Seychelles

Financial Leasing Act, 2013

Financial Leasing (Lease Classification and Provisioning) Regulations, 2014

Statutory Instrument 112 of 2014

Legislation as at 31 December 2015

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1. Citation

These Regulations may be cited as the Financial Leasing (Lease Classification and Provisioning) Regulations, 2014.

2. Interpretation

In these Regulations, unless the context otherwise requires—

"**Act**" means the Financial Leasing Act, 2013;

"**banks**" shall have the meaning ascribed to it under section 2 of the Financial Institutions Act;

"**Board of Directors**" means the highest body of authority in a financial leasing institution responsible for strategically guiding the institution, effectively monitoring management and properly accounting to shareholders;

"**book value**" means the value of a leased asset as stated on the books of account of a financial leasing institution being the amount of the financial leasing institution's investment in that asset less any specific or general provisions for loss;

"**charge-off**" means the accounting process of expensing a company's income statement in view of a facility being deemed uncollectible, such that continuation as a recoverable advance is no longer warranted and being purely an accounting entry it does not forfeit the lessee's obligation to pay the outstanding payments due or the right of the financial leasing institution to institute legal action to enforce payment of the outstanding payments due under the financial lease;

"**core capital**" shall have the meaning ascribed to it under regulation 2 of Financial Leasing (Capital adequacy and Reserve Fund) Regulations, 2014;

"**collateral**" means the net realisable value of the following assets in which the interests of the financial leasing institution is fully enforceable and may include—

(a) balances with banks;

(b) debt security issued by—

- (i) the Government of Seychelles;
- (ii) the Government of a member country of the Organisation of Economic Cooperation and Development; or
- (iii) the Government of a country with a current consensus country risk classification of one or two, as published by the Organisation of Economic Cooperation and Development;

(c) any guarantee which meets the following criteria—

(i) the guarantee is issued by—

(A) The Government of Seychelles;

(B) The Government of a member country of the Organisation of Economic Cooperation and Development; or

(C) The Government of a country with a current consensus country risk classification of one or two, as published by the Organisation of Economic Cooperation and Development;

(D) A bank with an independent credit assessment of AAA to AA issued by an external credit assessment institution acceptable to the Central Bank;

(ii) the guarantee represents a direct claim on the guarantor;

(iii) the guarantee is denominated in the same currency as the credit;

(iv) the guarantee clearly and incontrovertible defines the extent of the guarantee's cover of a specific credit;

(v) the guarantee is irrevocable and non-cancellable by the guarantor, except for non-repayment of the credit protection contract;

(vi) the guarantee has no clause in the credit protection contract that would allow the guarantor unilaterally to cancel the guarantee, increase the effective cost of the guarantee, or delay payment under the guarantee for any reason including the need to be funded in the budget;

(vii) the guarantee is realisable or enforceable only on the condition of the obligor's failure to meet his or her obligation to the financial leasing institution; and

(viii) the guarantee is executed so that the guarantor or any other person cannot challenge the legal rights of the financial leasing institution in realising enforcing the guarantee;

(d) the amount of 50 percent of the net realisable value of other tangible securities as approved by Central Bank;

"**financial lease**" means any facility issued under a financial leasing agreement and it shall be used interchangeably with the term "facility";

"**foreign financial leasing institution**" includes a bank or a company licenced in a country or territory outside Seychelles and authorised to engage in financial leasing operations in that country or territory;

"**large exposure**" means an exposure to a customer, or group of closely-related customers, that meets or exceeds 10 percent of core capital but does not exceed more than 25 percent of core capital;

"**financial lease concentration**" means an exposure to a customer or group of closely-related customers that meets or exceeds 25 percent of core capital;

"**net financial lease balance**" means the outstanding principal balance of a facility less the net realisable value of any eligible collateral;

"**net realisable value**" means the estimated selling price of an asset in the ordinary course of business less the estimated costs of recovery of the asset and the estimated costs necessary to sell the asset;

"**non-performing financial lease**" means a facility that is classified as sub-standard, doubtful, or loss in accordance with these Regulations;

"**re-negotiated financial lease**" means a facility which has been refinanced, rescheduled, rolled over or otherwise modified because of weaknesses in the borrower's financial position or nonrepayment of the outstanding facility according to the original terms;

"**standard asset**" means any asset that can be easily resold;

"**specific asset**" means any asset that is difficult to resell.

3. Application

(1) Unless otherwise provided, these Regulations shall apply to financial leasing institutions licenced by the Central Bank pursuant to the Act, to engage in financial leasing business.

(2) Banks granted approval to engage in financial leasing business pursuant to section 36 of the Act as part of its banking business licence shall adhere to the Financial Institutions (Credit Classification and Provisioning) Regulations, 2010, except for its financial leasing operations, for which it shall abide to the Regulations hereunder.

4. Requirements for lease classification process

(1) For purposes of lease classification, the financial leasing institution's portfolio shall be reviewed on a monthly basis in accordance with these regulations and the policy and guidelines of the financial leasing institution.

(2) This lease portfolio review shall be made by a person who is independent from the lease origination function of the financial leasing institution.

