

CENTRAL BANK OF IRAQ

Instructions and Actions Issued by the CBI **Regulating Banking Activity in Iraq**

Based on the CBI's functions and in accordance with its law no. 56 of 2004 and Iraqi Banking Law no. 94 of 2004, the CBI's Board of Directors has approved a group of actions and instructions to regulate banking activity within the prudential actions as set forth in the two above mentioned laws to create a strong, sound and safe banking system in Iraq. These instructions and actions are:

1. Granting Licenses for Banks and Non Banking Financial Institutions.
2. Guidelines on Credits Policies and Classification.
3. Guidelines/Restrictions on Investments
4. Instructions Related to the Capital Adequacy Standard.
5. Instructions on Islamic Banking in Iraq.

Updated January 3, 2007

CENTRAL BANK OF IRAQ

Regulatory Instruction (1)

Granting Licenses for Banks and Non Banking Financial Institutions

Consideration of Requests of Licensing Local and Foreign Banks

1.1 Licenses:

Granting licenses to practice banking activities as set forth in article 27 of the Banking Law No. 94 of 2004, to open a representative (agent) office in Iraq or to establish a non-banking financial entity that performs part of the banking activities, such as:

- Financial transfer and exchange companies.
- Financial investment companies.
- Lending companies or lending funds.

1.2 License Limitations:

- 1.2.1** Establishing a local bank, foreign bank branch or subsidiary banking company or opening an agent office of a foreign bank or a non-banking financial company require licenses of the (CBI).
- 1.2.2** The license is to be given for unlimited period and it is non transferable.
- 1.2.3** License defines rules and provisions under which it was issued. These provisions are considered as permanent, unless revised by the (CBI) later on.
- 1.2.4** Licenses are issued exclusively for companies established in the form of a juridical person according to Iraqi legislation, and registered according to it.
- 1.2.5** Licensing foreign bank branches subject to comprehensive supervision and uniform fundamentals made by the regulatory authority of the country where the foreign bank's headquarters locate.
- 1.2.6** License applications shall be submitted in writing with the required documents and data attached.

Section (1)

Opening a Local Bank in Iraq

Licensing Local Banks

This is a 2 stage process:

1) Stage 1:

The CBI board of directors may issue an initial approval to apply for a banking license after reviewing the documents listed below. These documents have to be attached to the license application:

- Draft of foundation contract and by-laws.
- Business plan proving that capital is no less than (ID 50 billion).
- Trade name, including bank's name in both Arabic and English.
- A list of founders including name, nationality, vocation, domicile, address, amount of contribution shares (number of shares), ratio of share to total capital, and names of at least two persons who can be references to confirm its financial soundness position, plus taking notice of the following:
 - If there is a foreign bank whose share in the local bank is (10%), or more, of the local bank's total capital and if this foreign bank is subject to comprehensive consolidated supervision of a regulatory authority in the country where the foreign bank's headquarters is located.
 - At least two of the founders should have banking expertise.
- If one of the founders is a company, it must submit the following documents:
 - Balance sheet and profit and loss statements for the last 3 years, audited by an authorized auditor (or whatever periods are available if the operating period is less than 3 years since foundation).
 - Names of parties that have eligible holding (10% or more of the company's capital).
- The organizational structure of the bank plus number of employees expected to be working in the first stage.
- A document that proves payment of application fees.

The above-mentioned documents will be reviewed by the CBI. The applicant is to be informed (within two months from date of submitting the application) whether the application is satisfactory. The CBI may extend this period, provided that the applicant is informed in writing of the reasons for the delay before the above-mentioned two month period expires. If the application is satisfactory, the CBI will give its initial approval for licensing within an additional two month time period. The initial approval is valid for one year.

