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**LEGAL NOTICE NO. 111 OF 1999**

**FINANCIAL INSTITUTIONS (RISK-BASED CAPITAL  
REQUIREMENTS) REGULATIONS 1999**

IN EXERCISE OF THE POWERS CONFERRED UPON THE COMMISSIONER OF FINANCIAL INSTITUTIONS BY SECTION 21 OF THE FINANCIAL INSTITUTIONS ACT 1999<sup>1</sup>, THE COMMISSIONER MAKES THE FOLLOWING REGULATIONS-

**PART 1  
PRELIMINARY**

**Citation and commencement**

1. These Regulations may be cited as the Financial Institutions (Risk Based Capital Requirements) Regulations 1999 and shall come into operation on the date of publication in the Gazette.

**Interpretation**

2. In these Regulations, unless the context otherwise requires, words used have the same meanings assigned to them in the principal law.

**Objectives**

3. These Regulations are intended -
- (a) to ensure that each bank maintains an adequate level of capital to protect its depositors and creditors and to promote public confidence; and
  - (b) to prescribe a capital adequacy ratio computed according to the Basle Committee on Banking Supervision which takes into consideration the different levels of credit risk inherent in a bank's balance sheet and off-balance sheet activities.

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### **Application**

4. These Regulations apply to all banks licensed to operate in Lesotho but do not apply to other financial institutions which may be operating in Lesotho.

## **PART II REGULATORY REQUIREMENT**

### **Capital adequacy ratio**

5. (1) A bank shall maintain a capital base of an amount not less than 8% of its weighted risk assets and the Commissioner may vary this percentage from time to time, by notice published in the Gazette.

(2) The basic framework for computing the ratio of a bank's capital base to its weighted risk assets is that adopted by the Basle Committee on Banking Supervision, subject to certain modifications to suit local conditions.

(3) The emphasis of the framework shall be on assessing capital in relation mainly, to credit risk but shall also take into account foreign exchange risk, interest rate risk and other risks as may be necessary.

(4) The ratio shall be computed by using the attached Capital Adequacy Ratio Worksheet set out in Schedule I (along with supporting schedules IA, IB and IC) which shall be submitted to the Central Bank not later than 30 days from the end of each calendar quarter.

(5) A bank which fails to comply with the minimum capital adequacy ratio on the date at which these Regulations come into effect shall within 60 days submit, for approval by the Central Bank, a detailed plan describing the means and specifying the time-table by which the bank shall meet the requirement, and thereafter comply with it.

(6) Quarterly reports of compliance with the approved plan shall then be submitted to the Central Bank using the Capital Adequacy Ratio Worksheet.

### **Constituents of capital**

6. (1) The capital base for the purpose of these Regulations shall consist of Tier I or Core Capital and Tier II or Supplementary Capital.

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(2) Tier I Capital or Core Capital shall not be less than 50% of the total qualifying capital and shall consist of –

- (a) issued and fully paid ordinary shares or common stock and related surplus (share premium) or assigned capital;
- (b) fully paid perpetual non-cumulative preference shares and related surplus; these are preferred shares which –
  - (i) do not have a maturity date;
  - (ii) cannot be redeemed at the option of the shareholder;
  - (iii) give the issuer the legal right to defer or eliminate preferred dividends; and
  - (iv) have no other provisions that will require future redemption of the issue;
- (c) a reserve account as required by the Financial Institutions Act 1999;
- (d) capital reserves excluding asset revaluation reserves;
- (e) general reserves excluding reserves or provisions for identified losses or in respect of an identified deterioration in the value of any asset; and
- (f) retained earnings as stated in the latest audited financial statements.

