



CENTRAL BANK OF CYPRUS
EUROSYSTEM

**POLICY STATEMENT
ON THE LICENSING OF BANKS IN THE
REPUBLIC OF CYPRUS
AND
GUIDELINES ON THE INFORMATION WHICH
MUST BE INCLUDED IN AN APPLICATION FOR A
LICENCE**

BANKING SUPERVISION AND REGULATION DIVISION

2010

CONTENTS

Part I: Policy Statement on the licensing of banks in the Republic of Cyprus

Part II: Guidelines on the information which must be included in an application for a licence - Questionnaires

CONTENTS

Part I: Policy Statement on the licensing of banks in the Republic of Cyprus

1. Introduction

- 1.1 Scope and application
- 1.2 Definitions

2. Application procedure for a Banking Business Licence

- 2.1 The licensing process
- 2.2 Pre-application meetings
- 2.3 Application
- 2.4 Determination of an application for a Banking Business Licence
- 2.5 Authorisation for commencement of business of a licensed bank

3. Statutory requirements for the granting of a Banking Business Licence

- 3.1 Legal form and location of Head Office
- 3.2 Identification and suitability of the Applicant's Controllers
- 3.3 Minimum Capital
- 3.4 Business plan
- 3.5 Close links
- 3.6 Prior consultation with the competent supervisory/regulatory authorities of the parent undertaking
- 3.7 "Fitness and properness" of Directors, Chief Executives and Managers
- 3.8 The "four eye" principle

4. Further guidance to Applicants which are legal persons established in the Republic, the Controllers of which are not part of a regulated banking/financial group

5. Possible reasons for refusing to grant a Banking Business Licence

PART I: POLICY STATEMENT ON THE LICENSING OF BANKS IN THE REPUBLIC OF CYPRUS

1. INTRODUCTION

1.1 Scope and application

The procedure and requirements for the granting of a licence for the pursuance of banking business (“banking business licence”) are laid down in the Banking Laws of 1997 to 2009 as may be amended (hereinafter to be referred to as “the Law”). This document is issued under Section 4(7) of the Law and outlines the policy of the Central Bank of Cyprus (“CBC”) with regard to the licensing of banks. It also provides guidance as per the provisions of section 4(2)(a) of the Law, as to the information and documentation that must be submitted with an application. The current document should be viewed as a supplement and be read in conjunction with the Law and the CBC Directives issued thereunder. It must not be regarded as a substitute for reading or adhering to the provisions of the Law itself.

The application for a banking business licence must be addressed to the Governor of the CBC and must be signed by the authorised representatives of the Applicant. The responsibility for the correctness, completeness and accuracy of the information included in the application as well as for the details and documents that accompany it, rests with the person(s) signing and submitting the application as well as the persons completing and submitting the questionnaires included in Part II of this document, to the CBC.

The CBC is statutorily charged with the licensing and supervision of banks. The powers of the CBC, in this respect, derive from the Law, which contains provisions relating to, inter-alia, the granting and revocation of licences, requirements for submission of information by banks, the undertaking of on-site inspections and the supervision generally of their activities, as well as the authorisation of significant changes in their ownership structure and the assessment and approval of their directors/managers.

Section 4(1)(b)(i) of the Law provides that a banking business licence is granted only to a legal person established in the Republic pursuant to the provisions of the

Companies Law, Cap 113 or of any other law or to a legal person established in a country other than the Republic, pursuant to the corresponding legislation of that country.

The provisions of the present document, therefore, apply to Applicants which are:

- i. legal persons established in the Republic, (e.g. a company incorporated in the Republic, under the provisions of the Companies Law) which wish to obtain a banking business licence; or
- ii. legal persons established in a third country (registered in the Republic as an overseas company under section 347 of the Companies Law) which wish to obtain a banking business licence.

The relevant licensing section of the Law does not distinguish between a banking business licence granted to a legal person established in the Republic (i.e. a locally incorporated bank) and a banking business licence granted to a legal person established in a third country, which registers a place of business (i.e. branch) in the Republic. The licensing requirements applied by the CBC are, therefore, approximately the same for both cases.