2) Stage 2

After the approval is obtained in Stage 1, the company is to submit a written request to obtain a license for practicing banking activity, after being founded and registered according to regulations under Company Law. No less than (ID 25 billion) to be paid, which represents (50%) of the minimum capital defined by legislation, plus a pledge of paying the rest of the capital within 18 months from date of licensing. The following documents are to be attached to this request:

- A certified copy of the company foundation contract.
- A certified copy of the company foundation certification.
- A certified copy of the company by-laws.
- Filing attached formats:
 - Form (1) of the Bank.
 - Form (2) of the Founders.
 - Form (3) of the Board of Directors Members.
 - Form (4) of the General Manager.
- Minutes of the company general assembly establishing meeting, that contain names of elected board members, General Manager, external auditor and audit review committee; as approved by the CBI previously.

The CBI is to verify that the application meets all the stipulations within 2 months of the date of submission. The CBI may extend this period, provided that the applicant is informed in writing of the reasons for the delay before the above-mentioned 2 month period expires. After the CBI has issued a letter saying the application is satisfactory, the CBI has an additional 6 months to either accept or reject the application.

Once this final decision is made, the CBI is to:

- Inform the applicant of the decision of licensing and to publish the decision in the Iraqi Gazette or in public bulletins of wide circulation.
- Upon issuance of the license, the bank is added to the CBI's Record of Banks and thus all competent CBI laws, regulations and instructions are applied to the new bank.

Section (2)

Opening a Foreign Bank Subsidiary or Branch Office in Iraq

1) **Licensing Procedures:**

- A. To establish a foreign bank subsidiary or branch in Iraq, a CBI license should be obtained.
- B. Licenses and permissions can only be given to foreign banks subject to comprehensive consolidated supervision of a regulatory authority in the country where the foreign bank's headquarters is located.
- C. Request for obtaining license is to be submitted, in writing, to the CBI; plus information, statements and documents required under Appendices (1 & 2).
- D. Within 2 months of the date of submission, the applicant will be informed whether the application is satisfactory. The above-mentioned period may be extended, provided that the applicant is informed of the reasons for delay before the deadline expires.
- E. The CBI has an additional 6 months from the date the applicant is notified that the application is satisfactory, to either approve or reject the request and send its written decision to the applicant.
- F. The CBI informs the applicant with its decision of licensing and publishes it in the Iraqi Gazette or in public bulletins of wide circulation.
- G. Upon issuance of the license, the bank is added to the CBI's Record of Banks and thus all competent CBI laws, regulations and instructions are applied to the new bank.

2) Licensing Documentation:

The CBI will approve the application submitted by a foreign bank to obtain a license to open a branch or establish a banking subsidiary, once it is satisfied with the following documents furnished:

- All submitted information and documents attached to the application in accordance with Section 2 Appendices (1 & 2).
- Financial position, history and reputation of the applicant.
- Documentation confirming that the entire capital of ID 50 billion or more, has been paid to the banking subsidiary or bank branch and all procedures under applicable Iraqi laws to establish the entity have been completed.
- Resources allocated by the foreign bank (which intends to practice banking activity in Iraq) should be adequate to cover its liabilities.
- The existence of an actual and permanent address in Iraq.
- Official approval letter issued by the foreign supervising authority in the parent country (Central (National) Bank or any other authorized power) to establish the subsidiary or open a branch in Iraq.
- Official letter confirming that the foreign bank's supervisor in its parent country is ready to perform comprehensive consolidated supervision on the foreign bank including its branch or subsidiary in Iraq.

Section (3)

Opening a Foreign Bank Representative Office in Iraq

Licensing Procedures

- 1) Representative office activities are limited to providing information and making contacts. They do not practice banking or other same activities nor accept deposits or other funds repayable to the public.
- 2) The foreign bank is to submit an application to the CBI to open one or more representative offices in Iraq.
- 3) The applicant bank must be authorized to perform banking activities in its foundation country.
- 4) The CBI will approve the application to open a Representative office of a foreign bank in Iraq after it is satisfied with the following items:
 - All documents, information and statements required in appendices (1& 2).
 - The location of the proposed office and an actual address in Iraq.
 - Documentation confirming that the application submission fees have been paid.
- 5) The CBI will inform the applicant, within 2 months, whether the application is satisfactory.
- 6) The CBI has an additional 2 months from the date of informing the foreign bank the application is satisfactory, to make its decision and inform the applicant on whether the license is approved or rejected.

