

CIRCULAR

TO: All Non-Bank Financial Institutions (NBFIs)

FROM: The Non-Bank Financial Institutions Regulatory Authority (NBFIRA)

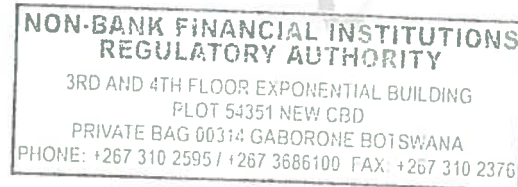


Sriram Gade

Deputy CEO- Regulatory

DATE: January 26, 2021

SUBJECT: **INVITATION FOR COMMENTARY ON THE RELATED PARTY
TRANSACTIONS GUIDELINES FOR NON BANK FINANCIAL
INSTITUTIONS (“NBFIs”)**



1. The Non-Bank Financial Institutions (“NBFIs”) in Botswana are regulated by the Non-Bank Financial Institutions Regulatory Authority (“NBFIRA”) in accordance with the NBFIRA Act of 2016 (“the Act”). The Act provides for the *Regulatory Authority*’s powers and functions to regulate NBFIs for the purposes of improving the fairness, efficiency and orderliness of the non-bank financial sector; the stability of the financial system; and for matters incidental thereto.
2. The *Regulatory Authority* is empowered by section 4(2)(d) of the Act to make rules, set standards and provide guidelines for NBFIs. In addition, section 4(2)(e) empowers the *Regulatory Authority* to give directions to any person to ensure compliance with a relevant law, rule or guidelines.
3. In pursuit of the aforementioned, the *Regulatory Authority* has drafted the Guidelines for Related Party Transactions (“the Guidelines”). The Guidelines (herein attached) for your review and commentary, were developed for all NBFIs.

4. NBFIs are encouraged to share their written comments, suggestions and feedback, on or before February 26, 2021, with their respective regulatory departments at the following email addresses.

- i. Capital Markets: mmodise@nbfira.org.bw & kntebang@nbfira.org.bw;
- ii. Insurance: otshoswane@nbfira.org.bw & gmolojwane@nbfira.org.bw;
- iii. Lending Activities: gsechele@nbfira.org.bw & tlekorwe-modibedi@nbfira.org.bw; and
- iv. Retirement Funds: bndlovu@nbfira.org.bw & kmarumo@nbfira.org.bw.



RELATED PARTY TRANSACTIONS GUIDELINES

NON-BANK FINANCIAL INSTITUTIONS

(“NBFIs”)

1. Overview

The Non-Bank Financial Institutions Regulatory Authority (NBFIRA) recognizes that transactions between and among related parties create financial and economic benefit to group companies. However, the nature of the related parties’ relationships and greater significance or complexity of their transactions may give rise to specific risks of material misstatement of the financial statements due to error or fraud.

The *Regulatory Authority* is empowered by section 4(2)(d) of the NBFIRA Act of 2016 to make rules, set standards and provide guidelines for non-bank financial institutions. In addition, section 4(2)(e) empowers the *Regulatory Authority* to give directions to any person to ensure compliance with a relevant law, rule or guideline.

The purpose of this document is therefore to give guidance on the disclosure of transactions between non-bank financial institutions (NBFIs) and their Related Parties. The guidelines give direction to the regulated entities to develop policies and procedures which guard against conflict of interest and any possibility of abuse when conducting transactions with Related Parties.

This guidance note must therefore be read together with Sections 6, 7 and 8 of Companies Act, 2018, Financial Reporting Act, 2010 and its supporting legislation, International Reporting Standard (IFRS 12 – Disclosures of Interests in Other Entities) and International Accounting Standard (IAS); IAS 24-Related Party Disclosures, IAS 28 – Investment in Associates, Joint Ventures and IAS 31 – Interest in Joint Ventures and other financial services laws.

2. Objectives

The objectives of the guidelines are to improve disclosure requirements on related party transactions and outstanding balances with an NBFIs related party in order to:

- 2.1 Ensure that there is no conflict of interest in Related Party Transactions and that such transactions are conducted at arms' length.
- 2.2 Ensure that entities effectively appraise, ratify, approve and disclose Related Party Transactions in a transparent manner.
- 2.3 Prohibit preferential transactions with executive officers, directors and shareholders of affiliated financial institutions.
- 2.4 Ensure that an NBFIs financial statements contain the disclosures necessary to draw attention to the possibility that its financial position and profit or loss may have affected by such parties.
- 2.5 Prescribe ceilings for Related Party Transactions to limit risk.

3. Key terms

- 3.1 **Arm's length:** Any transaction between an NBFIs related party shall be on an arm's-length basis.

