



Banc Ceannais na hÉireann
Central Bank of Ireland

Eurosystem

2013

Code of Practice on Lending to Related Parties



Code of Practice on Lending to Related Parties

1 Overview

In order to guard against abuses in lending to related parties and to address possible conflicts of interest, the Central Bank hereby requires that such lending be on an arm's length basis and subject to appropriate management oversight and limits.

2 Legal Basis and Application of this Code

This Code is imposed pursuant to Section 117 of the Central Bank Act 1989 on banks incorporated in the State licensed under Section 9 of the Central Bank Act 1971 and on building societies authorised under the Building Societies Act 1989. It also applies to designated credit institutions registered under the Asset Covered Securities Act 2001. Separately from this document, the reporting requirements described in Part 7 of the Code will be imposed from time to time pursuant to Section 117(3) (a) of the Central Bank Act 1989.

This Code does not apply to credit institutions incorporated in other EEA member states who conduct their business in the State on a branch or services basis pursuant to EU law and Directive 2006/48/EC relating to the taking up and pursuit of the business of credit institutions (recast) ("Directive 2006/48/EC").

References in this Code to provisions of statute (whether under the laws of the State or EU) are references to those provisions as amended, substituted or replaced from time to time.

A contravention of the Code may be liable to the Central Bank using any of its regulatory powers, including but not limited to one or both of the following:

- The imposition of an administrative sanction under Part IIIC of the Central Bank Act, 1942;
- The prosecution of an offence.

3. Commencement

The original 2010 Code came into force on 1 January 2011. This revised Code comes into force on 1 July 2013.

4. Scope of Loans Covered by this Code

This Code applies to all loans to related parties, whether granted:

- in the State or outside the State; or
- prior or subsequent to the entry into force of this Code.

5. Definitions:

Board: means the board of directors of the credit institution.

Business Day: Any day except Saturday, Sunday, bank holidays and public holidays in Ireland.

Connected Persons and Clients:

- (a) a spouse, domestic partner, civil partner (within the meaning of the Civil Partnership and Certain Rights and Obligations of Cohabitants Act 2010) or child (whether natural or adopted) of a person;
- (b) two or more natural or legal persons who, unless it is shown otherwise, constitute a single risk because one of them, directly or indirectly, has control over the other or others; or
- (c) two or more natural or legal persons between whom there is no relationship of control as set out in point (b) but who are to be regarded as constituting a single risk because they are so interconnected that, if one of them were to experience financial problems, the other or all of the others would be likely to encounter repayment difficulties.

Credit Institution: A bank licensed under Section 9 of the Central Bank Act 1971 or a building society authorised under the Building Societies Act 1989, including a credit institution registered as a designated credit institution under the Asset Covered Securities Act 2001.

Exposure: Exposure has the meaning as set out in Directive 2006/48/EC.

Lending: The provision of a loan.

Loan: Loan includes loan, quasi-loan or credit transaction which results in an exposure or potential exposure, including guarantees.

Own Funds: Own funds has the meaning as set out in Directive 2006/48/EC.

Related Party: A director, senior manager or significant shareholder of the credit institution or an entity in which the credit institution has a significant shareholding, as well as a connected person of any of the aforementioned persons.

Senior Management: Members of management of the institution or person who report directly to the board of directors or the chief executive (howsoever described) of the credit institution.

Senior Manager: A person who is a member of senior management.

Significant Shareholder: A person who holds, either themselves or in aggregate with their connected persons, a significant shareholding. Governments are excluded from this definition.

Significant Shareholding: 10% or more of the shares or voting rights in the credit institution or business.