Section (4)

Allowing a Local Bank to Open a Branch, Banking Subsidiary, or Representative Office Abroad

The local bank will submit a written application to the CBI to establish a branch, banking subsidiary (company established under provisions of the host country, provided that the bank holds over (50%) of the shares) or representative office abroad. The following documentation must be attached to the application:

- 1) Balance sheet and profit and loss statements examined by an auditor for the last operation year.
- 2) Capital of the applicant bank.
- 3) Business Plan of the branch, subsidiary or representative office.
- 4) The location of the branch, subsidiary or representative office.
- 5) Name, nationality, domicile and professional expertise of the manager of the branch, subsidiary or representative office.
- 6) Documentation confirming that the fees for the application submission have been paid.
- 7) Information on the regulatory and supervisory system of the host country, including any laws of the country that may hinder the CBI's ability to obtain information it considers necessary to perform consolidated supervision on the bank.
- 8) The CBI will inform the applicant within two months if the application is satisfactory. This period may be extended for no more than 6 months, providing the reason for the delays is explained. After issuing a letter from the CBI, explaining that the application is satisfactory, the CBI has an additional 2 months to either approve or reject the application.
- 9) The local bank will promptly inform the CBI of any errors or lack of submitted information during the review period and will provide the CBI with the corrected information.
- 10) In case of rejection of the application, the CBI will inform the local bank the reasons for the rejection. In addition, the local bank cannot recover any of the fees paid for submitting the application.

Section (5)

Licensing of Financial Investment Companies, Lending Companies and Funds, and Financial Transfer and Exchange Companies (Non-Banking Financial Institutions)

This is a 2 stage process:

1) Stage 1 – Establishing the Company

An application for establishing a Non-Banking Financial Institution is to be submitted to the CBI and must include the following documents:

- Establishment contract draft.
- Business Plan.
- Trade name in both Arabic and English.
- A list of founders' names, nationalities, vocations, addresses, amount of shares owned (number of shares), percentage of each founder's shares to total capital. Two of the founders must have financial expertise.
- If case one of the founders is a company, it should submit the following documents:
 - Balance sheet and profit and loss statements for the last 3 years, examined by an authorized auditor.
 - Names of parties that have eligible holding (10% or more of the company's capital).
- The CBI will inform the applicant, within 2 months of submission, whether the application is satisfactory and submits the matter to the CBI Board of Directors. If approved, the company will be given initial approval to finish the establishment procedures. This initial approval is good for 6 months but can be extended for a further 6 months.

2) Stage 2 – Obtaining the Final License

After obtaining the initial approval from the CBI, the company submits a final written request to obtain a license to start performing its business practice after being established and legally registered. The following documents are to be attached to this request:

- A certified copy of the company establishment contract.
- A certified copy of the company establishment certification.
- A certified copy of the company by-laws.
- Minutes of the company general assembly establishment meeting, which contain names of the members of the Board of Directors and General Manager. The entire matter is then submitted to the CBI board of directors, for final approval or rejection of the license.
- Within 2 months of the date of submission of acceptable documents, the CBI will inform the applicant of the CBI Board's decision to either approve or reject the requested financial activity.
- Once the license is issued, the company is added to the record of Non-Banking Financial Companies and Institutions. Thus, all applicable Iraqi laws, regulations and instructions issued by the CBI will be applied to it.

Section (2)

Appendix 1

Opening a Foreign Bank Subsidiary or Branch Office in Iraq

1) General Information on Applicant

- Name:
- Legal form of ownership:
- Total assets:
- Total capital / declared , subscribed and paid-up capital:
- Number of employees:
- Home Office location:
- Foreign supervision authority to which the bank is subject:
- Classification degree of a recognized international agency:
- Applicant should have practiced banking activity for no less than 3 years:
- Applicant should be subject to comprehensive consolidated supervision by a banking supervision authority in its home country:

2) International Presence:

- Number of branches / bureaus world wide:
- Number of branches / bureaus in the Middle East:
- Brief summary of the bank's expertise and presence:
 - in the Middle East:
 - in developing and transitional economies:

3) Proposed structure to operate in Iraq

- Branch or Subsidiary:

Section (2)

Appendix 2

Opening a Foreign Bank Subsidiary or Branch Office in Iraq

Documents and information to be attached to the application

- 1) Business Plan with three years of estimates that contains:
 - **1-1:** Number of proposed branches to support the business plan in Iraq.
 - **1-2:** Banking services that will be proposed and economic sectors targeted by these services.
 - **1-3:** Estimate of the source and uses of funds, economic and financial analyses expected for operation of the branch or branches.
 - **1-4:** Risk Management Policy, Credit Management Policy, and Credit Policies and procedures that will be followed.
 - **1-5:** Organizational structure, information on key officials and their responsibilities, information that checks have been completed to insure that no key official has business or project which will cause a conflict of interest.
 - **1-6:** A summary of the information technology plan to support the strategy in Iraq.
 - **1-7:** A summary of Iraqi employee percentages and their training plan.
 - **1-8:** A list of key owners of the foreign or parent bank.
- 2) Parent company foundation license certified by an authorized official party in the parent country, that shows the company's ownership structure, the applicable law governing it and the founding contract or charter.
- 3) Appointment order of the branch manager, issued by an authorized party, including name, domicile, nationality and vocation or career; appointed as the top employee of the bank in Iraq and responsible for running the bank's business, mentioning his/her educational qualifications and expertise, and providing that his/her banking expertise is not less than 3 years.
- 4) A statement on financial fines or other penalties that can be imposed by the foreign supervisory authority on the applicant bank in case of violations of rules.
- 5) Provisions imposed by the parent company to fight money laundering, terrorism and other illegal activities.
- 6) A statement on the parent bank's implementation of the 40 recommendations contained in the Anti Money Laundering World Agreement.
- 7) Naming the contact party of the supervisory authority in the applicant's parent country.

- 8) A letter from the supervisory authority on the applicant's position.
- 9) A letter from the supervisory authority, assuring that the performance of the applicant is subject to its actual supervision.
- 10) Audited copies of financial statements of the last 3 working years.
- 11) A letter from a recognized auditor, in which he / she shows his / her will to take over external auditing.
- 12) Informing on any real change in the financial position since publishing the last financial statement.
- 13) A pledge in which the applicant pledges commitment to regulations of the foreign supervisory authority and for the regulations issued by the CBI.
- 14) A pledge in which the applicant assures the CBI of its commitment to provide information required by the CBI, concerning its compliance with Iraqi legislation.
- 15) Informing on any restrictions in the parent country that may restrict the applicant's ability to comply with CBI requests for information.
- 16) A certified copy of the Banking Practice License of the applicant's bank.
- 17) If the applicant company belongs to a foreign bank or a foreign bank holding company, it should submit a statement mentioning that the supervisory authority of the parent country responsible for banking supervision of the parent company has no objection to the submitted application and will provide consolidated uniform supervision of the applicant company.
- 18) Any other statement considered as necessary by the CBI.

Section (3)

Appendix 1

Opening Foreign Bank Representative Office in Iraq

Documents and Information to be Attached to the Application

- 1) A certified copy of the foundation certification of the applicant company (foreign bank), plus its by-laws and head office's address.
- 2) Information on the applicant bank's declared, subscribed and paid-up capital.
- 3) Appointment order of the office manager, including name, domicile, nationality, appointed as the top employee of the office in Iraq and responsible for performing the office's functions; detailed information on his/her qualifications and professional expertise and listing three references to be contacted as necessary.
- 4) A list of the applicant bank's major shareholders and ultimate beneficiaries from shares, that includes name, address and related share holdings, plus a copy of shareholders' register in case of registered shares.
- 5) Completion and duly signing Appendix (2), Section 3 by the office manager.
- 6) Copies of the last 3 audited balance sheets and profit and loss statements of the applicant company, plus the latest report of both the external auditor and the board of directors.
- 7) A list of the applicant bank's branches and the representative office locations to be opened in Iraq.
- 8) A statement which states that foreign supervision authority, responsible for banks' supervision in the applicant's country, has no objection on establishing the office and that it practices comprehensive uniform supervision on the applicant bank.
- 9) The foreign bank should urgently inform the CBI at having any unreal or inaccurate information attached to the application before deciding about it and it should provide the corrected complementary information to the CBI.
- 10) A pledge of the applicant to comply with Iraqi legislation and CBI regulations and instructions.