(3) While small homogenous financial leases may be reviewed on a group-wise basis, the following financial leases must be reviewed on an individual basis—

(a) large exposures;

(b) lease concentrations;

(c) non-performing financial leases;

(d) financial leases that have been charged off; and

(e) a sample of financial leases from each group within the portfolio.

(4) The remainder of the financial leasing institution's lease portfolio may be divided into groups of leases with similar credit risk characteristics (such as type of facility) for review on a collective basis.

(5) Where a financial leasing institution has more than one financial lease extended to a single customer or group of closely-related customers and one such facility is non-performing, the financial leasing institution shall review all other facilities to that customer or group of closely-related customers for the purposes of classification and shall document such review.

(6) The financial leasing institution shall, based on the financial lease portfolio review, assign each facility to classification categories on the basis of credit risk as per regulation 5.

(7) A financial leasing institution may develop internal risk-grading system to indicate various levels of risk exposure in financial leases which shall be reconciled to the five classification categories under these Regulations for the purposes of reporting to the Central Bank.

(8) If a financial leasing institution, within the period of two monthly financial lease portfolio review, comes to know about any material deterioration in the quality of an individual facility or group of facilities within its portfolio, the financial lease shall promptly be assigned to the classification category that accurately reflects its new status.

5. Lease classification categories

A financial leasing institution's facilities are to be classified on the basis of credit risk into the five categories as provided under Schedule 1 to these regulations.

6. Re-negotiated financial leases

(1) A non-performing financial lease, once re-negotiated, shall be classified, as a sub-standard asset, or continue to remain in the same category in which it was, prior to its re-negotiation.

(2) The classification of a facility which has been re-negotiated to modify one or more of its terms shall not be improved unless repayment of principal and interest, in accordance with the new payment schedule under the financial lease, has been made for six installment periods or for a period of not less than six months, whichever period is greater.

(3) On the expiry of the period referenced in subregulation (2), the re-negotiated may be classified no more favourably than "special mention" until repayment of principal and interest has been made for six additional installment periods or for an additional period of not less than six months, whichever period is greater.

(4) Subject to subregulations (2) and (3), a re-negotiated financial lease may be classified in accordance with regulation 5.

7. Minimum provisioning requirements

(1) Any impairment to the value of a financial lease or group of financial leases shall, at least monthly and based on the financial leasing review and classification process, be recognised by reducing the book value of the financial lease and charging the income statement in the period in which the impairment occurred by using the—

(a) general provisions for bad and doubtful account for facilities classified as pass; or

(b) specific provisions for bad and doubtful account for facilities classified as special mention, sub-standard, doubtful or loss.

(2) The financial leasing institution shall determine the amount of provisions for bad and doubtful facilities using the Standard Percentages Method by applying the minimum percentages to the sum of the gross financial lease balance for general provisions and the sum of the net financial lease balance for specific provisions in each classification category as follows—

General Provisions	**Provisioning rules**	**Provision Classification**
	1%	Pass
	0% for facilities extended to Seychelles Government	Pass
	5%	Special Mention
	25%	Sub-standard
Specific Provisions	50%	Doubtful
	100%	Loss

(3) The value of the asset shall be determined on the unamortised amount for each of the following asset categories—

Asset category	Amortisation (for provisioning purposes)
Standard Asset	Shall be amortised fully over five years.
Specific Asset	Shall be amortised fully over three years: 40 percent in years one and two, and 20 percent in the third year.

(4) The Central Bank may direct a financial leasing institution to increase its levels of provisions where reliable information indicates that losses are likely to be more than the minimum amounts as specified under section 7(2).

8. Reconciliation with International Accounting Standard 39

(1) A financial leasing institution shall apply provisions of this regulation in reporting under the International Financial Reporting Standard.

(2) The financial leasing institution shall calculate its provisions in accordance with the requirements of—

(a) the International Accounting Standard 39; and

(b) these Regulations.

(3) If the provisions computed under the International Accounting Standard 39 are less than required under these Regulations, the financial leasing institution shall assign the difference to a nondistributable equity reserve created through an appropriation of reserve.

(4) Where the International Accounting Standard 39 requires a higher provisioning than prescribed by these regulations, the financial leasing institution shall provide for the greater amount.

9. Charge off

(1) A financial lease which is uncollectible and that continuation as a recoverable advance is no longer warranted shall be charged off.

(2) A financial lease or any portion thereof shall be charged off within 12 months of being classified as "loss".

(3) A charge-off shall be made against the specific financial lease loss reserve account and if the amount of the financial lease to be charged off exceeds the balance of the specific financial lease loss reserves account additional reserves shall be established to cover the shortfall through charges to income or through transfers from the general financial lease loss reserves account.

(4) The recovery on a financial lease previously charged off shall be recorded as income in the financial period during which such recovery occurs.

10. Income recognition requirements

(1) A non-performing financial lease shall be placed on a non-accrual basis, and interest due but uncollected shall not be accrued as income but instead be shown as interest in suspense.

(2) Notwithstanding subregulation (1), interest on a financial lease to the Government of Seychelles and a facility guaranteed by the Government of Seychelles which becomes non-performing, shall continue to accrue interest up to the limit of the guarantee.