In this context it must be clarified that where the Applicant is a legal person as described in (i) above, then the said legal person may, either be a Cyprus subsidiary of a foreign bank, or a Cyprus company the shareholders of which are not all necessarily financial entities, but may be a joint venture between financial and non-financial entities/persons, the application of which, if successful, will be granted a banking business licence by the CBC. Where the Applicant is a legal person as described in (ii) above, the said legal person must be a bank established in a third country which, in the event that its application is successful, will be granted a banking business licence to establish a branch in the Republic. In the latter case the licence is not granted to the branch, which is not a separate legal entity, but to the Applicant, as described in (ii) above. In this case the CBC, once it licenses the Applicant bank, only supervises the activities of its branch in the Republic.

Branches of banks established in a third country are subject to the same obligations as locally incorporated banks, with respect to their organisation, their operating conditions, accounting and prudential standards. Branches are, therefore, subject to the CBC's regulations designed to safeguard the interests of customers, the principle

being that users of banking services must be protected in the same way, whether the services are provided by a locally incorporated bank or by a branch of a foreign institution. Accordingly, the branches of third country banks are also members of the deposit guarantee scheme. Branches are, however, allowed a certain degree of flexibility with regard to prudential requirements (may be exempt from solvency requirements, and limits on large exposures).

The present document does not apply to E.U. credit institutions wishing to establish a branch in the Republic, since credit institutions licensed by competent authorities of another member state of the E.U. may, under the provisions of Section 10A of the Law, establish a branch in Cyprus without the need of obtaining a banking business licence from the CBC. In this respect, the CBC has issued a document titled *“Guidelines on the Freedom of Establishment and the Freedom to provide services in the Republic of Cyprus by a credit institution incorporated in another member state of the European Union”* which is downloadable from the CBC’s website at <http://www.centralbank.gov.cy>.

1.2 Definitions

For the purposes of this document, the following terms and expressions have the following meaning:

“Applicant” means a legal person established in the Republic pursuant to the provisions of the Companies Law or of any other law or a legal person established in a third country, pursuant to the corresponding legislation of that country, which submits an application to obtain a banking business licence, under the provisions of the Law.

“Banking business” has the meaning ascribed to the said term in Part I of the Law.

“Bank incorporated in the Republic” means a legal person established in the Republic pursuant to the provisions of the Companies Law, Cap 113, and licensed to carry on banking business under the provisions of the Law.

“Bank” has the meaning ascribed to the said term in Part I of the Law.

“Branch” has the meaning ascribed to the said term in Part I of the Law.

“**Branch of a bank incorporated in a third country**” means a branch operating in the Republic of a bank established in a third country, pursuant to the corresponding legislation of that country.

“**CBC**” means the Central Bank of Cyprus.

“**Close links**” have the meaning ascribed to the said term in Part I of the Law.

“**Competent authorities**” have the meaning ascribed to the said term in Part I of the Law.

“**Control**” has the meaning ascribed to the said term in Part I of the Law.

“**Controller**” means a person who/which: (a) beneficially owns 10% or more of the share capital of the Applicant or of its holding company, enabling the said person to have 10 per cent or more of the voting rights at any general meeting of the Applicant or its holding company, or (b) have the ability to determine in any manner the election of a majority of the directors of the Applicant or of its holding company.

“**Credit institution**” has the meaning ascribed to the said term in Part I of the Law.

“**Director**” has the meaning ascribed to the said term in Part I of the Law.

“**Foreign bank**” is a bank incorporated outside the Republic.

“**Home Member State**” and “**Host Member State**” have the meaning ascribed to the said terms in Part I of the Law.

“**Law**” means the Banking Laws of 1997 to 2009 as may be amended.

“**Legal person**” has the meaning ascribed to the said term in Part I of the Law.

“**Licence**” has the meaning ascribed to the said term in Part I of the Law.