Section (3)
Appendix 2

Opening Foreign Bank Representative Office in Iraq

Documents and Information to be Attached to the Application in Regards to the Proposed Office Manager

1. Full Name:
2. Date of birth:
3. Nationality:
4. Residence address in Iraq:
5. Last vocation:
6. Number of shares owned in the applicant bank:
7. Have you ever been convicted by a criminal court with a verdict crime or you could have had a sentence of one year or more without having the choice of paying fine?
8. Have you been declared as bankrupt by a juridical body during the last 7 years?
9. Did any competent authority declare you ineligible or stop you from performing any vocation or career practice?
10. Has any juridical body ever made a declaration or any competent body ever made an order of your non-fitness for running a company?

CENTRAL BANK OF IRAQ

Regulatory Instructions (2)

Credit Policies and Classification

Process of making loans (credit) is considered as one of the most important income generating activities. Therefore, good management of credit risks is significantly important in bank activity performance and in securing a good source of profits to increase capital and shareholders' equity.

Accordingly, each bank needs fundamental principles in place to manage its credit portfolio. This will depend upon the size of the bank and its activities, diversification of its credit portfolio and types of risks to which the portfolio may be exposed.

The credit portfolio's effectiveness, management and course in each bank, whatever its size is, is dependent upon the following issues:

1. Proper determination of the risk types to which the bank will be faced in its lending activities.
2. Proper organization and presentation of this information to top bank management and the Board of Directors.
3. Soundness of corrective procedures taken to mitigate risks.

Good lending standards, a proper loan classification system, proper determination of the risks and corrective actions taken to reduce these risks are the backbone of credit policy. This policy should be in the form of written directions and procedures for granting credit and following up repayment. They are approved by the bank Board of Directors and must be applied by everyone.

Main objectives of credit policy are:

- 1) Granting collectable loans on a sound and safe basis.
- 2) Investment of bank funds profitably for the benefit of shareholders and to protect depositors.
- 3) Serving the legitimate credit needs of the various economic areas, sectors and activities so as to develop them and to stimulate economic activity for the overall development of the Iraqi economy.

Therefore, a written plan that clearly sets out the objectives of the credit portfolio should be developed and put in place. This plan should be reviewed periodically and updated depending upon the requirements of the continuously changing and developing economic and social issues.

The Credit Policy should contain the following basic topics:

1. General financial and economic objectives of lending (such as increasing revenues, meeting and covering part of financial needs of economic activity of the Iraqi society.... etc.).
2. Determination of diversification and objectives of the credit portfolio, regarding volume and type of loans in the credit portfolio (size of loans, length of time to maturity, types of loans: general or specific, overdraft, check and bill discount, loan pricing.... etc.).
3. Specialization in specific types of loans based on sector, geographical, demographical or all together...etc.).
4. The credit portfolio share in the bank's annual financial plan, in comparison to other banking activities and in line with the regulatory instructions issued by the CBI and competent laws.
5. Determination of targeted economic activities, geographical markets the bank intends to enter and the bank's intended share in the target markets.
6. Delegations of Authority for approving loans that includes the lending limits permitted at each level in the bank and the signatures required on each approval.
7. Determination of procedures required for granting level depending on its size and level, from the initial submission of the credit application up to giving approval and disbursing the credit and the documentation required for each type of credit.
8. Procedures for following up on developments in the credit portfolio including payment procedures for each credit separately, review procedures, analysis and re-evaluation of each loan continuously; including communicating and following-up with the borrowers (loan takers) depending on their payment commitment.
9. Classification of the credits and risks, in such a way that helps to define the amount that may cover any unexpected losses in the loans.
10. Information System to manage the credit portfolio, to generate the reports necessary to take appropriate actions on any loans and to assess whether the credit portfolio is meeting the needs and adhering to Bank Credit Policy.