(3) Tier II Capital or Supplementary Capital shall be limited to 100% of Tier I or Core Capital and shall consist of –

- (a) fixed assets revaluation reserves arising from a prudent revaluation of an immovable property carried out by independent professional appraisers on a basis satisfactory to both the Central Bank and the external auditors;
- (b) securities revaluation reserves which arise from the practice of holding securities in the balance sheet valued at historic cost and the difference between the historic cost and the market value shall be discounted by 55%;

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- (c) undisclosed or hidden reserves accepted by the Central Bank which have the same intrinsic quality as published retained earnings and which represent accumulations of post-tax profits which are not encumbered by any known liability and are not routinely used for absorbing operating losses;
  - (d) General provisions or general reserves for losses on assets, which refer to provisions and reserves not ascribed to specific assets. General provisions or general reserves made for specific assets are not eligible for inclusion in capital. General provisions or general loan loss reserves which qualify for inclusion in Tier II capital do so subject to a limit of 1.25% of weighted-risk assets;
  - (e) hybrid debt capital instruments which refer to a range of instruments that combine the characteristics of equity capital and of debt, such as perpetual cumulative preference shares, long term preference shares, perpetual instruments debt and mandatory convertible debt instruments, which shall meet the following requirements –
    - (i) they should be unsecured, subordinated and fully paid;
    - (ii) they should not be redeemable at the discretion of the holder;
    - (iii) they should be available to absorb losses; and
    - (iv) service obligations attached to the instrument should be deferrable;
  - (f) subordinated term debt includes conventional unsecured subordinated debt capital instruments with a minimum original fixed term to maturity of over 5 years and limited life redeemable preference shares. During the last 5 years to maturity, a cumulative discount (or amortisation) factor of 20% per year shall be applied to reflect the diminishing value of these instruments as a continuing source of strength.
  - (g) Such instruments are subordinated to the claims of both depositors and general creditors and shall be limited to a maximum of 50 % of Tier I capital.
- (4) The following deductions shall be made from core and total qualifying capital –

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- (a) from Tier I or Core Capital –
    - (i) goodwill arising from the acquisition of assets; and
    - (ii) losses made in current year, whether audited or unaudited;
  
  - (b) from total qualifying capital –
    - (i) investments in unconsolidated subsidiaries engaged in banking or financial activities;
    - (ii) other intangible assets, such as, formation and other preliminary expenses;
    - (iii) deficiencies in provision for losses on loans and other assets as may be determined by the Central Bank unless a significant improvement in the quality of the assets is reported by the bank and accepted by the Central Bank;
    - (iv) reported by the bank and accepted by the Central Bank;
    - (v) and
    - (vi) other deductions which may impair, distort or dilute core capital as may be determined by the Central Bank.

#### **Weighted risk assets**

7. (1) Weighted risk assets for the purpose of these Regulations shall consist of On-Balance Sheet Assets and Off-Balance Sheet Accounts.

(2) "On-Balance Sheet Assets" refer to all assets appearing in the balance sheet (statement of assets and liabilities) which shall be multiplied by the applicable risk weights as set as set out in this regulation.

- (3) 0% Risk Weight for the following –
  - (a) local and foreign currencies;
  - (b) balances due from the Central Bank including securities issued by it or loans guaranteed by such securities;
  - (c) treasury bills and other securities issued or guaranteed by Lesotho Government or loans guaranteed by such securities;
  - (d) claims or loans to local governments, statutory boards and other public sector entities fully guaranteed by Lesotho Government;
  - (e) claims on OECD countries and approved regional countries' central banks and central governments and other obligations fully guaranteed by these institutions; and
  - (f) claims fully secured by cash deposited with the reporting bank or by Lesotho Government or Central Bank securities and guarantees.

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- (4) 20% Risk Weight for the following –
- (a) claims on banks and other financial institutions licensed in Lesotho or in OECD countries or approved regional countries and loans guaranteed by such institutions;
  - (b) claims on multilateral institutions and claims guaranteed or collateralised by securities issued by such institutions;
  - (c) balances due from banks and other financial institutions licensed in other countries with residual maturity of 1 year or less; claims on OECD countries and approval regional countries' public sector entities and loans guaranteed by or collateralised by securities issued by such entities; and
  - (d) cash items in the process of collection.
- (5) 50% Risk Weight for real estate housing loans fully secured by mortgages on residential properties which are owner-occupied or rented.
- (6) 100% Risk Weight for the following –
- (a) claims on the private sector;
  - (b) other loans and advances;
  - (c) premises, plant and equipment and other fixed assets;
  - (d) real estate and equity investments;
  - (e) capital instruments issued by other financial institutions (unless deducted from capital); and
  - (f) all other assets.
- (7) (a) OECD countries are as set out in Schedule II;  
(b) Approved Regional Countries refer to SADC countries as set out in Schedule III;  
(c) Multilateral institutions refer to those set out in Schedule IV.
- (8) From the total weighted on-balance sheet accounts, the following amounts shall be deducted –
- (a) specific accumulated provision made for losses on assets (if corresponding assets are presented at gross in the balance sheet);
  - (b) general reserves or provisions for losses on assets disallowed under Tier II capital (if corresponding assets are presented at gross in the balance sheet);