An NBFIs shall not enter into a transaction with or for the benefit of a related party if such transaction would be entered into on less favourable terms and conditions, or not at all, with or for the benefit of persons who are not so related to an NBFIs.

- 3.2 **Related Party:** A director, senior manager, trustee or significant shareholder of the NBFi or an entity in which the NBFi has a significant direct or indirect shareholding, as well as a connected person and entity of any of the aforementioned persons or entities.
- 3.3 **Related Party Transactions Committee:** A committee responsible for reviewing and endorsing related party transactions. The Related Party Transactions Committee may constitute of management or Board members depending on the structure of the NBFi.
- 3.4 **Senior Management:** Members of management of the NBFi or person who report directly to the Board of Directors or the Chief Executive (howsoever described) of the NBFi.
- 3.5 **Senior Manager:** A person who is a member of senior management.
- 3.6 **Significant Shareholder:** A person who holds, either themselves or in aggregate with their connected persons, a significant shareholding. Governments are excluded from this definition.
- 3.7 **Significant Shareholding:** 10% or more of the shares or voting rights in the NBFi or business.
- 3.8 **Ordinary Course of business:** Refers to the business that the entity is licensed by the Authority to conduct.

4. Scope and Nature of Related Party Transactions

- i) Financial transaction of purchase or sales of goods and exchange of services;
- ii) transactions on shared labour service;
- iii) Agency transaction
- iv) property transaction;
- v) leasing transaction
- vi) financing and interest collection & payment;
- vii) endorsements and guarantees;
- viii) transactions involving the assumption of financial/operating obligations;
- ix) transactions that include the subscription for debt/equity issuances (in cash and in kind);
- x) transactions that involve the establishment of joint-venture entities;
- xi) transactions involving the transfer of intangible items (e.g. research and development, trademarks, license agreements);
- xii) outsourcing arrangement

- xiii) management contracts; and
- xiv) any other transactions

5. Requirements of Related Party Transactions

5.1 The board of an NBFIs shall have a written Policies and Procedures put in place, and adhered to, in order to;

- i) Identify individual transactions to a Related Party as well as the total amount of such transactions and to monitor and report on such transactions through an independent review process;
- ii) Prevent members of staff of the entity from benefiting from a Related Party Transaction (otherwise than the receipt of standard remuneration also available in transacting with non-related parties).

5.2 Where applicable, NBFIs should disclose any other transaction deemed not on-arm's length such as staff purchase of repossessed assets of clients.

5.3 Related Parties are responsible for disclosing Related Party Transactions and the material interest that they or an immediate family member may have on such transactions.

5.4 The following information, to the extent relevant, with respect to the proposed Related Party Transaction should be disclosed by the Related Parties:

- i) The name of the Related Party and the basis on which such person or entity is a Related Party.
- ii) A general description of the transaction(s) including the material terms and conditions.
- iii) The Related Party's interest in the transaction(s) including the Related Party's position or relationship with, or ownership of, any entity that is a party to or has an interest in the transaction(s).

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- iv) The total value of the proposed transaction and the share of the Related Party's interest in the transaction(s).
 - v) Whether the entity will be a party to the transaction and if not, the nature of its participation in the transaction(s).
 - vi) Whether the proposed transaction includes any potential reputational risk issues that may arise as a result or in connection with the proposed transaction.
 - vii) A reconciliation of the related party transactions to ensure that any deviations are promptly addressed.
 - viii) Any other material information regarding the transaction(s) or the Related Party's interest in the transaction(s).
 - ix) Necessary disclosures shall be made also in the Notes to the Audited Financial Statements

5.5 NBFIs to ensure that all service providers including auditors, suppliers and vendors certify that they do not have a conflict of interest with the company.

5.6 Disclaimer is required from all approving officer(s) signing contracts, agreements, work orders and purchase orders that they are not related to the counterparties of the proposed transaction.

5.7 Related Party Transactions should be subjected to a written process, approved in advance by the Board, for on-going monitoring by senior management;

5.8 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. Furthermore, the institution shall, within 5 business days, report any such deviation to the **Regulatory Authority**, advising of the background and the proposed remedial action;

6. Exposures

6.1 An NBFI shall not transact with a Related Party where to do so would result in the exposures of the NBFI exceeding one or more of the following limits:

Exposure Category	LIMITS			
	Lending	Capital	Retirement Funds	Insurance
i) Exposures to any one of the NBFI's directors or senior management, trustee 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 total equity	0.5% of total equity	0.5% of total equity of Related Party	0.5% of total equity
ii) The aggregate of exposures under i), above.	5.0% total equity	5.0% total equity	5.0% of total equity of Related Party	5.0% total equity
iii) Exposure to any one of its significant shareholders, including exposures to businesses in which the significant shareholder has a significant shareholding.	5% of total equity	5% of total equity		5% of total equity
iv) The aggregate of exposures under iii), above	15% of total equity	15% of total equity		15% of total equity

v)	Exposures to a client or group of connected clients, other than a NBFI, in which the NBFI has a significant shareholding	5% of total equity	5% of total equity		5% of total equity
vi)	The aggregate of exposures under v)., above.	15% of total equity	15% of total equity		15% of total equity

NB: Exemption from iii) and iv): An NBFI may apply to the *Regulatory Authority* 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 NBFI itself is subject.