Credit Classification and Obligatory Needs:

Each bank's internal policies should define the volume of credit exposures, the minimum and maximum percentages, risk management standards, investment policies and other precautionary policies and procedures to appropriately maintain its assets and off- balance-sheet items.

Precautionary Requirements:

For supervising and controlling the credit portfolio, banks should continuously reviews, evaluate and classify granted credits according to types, depending on the following:

A. Preferred Credit:

Contains credits secured by collateral that is fast and easy to liquidate that will cover principal and accrued interest. Such collateral would be: valuable metals (gold and silver), fixed deposits and saving accounts, governmental securities (where the value of the securities is at least twice more than the principal and accrued interest), guarantees offered by the government and guarantees offered by OECD countries (Organization of Economic Cooperation and Development). These credits are not subject to any provision for loan loss until its due date.

B. Good (standard) Credit:

Contains credits completely supported by the payment ability and financial borrower's ability to pay. The loans are to be covered by appropriate signed guarantees and must be current and performing according to their terms. Loans should not be renewed or rescheduled without payment. Current account facilities (debit) "overdraft accounts" should not exceed the approved credit limit.. It also contains existing custody credit which is recent, valid, not canceled and unpaid minus cash collaterals pledged against it.

C. Medium Credit:

Contains credit which is considered a potential problem because of a customer's weak financial position and which requires management's attention. If left unattended, further deterioration in the repayment potential is expected. It includes all types of granted credit which is 90 days or less past due.

D. Sub Standard Credit:

This category contains credits which are past-due for principal and/or interest payments. Payment of the principal is not protected sufficiently by the borrower's ability to pay based on the borrower's financial position and where losses are expected if management does not take appropriate action. It contains all types of unpaid credits which are past due for 90 days or more but less than 180 days. This category also includes: those credits which have not had payment of interest and principal installments on due dates; those borrowers who have stopped paying on debit current accounts (overdrafts) where the entire credit limit is used and interest has not been paid for 3 months; those borrowers who have not used the entire credit limit but did not pay interest or any other payment for 6 months; and any credit which has been extended or re-scheduled one time.

E. Bad (doubtful) Credit:

Contains loans which display the same attributes as Sub-Standard Credit but in addition the likelihood of complete collection is doubtful and therefore a loss is highly probable. It contains all types of credits which are 180 days or more but less than 365 days past due and contains all credits that have been extended or re-scheduled for two times.

F. Loss Credit:

This category contains all credits which, despite the potential for collection in the future, is uncollectible now. It contains all types of granted credit which is one year or more past due.

Reserve Ratio:

A bank will determine appropriate reserves to be allocated for the losses it expects in its lending portfolio based on the classifications mentioned under the Credit Classification section above, as follows:

- | | |
|---------------------------|---|
| a) Preferred Credit | no allocation |
| b) Good (Standard) Credit | allocation: 2% of total Good Credit. |
| c) Medium Credit | allocation: 10% of total Medium Credit. |
| d) Sub Standard Credit | allocation: 25% of Total Sub-Standard Credit. |
| e) Bad (Doubtful) Credit | allocation: 50% of Total Bad Credit. |
| f) Loss Credit | allocation: 100% of Total Loss credit. |

Interim Rules:

A bank licensed after validity date of these instructions must immediately comply with the requirements mentioned herein. As to banks licensed before these instructions' validity date, classification and allocation of credit loss revenue will be handled by instructions to be issued by this Bank

Large Credit Exposures :

No bank shall grant credit to a natural or legal person if:

- a. The total aggregate outstanding principal amount of all credits to that person exceeds the equivalent of (10%) of the bank's unimpaired capital and reserves without obtaining prior approval of the CBI, provided that the aggregate outstanding principal amount of the credit given to that person does not exceed the equivalent of (15%) of the bank's unimpaired capital and reserve.
- b. The total aggregate principal amount of all the bank's major credit exposures pursuant to sub-paragraph (a), would exceed the equivalent of (400%) of the bank's unimpaired capital and reserves; provided that total (cash and contractual) credits given by the bank, including major credit exposures guaranteed by the government (i.e. the MOF – Ministry of Finance, its bodies and institutions authorized by it and provinces' councils) and credit completely guaranteed by deposits in a separate account at the bank, including all credits guaranteed by collateral of fast and easy liquidation; shall not exceed (70%) of the bank's total deposits on the calculation day.