“**Proposed bank**” means the bank to be licensed by the CBC and includes the prospective subsidiary/branch of a foreign bank or the prospective locally incorporated bank which is not a subsidiary.

“**Republic**” means the Republic of Cyprus

“**Significant influence**” means to exercise a significant influence over the management of a bank (for example by having a representative on the board of directors), although not being a controlling shareholder.

“**Subsidiary company**” or “**holding company**” have the meaning ascribed to the said terms in Part I of the Law.

“**Third country**”, has the meaning ascribed to the said term in Part I of the Law.

2. APPLICATION PROCEDURE FOR A BANKING BUSINESS LICENCE

2.1 The licensing process

The licensing process for obtaining a banking business licence involves four stages:

- (a) Pre-application meetings.
- (b) Application stage.
- (c) Licensing of the bank.
- (d) Authorisation for the commencement of banking business by the bank.

The licensing of a bank, presupposes, also, the approval by the CBC, of all direct and indirect Controllers and of all persons appointed as board members and chief executives or managers of the bank concerned.

2.2 Pre-application meetings

The licensing process, while governed by formal procedures, is intended to be interactive, and in this respect prospective Applicants should seek to consult with the CBC as early as possible and, in any event, prior to their final decision to submit an application, in order to discuss the nature of the prospective application and to receive the CBC's preliminary views on the manner in which the application should be prepared as well as on the prospects of a possible application.

2.3 Application

Applications for a banking business licence, must be submitted in writing by or on behalf of the Applicant to the CBC, together with the Memorandum and Articles of Association, or any other incorporation document or determinative for the establishment of a legal person. It must be noted that if the application is for the incorporation of a bank in the Republic, it is preferable that a draft Memorandum and Articles of Association be submitted to the CBC.

It is important for Applicants to ensure that, during the application process, they disclose all matters that may be of interest to the CBC in assessing the Applicant's ability to satisfy and continue satisfying the CBC's requirements. For an application to be regarded by the CBC as complete, the Applicant must submit all relevant

information and fill in and submit all the relevant forms, which may be found in Part II of this document. The information on these forms needs to be complete and accompanied by all the required supporting documentation. The application documentation is intended to provide the CBC with, inter-alia, information on:

- (a) the identity and suitability of all direct or indirect Controllers, directors and managers of the Applicant;
- (b) the source of funding of the proposed bank, as well as the transparency and legitimacy of this source;
- (c) the financial standing of the Applicant, its Controllers and/or the group to which it belongs;
- (d) the adequacy of the proposed bank's business plan, which must provide insights on the proposed banking activities to be conducted as well as on the proposed bank's projected financial condition, its management and organisational structures, including the proposed internal governance and compliance procedures and systems to be used;
- (e) the existence of any close links between the Applicant and other natural or legal persons, which may prevent the effective exercise of the CBC's supervisory function.

At any time after receiving an application and before determining it, the CBC may require the Applicant to provide it with such further information, as it reasonably considers necessary to enable it to determine the application.

2.4 Determination of an application for a banking business licence

The CBC may, under section 4(3) of the Law, with an adequately reasoned decision:

- (a) grant a licence without any condition or subject to such conditions it may consider proper to impose; or
- (b) refuse to grant a licence.

A refusal must be notified to the Applicant within six months from the date of receipt of the application for a licence. Should an application be incomplete, a refusal must be

notified to an Applicant within six months from the date of receiving the additional information/clarifications. Notwithstanding the above, the CBC is bound to take a decision within a year of the receipt of an application.

2.5 Authorisation for commencement of business of a licensed bank

In the event that the application is successful, and a licence is issued by the CBC, the licensed bank must, within a maximum period of 12 months, prepare for its setting up and operation.