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- (c) deficiencies in provisions for losses on loans and other assets as may be determined by the Central Bank unless a significant improvement in the quality of the assets is reported by the bank and accepted by the Central Bank; and
  - (d) other deductions from core capital or total qualifying capital such as goodwill and other intangible assets, and investments in unconsolidated subsidiaries engaged in banking or financial activities.

(9) "Off-Balance Sheet Accounts" refer to contingent accounts and other off-balance sheet terms which shall be multiplied by the applicable conversion factors to arrive at the credit equivalent amount and which shall then be weighted accordingly to the applicable risk weights used for on-balance sheet accounts –

- (a) 100% Conversion Factor for the following –
  - (i) items which substitute for loans and advances such as financial guarantees, including standby letters of credit and bankers' acceptances;
  - (ii) sale and repurchase agreements with recourse where the credit risk remains with the financial institution; and
  - (iii) forward asset purchases, forward deposits and partly-paid shares and securities representing commitments with certain drawdowns;
- (b) 50% Conversion Factor for the following –
  - (i) certain transaction-related contingent items such as performance bonds, warranties and standby letters of credit related to particular transactions;
  - (ii) note-issuance facilities and revolving underwriting facilities; and
  - (iii) other commitments such as formal standby facilities and credit lines with an original maturity of over one year;
- (c) 20% Conversion Factor for the following –

Short-term self-liquidating trade-related contingencies such as documentary credits collateralised by the underlying shipments;
- (d) 0% Conversion Factor for other commitments such as formal standby facilities and credit lines with an original maturity of up

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to one year or which can be unconditionally cancelled at any time.

**Supervisory actions**

8. The Central Bank may require higher minimum capital adequacy ratio for an individual bank based on, but not limited to, any one or more of the following criteria:

- (a) if the bank is less than 3 years old;
- (b) if the bank has significant exposure to market risk, interest rate risk, liquidity risk, operational risk or other risks arising from non-traditional activities;
- (c) if the bank is growing rapidly, either internally or through acquisitions;
- (d) if the bank may be adversely affected by the activities or financial condition of its parent or holding company, subsidiaries or affiliates; or
- (e) if the bank has severe internal control deficiencies or weak risk management policies and procedures.

**Failure to comply**

9. If a bank fails to comply with this Risk-Based Capital Requirement, the Central Bank may pursue any remedial measures at its disposal, including requiring the bank to take any or all of the following measures –

- (a) desist from engaging in any further foreign exchange activities;
- (b) suspend lending, investment or other credit extension operations;
- (c) restrict declaration and/or payment of dividends or remittance of profits;
- (d) stop establishment of new branches or facilities; or
- (e) prohibit payment of bonuses, salary incentives, management fees or other discretionary compensation to directors or officers.