Credits Given to Relatives and Bank Top Employees

A bank may give credit to a related person or senior bank official provided that the bank's Board of Directors has issued written approval of the credit and its terms, and:

- a) Credit is completely guaranteed by a corporeal collateral whose value is one third over total amount of given credit plus its interests.
- b) Total credit, given by the bank or / and its subsidiaries to that person, does not exceed (5%) of sound capital and sound reserves.
- c) Total of due credits given to all relatives does not exceed (15%) of the bank's sound capital and sound reserves.
- d) The given credit's provisions and rules are not less favorable for the bank than those offered by the bank to the public, depending on the usual custom at giving credit.

- II. A bank may give credit to a relative or senior bank official on the condition of obtaining written approval of the Board of Directors on the credit and its provisions, and provided that:
- a) The credit is guaranteed by an acceptable guarantee. .
 - b) Total credit, given by the bank or one of its subsidiaries, does not exceed (50%) of that person's annual compensation.
 - c) Total ue credits given to all relatives does not exceed (10%) of the sound capital and sound reserves.
 - d) The given credit's provisions and rules are not less favorable for the bank than those offered by the bank to the public, depending on the usual custom at giving credit.

Foreign Currency Disclosures:

The above-mentioned paragraphs are applied to this, concerning major disclosures of all paragraphs after re-evaluating foreign currency with its Iraqi currency equivalent according to the rates of auction or (the Bulletin) issued by the CBI on the day of giving the credit and for all rates defined for the currency; including the (70%) ratio of total credit to deposits.

CENTRAL BANK OF IRAQ

Regulatory Instructions (3)

Investment Limitations

A bank's capital and its use is one of the most important indicators of the current financial strength of the bank and its potential for continued operation and development. Banks usually maintain an appropriate level of capital to be able to sustain future growth and development, to provide more banking operations and services to its customers, and to be able to compete and realize profits. The CBI has determined minimum capital standards as defined in Article 14/1 of the Banking Law No. 24 of 2004. To continue providing required potentials at banks and provide most extended services, the CBI; confirms the following in accordance with the Banking Law:

- 1) A bank should not, without prior written approval of the CBI, invest in stocks, shares or equity linked bonds related for the purpose of trading in any project in an amount over (20%) of the bank's unimpaired capital and reserves.
- 2) If any stocks, shares, or equity-linked bonds transferred to the bank in the course of its banking operations would cause the bank's holdings to exceed the limit of 20%, the bank shall dispose of such increasing as soon as practicable and within two years as of the date of their acquisition without incurring a loss. The last period can be extended for an additional 1 year with the approval of the CBI.
- 3) A bank should not own any real estate that is not used in its banking operations or is housing for its employees and workers.
- 4) The bank may lease any excess portion of real estate held for the conduct of its operations, provided it obtains the CBI's prior approval and the leased area does not exceed 50% of the total building area occupied by the bank.
- 5) A bank shall dispose of any real estate transferred to it in the course of its banking operations by its granting loans that were secured by real estate as soon as practicable within two years of the acquiring date. This period may be extended for two additional periods of up to two years each by approval of the CBI. Such real estate shall be sold through an auction based on the required legal actions and it must be announced in at least two public newspapers of wide circulation. If the selling amount exceeds the amount the bank was owed, the bank will keep the amount it is owed and transfer the rest to the client's or his representative's account. In case the amount is not adequate to cover the amount owed the bank, the bank can continue collection efforts against the borrower to collect the rest of the debt.