6. Requirements of the Code

Credit institutions shall observe the following code of practice in granting or otherwise dealing with loans to related parties:

- a) a credit institution shall not grant a loan to a related party on more favourable terms (including without limitation terms as to credit assessment, duration, interest rates, amortisation schedules, collateral requirements) than a loan by the credit institution to non-related parties. An exemption is permitted for beneficial terms that are part of a remuneration package available to staff of the credit institution generally (e.g. staff loans at favourable rates) provided that such terms have been approved by the Board;
- b) a loan to a related party, or any variation of the terms of a loan to a related party, shall be subject to individual prior approval by the Board or a subcommittee of the Board established specifically to deal with related party lending where that subcommittee reports directly to the Board. Board members with conflicts of interest shall be excluded from the approval process;
- c) actions in respect of the management of a loan to a related party (including but not limited to permitting interest roll-up, granting a grace period for payment, loan write-off in whole or in part, provisioning against a loan, decisions to take or not to take enforcement action) shall be subject to individual prior approval in writing by the Board or a subcommittee of the Board established specifically to deal with related party lending where that subcommittee reports directly to the Board;
- d) where loans to a related party will exceed one million Euro the prior approval of the Central Bank is required;
- e) policies and processes shall be in place, and adhered to, in order to prevent:
 - (i) members of staff of the credit institution benefiting from lending to a related party (otherwise than the receipt of

- standard remuneration also available in lending to non-related parties, and
- (ii) persons related to the borrower from being part of the process of granting and managing a loan to such borrower;
- f) policies and processes shall be in place, and adhered to, in order to identify individual loans to a related party as well as the total amount of such loans and to monitor and report on such loans through an independent credit review process;
 - g) related party lending shall be subject to a written process, approved in advance by the Board, of on-going monitoring by senior management;
 - h) there shall be in place an obligation on senior management to report to the Board, on at least a quarterly basis, for timely action by the Board, any deviation from a policy, process or limit required by this Code. Furthermore, the institution shall, within 5 business days, report any such deviation to the Central Bank, advising of the background and the proposed remedial action;

- i) a credit institution shall not lend to a related party where to do so would result in the exposures of the credit institution exceeding one or more of the following limits:

Exposure Category	Limit
I. Exposures to any one of the credit institution's directors or senior management, and persons connected to them, including any exposures to any business in which the director or senior manager has a significant shareholding.	0.5% of own funds
II. The aggregate of exposures under I., above.	5.0% of own funds
III. Exposure to any one of its significant shareholders, other than credit institutions, including exposures to businesses in which the significant shareholder has a significant shareholding.*	5% of own funds
IV. The aggregate of exposures under III., above.*	15% of own funds
V. Exposures to a client or group of connected clients, other than a credit institution, in which the credit institution has a significant shareholding.	5% of own funds
VI. The aggregate of exposures under V., above.	15% of own funds

*Exemption from III and IV: A credit institution may apply to the Central Bank in writing for an exemption from the limit in III. and IV. Such an exemption would only be potentially available to the extent that an exemption is available in respect of intra-group lending to a parent undertaking, to other subsidiaries of that parent undertaking or to its own subsidiaries, in so far as those undertakings are covered by the supervision on a consolidated basis to which the credit institution itself is subject, in accordance with Article 113(2) of the CRD or with equivalent standards in force in a third country or such lending is of the type, as defined and published by the Central Bank from time to time for the purposes of this Code, as being considered to be intra-group lending.

- j) a credit institution shall not:
 - (i) engage in a practice,
 - (ii) enter into an arrangement,
 - (iii) execute a document, or
 - (iv) structure or restructure a loan,in order (whether or not as the sole or primary purpose) to avoid its obligations under this Code.

7. Reporting to the Central Bank

- a) Related party exposures shall be reported to the Central Bank on a periodic basis and in a format specified from time to time by the Central Bank pursuant to Section 117(3)(a) of the Central Bank Act 1989. This is without prejudice to the rights and powers of the Central Bank to otherwise request specific information at any point in time or to conduct inspections of a credit institution's compliance with the Code.
- b) Where a credit institution considers that there may have been an error in its conduct by reference to the requirements of this Code (including without limitation reporting requirements imposed in respect of this Code) the credit institution shall within 5 business days inform the Central Bank in writing of its proposals for correcting any such error as may have occurred. If any such information is provided to the Central Bank orally in the first instance, it shall be provided to the Central Bank in writing on the next business day.