**S. M. SWARAY**

**GOVERNOR - CENTRAL BANK OF LESOTHO**

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**NOTE**

**1. Act No. 6 of 1999**

**SCHEDULE I  
CAPITAL ADEQUACY RATIO WORKSHEET  
(regulation 5 (4))**

Name of Bank \_\_\_\_\_

For the Quarter Ended \_\_\_\_\_  
Due Date: 30 days from quarter-end

	M000
1. Total risk-weighted on-balance sheets assets (Schedule I-A)	
2. Total risk-weighted off-balance sheet accounts (Schedule I-B)	
3. Total risk-weighted assets before deductions (Add Items 1 and 2)	
4. Less Deductions: Total (Add 4a to 4e)	(     )
(a) Specific accumulated provisions for losses on assets (if assets are stated at gross)	(     )
General reserves and provisions for losses on assets disallowed under Tier II (if assets are stated at gross)	(     )
(c) Deficiencies in provisions for losses	(     )
(d) Other deductions from core and total capital (Add Items d (i) to (d) (iii))	(     )
(i) Goodwill	(     )
(ii) Other intangible assets such as formation and preliminary expenses	(     )
(iii) Investments in unconsolidated financial subsidiaries	(     )
(e) Others (as may be determined by the Central Bank)	(     )
5. Total risk-weighted assets after deductions (Item 3 less Item 4)	(     )
<b>Tier I Capital (Schedule I-C) to total risk-weighted assets after deductions (Items 5)</b>	<b>%</b>
<b>Total Tier I and Tier II qualifying capital (Schedule I-C) to total risk-weighted assets after deductions (Item 5)</b>	<b>%</b>

Submitted by: \_\_\_\_\_  
Name
Signature
Date

SCHEDULE IV - IA

RISK-WEIGHTED ON-BALANCE SHEET ASSETS

Cate- gory	Assets	Value (V) M000	Risk Weight (W)	Weighted Value (V x W) M000
0% Weight	<b>1. Cash</b>			
	(a) Local		0	
	(b) Foreign		0	
	<b>2. Balances Due from Central Bank</b>			
	(a) Deposits		0	
	(b) Securities		0	
	(c) Other claims		0	
	<b>Claims on or securities issued or guaranteed by Lesotho Government</b>			
	(a) Treasury Bills		0	
	(b) Government Securities		0	
	(c) Other claims on government		0	
	<b>Claims on local government, statutory boards and other public sector entities (Guaranteed by Lesotho Government)</b>			
	(a) Local Government Securities		0	
	(b) Other claims on local government		0	
	(c) Securities issued by public sector entities		0	
	(d) Other claims on state-owned entities		0	
	<b>Claims on OECD and approved Regional Countries</b>			
	(a) Central Banks		0	
	(b) Central Government		0	
	(c) Other claims guaranteed by (a) and (b) above		0	
	<b>6. Fully Secured Claims</b>			
	(a) by cash on deposit with the bank itself		0	
	(b) by Lesotho Government or Central Bank securities and guarantees		0	

**Schedule I - A**

Cate- gory	Assets	Value (V) M000	Risk Weight (W)	Weighted Value (Vx W) M000
20% Weight	<b>1. Due from banks and other financial institutions</b>			
	(a) Licensed in Lesotho		20	
	(b) Licensed in OECD countries		20	
	(c) Licensed in approved regional countries		20	
	(d) Licensed in other countries (residual maturity – 1 year or less)		20	
	<b>2. Other claims and loans guaranteed by banks and other Financial institutions</b>			
	(a) Licensed in Lesotho		20	
	(b) Licensed in OECD countries		20	
	<b>3. Claims on or loans guaranteed by multilateral institutions or collateralised by securities issued by such institutions</b>		20	
	<b>4. Claims on or loans guaranteed by OECD and approved regional countries' public sector entities</b>		20	
	<b>5. Cash items in the process of collection</b>		20	
<b>50% weight</b>	<b>Real estate housing loans fully secured by mortgage on residential properties which are owner-occupied or rented</b>		50	
<b>100% weight</b>	<b>1. Loans and advances</b>			
	(a) Commercial		100	
	(b) Personal		100	
	(c) Other		100	
	<b>Due from banks and financial institutions licensed in other countries with residual maturity of over 1 year</b>		100	

SCHEDULE 1 - A

Cate- gory	Assets	Value (V) M000	Risk Weight (W)	Weighted Value (Vx W) M000
	<b>3. Claims on other foreign governments</b>			
	Claims on and obligations guaranteed by other foreign Central Banks		100	
	(a) Claims on and obligations guaranteed by other Central Governments		100	
	<b>4. Fixed Assets</b>			
	(a) Land and buildings		100	
	(b) Furniture and equipment		100	
	(c) Other fixed assets		100	
	<b>5. Investments</b>			
	(a) Investments in other financial institutions		100	
	(b) Investments in securities and equities		100	
	(c) Other investments		100	
	<b>6. Other Assets</b>		100	
	<b>TOTAL RISK-WEIGHTED ON-BALANCE SHEET ASSETS</b>			