(3) Any interest on any non-performing financial lease previously accrued as income but uncollected shall be reversed and credited into interest in suspense account until paid in cash by the lessee.

11. Repossession of asset in lieu of repayment of the financial lease

(1) Where a financial leasing institution repossesses an asset in lieu of repayment of a facility, the book value of the repossessed asset shall be the unpaid balance of the financial lease or the net realisable value of the asset, whichever is lower.

(2) Where the net realisable value of the asset is less than the book value of the financial lease, the difference shall be charged off through the provisions for bad and doubtful account when the asset is added to the books of account of the financial leasing institution.

12. Management information system and reporting requirements

(1) When a lease is classified doubtful or loss, the financial leasing institution shall obtain a current and reliable written indication of the net realisable value of the asset and obtain regular updates thereafter.

(2) Every financial leasing institution shall maintain a management information system adequate to identify and track—

(a) the features of individual financial lease, groups of leases, and the financial lease portfolio (including types of facilities within the portfolio);

(b) the evolving condition of a facility such as—

(i) regularity of payments;

(ii) the financial condition of the obligor;

(iii) the status and value of collateral; and

(iv) all other attributes of the facility;

(c) the characteristics of obligors and groups of related customers; and

(d) sectors in which the financial leasing institution has credit exposures.

(3) Every financial leasing institution shall maintain, and make available to an authorised examiner of the Central Bank, adequate written records and reports in support of—

(a) financial lease review and classification functions;

(b) evaluation and calculation of potential loss exposure in the financial lease portfolio;

(c) the entries made to the provisions for bad and doubtful accounts; and

(d) actions taken to ensure that the amount of the provisions for bad and doubtful accounts is adequate to cover the identified potential loss exposure in the financial lease portfolio.

(4) The Board of Directors shall require regular written reports showing that—

(a) the lending activities of the financial leasing institution are in compliance with the financial lease policies approved by the Board of Directors, with the Act, and these regulations;

(b) the risks and potential loss exposure in the financial leasing institution's financial lease portfolio have been identified;

(c) the problem or deteriorating facilities have been identified, classified, placed on nonaccrual status, and the action taken by management to reduce the risk of loss on such facilities;

(d) the amount of accrued, but uncollected interest on the books of account of the financial leasing institution is appropriate;

(e) adequate provisions for potential financial lease losses have been made to the proper account; and

(f) losses have been identified and written off.

(5) Every financial leasing institution shall, within 15 days after the end of each month, submit to the Central Bank reports in such form provided by Central Bank showing an analysis and classification of its leases, provisions for bad and doubtful accounts, and interest in suspense accounts.

Schedule 1 (Regulation 5)

Financial lease classification criteria

	General Provisions	Specific Provisions			
Conditions	Pass (must meet all following conditions)	Special Mention (meets one or more of the following criteria)	Sub-standard (has one or more of the following deficiencies)	Doubtful (has one or more of the following deficiencies)	Loss (has one or more of the following deficiencies)
State of the facility and expectation of future of the facility	Facility is performing and expected to continue to perform in accordance with the financial lease agreement.	Despite the facilities may be currently performing and/or secured by unimpaired collateral, certain factors are known which could, in the future, impinge on the performance of the facility or impair the value of the asset or eligible collateral (if any) including deteriorating general economic or sector conditions and adverse trends in the obligor's financial condition.	Primary source of repayment of the facility is insufficient to service the facility and the financial leasing institution is relying on one or more secondary sources of repayment (such as sale of fixed assets or restructuring of the facility).	Collection of the facility in full is highly questionable or unlikely.	Facility is regarded as uncollectible such that its continuation on the financial leasing institution's books of account is not warranted.
Past-due period	less than 30 days past-due and despite any fluctuations, can at least service the interest	30 - 89 days past-due or is not in compliance with any other term or condition of the financial lease.	90 - 179 days past-due or is not in compliance with any other term or condition of the	180 - 364 days past-due.	365 - days past-due or more.

	applied/ charged.		financial lease agreement.		
Other factors	Sufficient documentation to support the outstanding facility, evidence the financial leasing institution's perfected interest in eligible collateral (if any), or permit the financial leasing institution to properly supervise the financial lease or any additional collateral held (if any). Financial condition of the obligor is sound and expected to remain sound.	Insufficient documentation to support the outstanding facility, evidence the financial leasing institution's perfected interest in eligible collateral (if any), or permit the financial leasing institution to properly supervise the facility or any additional collateral held (if any).	Non-performing financial leases that are totally secured (including 100% of the principal balance and accumulated interest) by cash, Government securities, of Government guarantee meeting the requirements of eligible collateral shall be classified no more adversely than Sub-standard.	Likelihood of loss on the facility; however, the situation could improve due to near-term important and reasonably specific pending factors such as a proposed merger, acquisition, liquidation, capital injection, perfection of liens; additional collateral, or other arrangements.	Facility may have some recovery value; however, the financial leasing institution deems it to be neither sensible nor desirable to postpone removing the facility from its books of account while it pursues long-term recovery efforts.

