parent.</p> <p>We reiterate that the bank Bahrain has submitted a <u>Letter of Guarantee</u> issued by the Parent re the Capital and addressed to Central Bank of Bahrain in support of our reasoning and opinion as above.</p>	<p>SP-5</p>	<p>This is not an international practice. All GCC countries require a minimum capital for branches of foreign banks.</p>
	<p><b>A Bank noted the following:</b></p> <ol style="list-style-type: none"> <li>1. In this connection, we submit that as on 28.02.2017, our Branch has maintained an amount of BHD 13.21 mio as Capital + Reserves/retained earnings. Further, we are continually maintaining our LTD Ratio below 80% rendering 20% of the deposits and the entire Capital &amp; reserves as surplus without making much earning. This surplus funds are being parked in un-remunerative assets (placements) making an average yield of 1.00%-1.50%, thereby considerably reducing the net interest margin as well as the net profit.</li> <li>2. Further, almost 65% of our deposits are in the form of term deposits putting pressure on our cost of funds and thus on profitability. It has also impacted our 'Return on Equity' which is on a reducing trend year over year. On the asset side, all our loans are Bahrain based and are extended to Bahrain Companies / Bahraini residents, thereby contributing to the growth of SME, Trading, Manufacturing, Services and Consumer sectors of the country. Accordingly, we are actively participating in the economic growth of the Kingdom of Bahrain.</li> <li>3. At present, we have idle funds/resources to the tune of BHD 22.21 mio in the form of capital and retained earnings and deposits that could not be deployed on account of LTD ratio. Given the size of our Balance sheet these are the main sources of liquidity for us. Further, we always have full support from our Parent issued in shape of an <u>unconditional, irrevocable and limitless Guarantee</u> to Central Bank of Bahrain, certifying that SBI is committed to support the Retail Branch in the Kingdom of Bahrain at all times.</li> <li>4. In view of the foregoing, we do not perceive any liquidity crisis at any point of time in future. As we are</li> </ol>	<p>SP-6</p>	<p>The new requirement is being applied by all GCC countries and it is now becoming a pre-condition for any regulatory harmonization. Please also see our response to SP-3.</p>

**Consultation on the Proposed Amendments to Licensing Requirements Module (Module LR)-  
Minimum Capital Requirement-Volumes 1 & 2**  
Industry Comments and Feedback  
April 2017

	<p>committed in enhancing the growth of the economy in the Kingdom through lending to local retail as well as corporate sectors, we are therefore, of the considered view that the Central Bank of Bahrain may consider:</p> <ul style="list-style-type: none"><li>i) <u>Not to raise the capital requirement</u> for Branch of Foreign Retail Banks having small presence in Bahrain (or alternatively Balance sheet size may be stipulated for maintaining the minimum capital), and</li><li>ii) That <u>Capital and Reserve / Retained Earnings to form part of resources as stable fund while calculating the LTD Ratio.</u></li></ul>		
--	--	--	--