**Schedule I - B**  
**RISK WEIGHTED OFF-BALANCE SHEET ACCOUNTS**

<b>Category</b>	<b>Accounts/Counter-Parties</b>	<b>Value (V) M000</b>	<b>Conversion Factor</b>	<b>Risk Weight (W)</b>	<b>Weighted Value (V x W) M000</b>
	<b>1. Lesotho, OECD and Approved Regional countries' government and central banks</b>				
	(a) Financial guarantees, standby letters of credit and bankers' Acceptances (loan substitutes)		1.0	0	
	(b) sale and repurchase agreements with recourse		1.0	0	
	(c) forward asset purchases, forward deposits, partly-paid commitments		1.0	0	
	(d) performance bonds, warranties, standby letters of credit (contingent accounts)		0.5	0	
	(e) note-issuance facilities and revolving underwriting facilities		0.5	0	
	(f) formal standby facilities and credit lines with original maturity of over 1 year		0.5	0	
	(g) documentary credits collateralised by underlying shipments		0.2	0	
	(h) revocable standby facilities and credit lines, cancellable any time		0.0	0	
	(i) formal standby facilities and credit lines with original maturity of up to 1 year		0.0	0	
	(j) others		1.0	0	

**SCHEDULE I - B**

<b>Category</b>	<b>Accounts/Counter-Parties</b>	<b>Value (V) M000</b>	<b>Conversion Factor</b>	<b>Risk Weight (W)</b>	<b>Weighted Value (V x W) M000</b>
	<b>2. Lesotho Public Sector Entities and Local Governments (Guaranteed by Lesotho Government)</b>				
	(a) Financial guarantees, standby letters of credit and bankers' acceptances (loan substitutes)		1.0	0	
	(b) sale and repurchase agreements with recourse		1.0	0	
	(c) forward asset purchases, forward deposits, partly paid commitments		1.0	0	
	(d) performance bonds, warranties, standby letters of credit (contingent accounts)		0.5	0	
	(e) note-issuance facilities and revolving underwriting facilities		0.5	0	
	(f) formal standby facilities and credit lines with original maturity of over 1 year		0.5	0	
	(g) documentary credits collateralised by underlying shipments		0.2	0	
	(h) revocable standby facilities and credit lines, cancellable any time		0.0	0	
	(i) formal standby facilities and credit lines with original maturity of up to 1 year		0.0	0	
	(j) Others		1.0	0	

**SCHEDULE I - B**

<b>Category</b>	<b>Accounts/Counter-Parties</b>	<b>Value (V) M000</b>	<b>Conversion Factor</b>	<b>Risk Weight (W)</b>	<b>Weighted Value (V x W) M000</b>
	<b>3. Domestic Financial Institutions, OECD and Approved Regional countries' Financial Institutions and Public Sector Entities and Multilateral Institutions</b>				
	(a) Financial guarantees, standby letters of credit and bankers' acceptances (loan substitutes)		1.0	20	
	(b) Financial guarantees, standby letters of credit and bankers' acceptances (loan substitutes)		1.0	20	
	(c) Forward asset purchases, forward deposits, partly- paid commitments		1.0	20	
	(d) Performance bonds, warranties, standby letters of credit (contingent accounts)		0.5	20	
	(e) Note-issuance facilities and revolving underwriting facilities		0.5	20	
	(f) Formal standby facilities and credit lines with original maturity of over 1 year		0.5	20	
	(g) documentary credits collateralised by underlying shipments		0.2	20	
	(h) revocable standby facilities and credit lines, cancellable any time		0.0	20	
	(i) formal standby facilities and credit lines with original maturity of up to 1 year		0.0	20	
	(j) others		1.0	20	