An NBFI will also be exempted based on merits from the limit in iii) and iv) as per its Group Treasury Management Policy, approved by the *Regulatory Authority*.

7 Review and Approval

7.1 All Related Party Transactions must go through the normal approval processes of the NBFI after due consideration to existing regulations and limits.

7.2 All Related Party Transactions including transactions falling under the ordinary course of business with deviations are referred to the Related Party Transactions Committee. The Committee reviews and ratifies these Related Party Transactions and endorses to the Board for approval.

7.3 The Committee should consider the following factors to the extent relevant to the Related Party Transaction in conducting an independent review:

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- i) The identities of the parties involved in the transaction or relationship;
 - ii) The terms of the transactions are fair and on arms' length basis to the NBFI;
 - iii) The impact on Director's or Senior management's independence; and
 - iv) Whether the Related Party Transaction would present an improper conflict of interest for any Shareholder, Director, Senior manager of the NBFI.

7.4 The Board of Directors approves and confirms all Related Party Transactions endorsed by the Related Party Transactions Committee.

7.5 Directors should ensure that they have, or have access to, sufficient knowledge or expertise to assess all aspects of the proposed related party transactions, where necessary they should obtain appropriate professional and expert advice from appropriately qualified persons.

7.6 Any member of the Board or Related Party Transactions Committee who has interest in the transaction must abstain from participation in the review and approval of any Related Party Transaction.

7.7 Where applicable, the following shall be required:

a) Independent Shareholders Approval

- i) An NBFI must send a circular to its investors including the information in section 7.6. Any circular sent to shareholders in connection with a related party transaction must provide sufficient information to enable any recipient of the circular to evaluate the effects of the transaction on the NBFI;
- ii) An NBFI must obtain independent shareholders' approval by way of an ordinary resolution or Special Resolution as shall be directed by the Regulator taking into account the circumstances of each matter.
- iii) In the event a Special Resolution is required, the validity of the resolution shall be subject to a minimum of 75% votes by independent shareholders in favor of the related party transaction.
- iv) The NBFI shall include in the special or ordinary resolution to approve or give effect to the transaction a condition that the validity of the resolution will be subject to a

simple majority (for an ordinary resolution) or a majority of 75% (for special resolution) of the votes of the independent shareholders being cast in favor of the resolution.

- v) Shareholder approval must be obtained either prior to the transaction being entered into or, if the transaction is expressed to be conditional on such approval, prior to the completion of the transaction.

b) Independent Expert's Opinion

- i) In the event that there is reliance on a report on the transaction from an independent expert, the report must state the expert's opinion as to whether the transaction is fair and reasonable to investors.
- ii) The expert's opinion must be displayed prominently in the notice of the meeting and on the covering page of any accompanying documents.
- iii) the report from the independent expert required must set out, at a minimum:
 - 1. the reasons for the opinion;
 - 2. the key assumptions made;
 - 3. the factors taken into consideration in forming the opinion; and
 - 4. a statement as to whether the transaction is on normal commercial terms, in the ordinary course of business, fair and reasonable and in the best interests of the investors.

8 Disclosure and Reporting to the Regulatory Authority

The NBFi shall publicly disclose in its website the Policy on Related Party Transactions and disclose to its shareholders and members at annual general meetings.

- Necessary disclosures shall be made also in the Notes to the Annual Financial Statements of the NBFi

8.1 Related Party exposures shall be reported to the *Regulatory Authority* on a quarterly basis, except in case of deviations, and in a format specified from time to time by the *Regulatory Authority*. This is without prejudice to the rights and powers of the *Regulatory Authority*

to otherwise request specific information at any point in time or to conduct inspections of a NBFIs compliance with the guidelines.

8.2 Where an entity considers that there may have been an error in its conduct by reference to the requirements of this guidelines (including without limitation reporting requirements imposed in respect of these guidelines) the NBFIs shall within 5 business days inform the *Regulatory Authority* in writing of its proposals for correcting any such error as may have occurred.