- 6) A bank is prohibited from acquiring a participation not for trading purposes in another bank, financial institution or any other company through purchase, subscription or debt repayment unless:
 - a. CBI's prior written approval has been obtained.
 - b. Reduce the participation from the bank's unimpaired capital and reserve.
 - c. Maintain the capital minimum as set forth in the law, regulation and instructions issued by the CBI.
 - d. If the transferred shares were result of debt repayment, the bank shall sell the shares as soon as practicable within two years of acquiring them unless the CBI grants approval to retain the shares.

CENTRAL BANK OF IRAQ

Regulatory Instruction (4)

Capital Adequacy

Capital adequacy is a bank's ability to meet its financial commitments timely by what it has in cash on hand, assets equal to cash or assets quickly and easily convertible to cash without loss. This requires a bank to properly monitor all cash inflows and outflows, forecast such flows for coming periods, work on providing sufficient cash and liquid assets to cover unexpected events that may lead to more cash outflows than cash inflows or find alternative sources of such cash like taking loans.

Each bank has to maintain at all times no less than (12%) of its unimpaired capital and reserves to its total risk weighted assets , according to the following equation:

$$\text{Principal Capital} + \text{Supporting capital}$$

$$\text{Risk Weighted Assets on Balance Sheet} + \text{Risk Weighted Assets off Balance Sheet}$$

Principal capital, or the so-called **Tier 1 Capital**, consists of:

1. Net paid in capital.
2. Additional reserves generated from issuing stocks (premium and others).
3. Reserves resulted from profits realized from the previous years.
4. Undistributed profits realized from the previous years.

The following amounts should not be part of this capital:

1. Amounts generated from re-evaluation of fixed assets that are registered as additions to capital.
2. Amounts related to the intangible assets (such as bank goodwill),

Supporting capital, or the so-called **Tier 2 Capital**, consists of:

1. Profit (loss) realized in the current year.
2. Objective money (money related to implementing specific business during the year and it was not paid).
3. General reserves restricted to (1.25%) of a bank's total assets probable with risks (loan allocation reserve).
4. Loans and bonds received by the bank, which can be considered as stocks, after obtaining CBI approval.
5. Secondary loans (provided to support the bank), whose period is no less than 5 years and annual discount is (20%) of their value for each year of the remaining 5 years.
6. Reevaluation of reserves provided that supporting capital amount does not exceed (100%) of principal capital value.

Risk Weighted Assets in Balance Sheet

1. Risk Weight of banknote and coins in Iraqi currency and foreign currency evaluated by ID according to USD exchange rate in the CBI auction, related to USD and other foreign currencies, they are converted to USD depending on the daily purchasing rate announced on the website of Federal Reserve Bank, New York on the day of conversion. Then the USD is converted to the ID depending on the exchange rate of the CBI auction, current account at the CBI, Iraq Government treasury bills, Iraq Government bonds and other bonds guaranteed by Iraq Government, cash facilities guaranteed by cash deposits (100%), cash facilities guaranteed by the Government (the MOF- Ministry of Finance) and same, is **(0%)**.
2. Risk Weight of stocks subject to circulation by their nominal value at issuance, current accounts and deposits at bank of evaluation (A) and upwards, evaluated by a recognized international organization and same, is **(10%)**.
3. Risk Weight of cash assets at other banks inside Iraq and abroad, such as debit current balances in foreign and Iraqi currencies that do not have an (A) classification by a recognized international organization and cash facilities given to the Public Productive Sector, for less than a year, unguaranteed by the State and same, is **(20%)**.
4. Risk Weight of companies and banks subject to circulation by purchasing time, cash facilities guaranteed for the private sector, cash facilities guaranteed for foreign parties (overseas), cash facilities unguaranteed for the mixed sector and same, is **(50%)**.
5. Risk Weight of unreleased gold, bonds unguaranteed by the Government, unguaranteed cash facilities, net value of fixed assets and same, is **(100%)**.

Risk Weighted Assets Off Balance Sheet

Probable weigh ratios are same as applicable currently.