**SCHEDULE I - B**

<b>Category</b>	<b>Accounts/Counter-Parties</b>	<b>Value (V) M000</b>	<b>Conversion Factor</b>	<b>Risk Weight (W)</b>	<b>Weighted Value (V x W) M000</b>
	<b>4. Private Sector and Other Institutions</b>				
	(a) Financial guarantees, standby letters of credit and bankers' Acceptances (loan substitutes)		1.0	100	
	(b) sale and repurchase agreements with recourse		1.0	100	
	(c) forward asset purchases, forward deposits, partly-paid commitments		1.0	100	
	(d) performance bonds, warranties, standby letters of credit (contingent accounts)		0.5	100	
	(e) note-issuance facilities and revolving underwriting facilities		0.5	100	
	(f) formal standby facilities and credit lines with original maturity of over 1 year		0.5	100	
	(g) documentary credits collateralised by underlying shipments		0.2	100	
	(h) revocable standby facilities and credit lines, cancellable any time		0.0	100	
	(i) formal standby facilities and credit lines with original maturity of up to 1 year		0.0	100	
	(j) Others		1.0	100	
	<b>Total Risk-Weighted Off-Balance Sheet Accounts</b>				

**SCHEDULE I - C**  
**TOTAL QUALIFYING CAPITAL**

<b>CATEG ORY</b>	<b>CAPITAL ACCOUNTS</b>	<b>M000</b>
<b>Tier I</b>	1. Paid-up ordinary share capital/assigned capital	
	2. Paid-up ordinary share premium	
	3. Undisclosed or hidden reserves	
	4. Paid-up perpetual non-cumulative preference shares	
	5. Paid-up perpetual non-cumulative preference share premium	
	6. Statutory Reserve	
	7. Capital reserves – excluding assets revaluation	
	8. General reserves – excluding reserves for losses on assets	
	9. Retained earnings – audited	
	<b>Tier I capital before deductions</b>	
	<b>Less deductions: Total</b>	
	(a) Goodwill	(       )
	(b) Current year's losses	(       )
	<b>Tier I capital after deductions</b>	

**SCHEDULE 1-C**

<b>CATEG ORY</b>	<b>CAPITAL ACCOUNTS</b>	<b>M000</b>
<b>Tier II</b>	1. Fixed Assets revaluation reserves	
	2. Securities revaluation reserves (discounted)	
	3. Undisclosed or hidden reserves	
	4. General provisions/reserves for losses on assets (up to 1.25% of weighted-risk assets)	
	5. Paid-up, perpetual, cumulative preference shares	
	6. Long-term preference shares	
	7. Perpetual debt instruments	
	8. Mandatory convertible debt instruments	
	9. Subordinated term debt and limited life preference shares (limited to 50% of Tier I capital)	
	<b>Tier II capital</b>	
<b>Tier I &amp; Tier II</b>	Total capital (Tier I & II)	
	Less deductions: (Total)	
	(a) Investments in unconsolidated financial subsidiaries	(      )
	(b) Intangible assets	(      )
	(c) Deficiencies in provisions for losses	(      )
	(d) Others (as may be determined by the Central Bank)	(      )
	<b>TOTAL QUALIFYING CAPITAL</b>	

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## SCHEDULE II

### OECD COUNTRIES

#### (regulation 7 (2) (e) (i) )

1. "OECD countries" means those countries which are full members of the organisation for Economic Cooperation and Development (or countries which have concluded special lending arrangements with the International Monetary Fund in terms of the said Fund's General Arrangements to BORROW), but excludes any country within this group which has rescheduled its external sovereign debt in the previous 5 years.
2. The following countries fall into the OECD -

Australia	Greece	Norway
Austria	Iceland	Portugal
Belgium	Ireland	Spain
Canada	Italy	Sweden
Denmark	Japan	Switzerland
Finland	Luxembourg	United Kingdom
France	Netherlands	United States of
Germany	New Zealand	America

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**SCHEDULE III**

**APPROVED REGIONAL COUNTRIES**

**(regulation 7(2) (e) (ii) )**

Approved regional countries refer to SADC countries of-

Angola	Seychelles
Botswana	South Africa
D. R. Congo	Swaziland
Malawi	Tanzania
Mozambique	Zambia
Mauritius	Zimbabwe
Namibia	

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**SCHEDULE IV**

**MULTILATERAL INSTITUTIONS**

**(regulation 7(2) (e) (iii) )**

Multilateral Institutions refer to the following–

African Development Bank  
African Export-Import Bank  
Development Bank of Southern Africa  
European Investment Bank  
European Union  
International Monetary Fund  
United Nations  
World Bank