8. Specific Exemptions

8.1 Non-Performing Loans

Where the credit institution becomes a significant shareholder in a borrower as a result of entering into an arrangement to restructure a loan, the credit institution and the borrower will become related parties for the purposes of this Code. In these circumstances, however, the subsequent provision of a loan to the borrower will be automatically exempted from the requirements of 6(d) and 6(i) above, provided that the following conditions are met at the time of providing the additional loan:

- (i) The initial acquisition of the shares or voting rights in the company must have been as a result of a scheme of arrangement or debt restructuring agreement entered into between the credit institution and the borrower due to the company being unable to repay its original debt;
- (ii) The additional loan must be issued on an arm's length basis;
- (iii) The credit institution and the borrower must not be related parties under any part of the Related Party definition other than the credit institution being a significant shareholder as a direct result of the debt restructuring arrangement;
- (iv) The Board of the credit institution is responsible for prudently satisfying itself that the credit institution is not engaging in a practice that is designed to circumvent the Code. If the Board has any doubt as to whether the Code applies to an exposure then it shall apply the Code;
- (v) In all cases it will be incumbent on the credit institution to maintain a register of these loans recording compliance with (i)-(iv) above and the credit institution must be able to

demonstrate that these loans are subject to regular monitoring and review by the credit institution's Board.

8.2 Performing Loans

Where the credit institution becomes a significant shareholder in a performing borrower in order for the borrower to secure further lending, the credit institution and the borrower will become related parties for the purposes of this Code in relation to any subsequent loans. In these circumstances, however, the subsequent provision of a loan to the borrower will be automatically exempted from the requirements of 6(d) and 6(i) above, provided that the following conditions are met at the time of providing the additional loan:

- (i) The initial acquisition of the shares or voting rights in the company must have been as a result of the collateral requirements set out in the loan agreement between the credit institution and the borrower;
- (ii) The additional loan must be issued on an arm's length basis;
- (iii) The credit institution and the borrower must not be related parties under any part of the Related Party definition other than the credit institution being a significant shareholder as a direct result of the collateral requirements in the underlying loan agreement;
- (iv) All other loans already in place between the credit institution and the borrower must be performing at the time the additional loan is issued;
- (v) The Board of the credit institution is responsible for prudently satisfying itself that the credit institution is not engaging in a

practice that is designed to circumvent the Code. If the Board has any doubt as to whether the Code applies to an exposure then it shall apply the Code;

- (vi) In all cases it will be incumbent on the credit institution to maintain a register of these loans recording compliance with (i)-(v) above and the credit institution must be able to demonstrate that these loans are subject to regular monitoring and review by the credit institution's Board.

8.3 Lending to Natural Connected Persons

- a) A credit institution is exempted from complying with the requirements at 6(b) in the case of incurring an exposure to a Connected Person as defined in category (a) of the definition of Connected Persons and Clients where such exposure relates to a personal credit card, personal overdraft or unsecured personal loan and the credit institution has incurred a total exposure of not greater than €25,000 with respect to that natural connected person;
- b) In all cases where a credit institution is availing of this exemption regarding lending to natural connected persons it will be incumbent on the credit institution to monitor such loans to ensure that the limit imposed in 8.3(a) above is not exceeded and to maintain a register of these loans recording how it has complied with this requirement;
- c) The credit institution must be able to demonstrate that these loans are subject to regular monitoring and review by the credit institution's Board.



Banc Ceannais na hÉireann
Central Bank of Ireland

Eurosystem

**Bosca PO 559, Sráid an Dáma, Baile Átha Cliath 2, Éire
PO. Box No 559, Dame Street, Dublin 2, Ireland**