Prior to the CBC giving its final authorisation to the licensed bank to commence operations, a letter must be addressed by the licensed bank to the CBC declaring that

- (a) it has observed all conditions attached to its banking licence ;
- (b) its initial capital has been fully paid-up (for locally incorporated banks);
- (c) its initial contributions to the Deposit Protection Fund and the Investor Compensation Fund for Clients of Banks have been paid, unless it is exempted from such an obligation under the relevant Regulations governing the establishment and operation of the above Funds ;
- (d) the premises where bank activity will be conducted comply with security and protection requirements according to best practices and industry standards ;
- (e) the information and accounting systems implemented, are capable of producing its true financial picture, providing the necessary information for decision making and ensuring the compilation of annual or periodic financial statements, as well as of the prudential/statistical returns, in an accurate and timely manner.

The above letter should be accompanied by a confirmation from the bank's approved external auditors, that requirements under points (b) to (e) have been met by the bank.

3. STATUTORY REQUIREMENTS FOR THE GRANTING OF A BANKING BUSINESS LICENCE

The Law sets a number of requirements for the granting of a banking business licence. In particular, the CBC is required by Law to ensure that the Applicant has suitable Controllers and, at least, the minimum capital required by the Law, and must give due consideration to the proposed bank's programme of operations, its technical and financial resources, as well as the suitability of the persons who will be managing its operations.

Always guided by the statutory requirements of the Law as indicated in paragraphs 3.1 to 3.8, and by the requirements of the Central Bank of Cyprus Laws of 2002 to 2007, which places an obligation on the CBC to preserve the stability of the banking system, the CBC has developed through the years, a consistent practice on the basis of the above principles, gradually refining its requirements under which applications for a banking licence are examined.

3.1 Legal form and location of Head Office

Section 4 of the Law allows an application to be made to the CBC by a legal person, which is either incorporated in the Republic or abroad. In specific, Sections 4(1) b (i) and b (ii), provide that a banking business licence is issued only to a legal person established in the Republic, under the Companies Law or any other law, or to a legal person which has been incorporated in a country other than the Republic, under the provisions of the corresponding legislation of the said country.

A locally incorporated bank (legal person established in the Republic) must have its Head Office in the Republic. A bank established in a third country, which is granted a banking business licence by the CBC, to establish a place of business in the Republic (i.e. branch), may have its Head Office in a country other than the Republic.

3.2 Identification and suitability of the Applicant's Controllers¹

3.2.1 In accordance with Sections 4(1)(c) and 4(1)(d) of the Law, the CBC shall not grant a banking business licence to an Applicant unless it:

- (a) has been previously informed of the **identity** of the shareholders or members (both natural and legal) who exercise control, directly or indirectly, in the Applicant and their respective shareholding, and
- (b) is satisfied that the above persons are "**suitable**" to ensure the proposed bank's sound and prudent management.

The CBC determines the identity and suitability of direct and indirect Controllers, through detailed questionnaires and other information required, which may be found in Part II of this document.

The CBC's assessment regarding the **suitability** of the Applicant's direct and indirect Controllers, and/or the Applicant aims at ensuring that the proposed bank will be managed in a sound and prudent manner. Suitability is tested against the following areas:

- Reputation of the Applicant and/or its Controllers.
- Financial soundness of the Applicant and/or of its Controllers.
- Suspicion of money laundering or terrorist financing by the Applicant and/or its Controllers.

3.2.2 Reputation of the Applicant² and or its Controllers

The CBC's assessment of the **reputation** of the Applicant and/or of its Controllers, covers two elements: (a) integrity and (b) professional competence.

(a) **Integrity requirements** imply the absence of "negative records". Matters which the CBC may take into account (but not limited to these matters) are:

- Any evidence that the Applicant and/or any of its Controllers have been convicted of a criminal offence. Special consideration is given to any offence under the laws governing banking, financial securities, or insurance activity, or concerning securities markets or payment instruments, including laws on

¹ Where the Applicant is a legal person established in a country other than the Republic, regulated and supervised as a bank, the identity and suitability criterion extends to both the Controllers of the legal person and the legal person itself.

² Where the Applicant is a legal person established in a country other than the Republic, regulated and supervised as a bank, the reputation criterion extends to both the Controllers of the legal person and the legal person itself.

money laundering, market manipulation, or insider dealing and usury as well as other offences under legislation relating to companies, bankruptcy, insolvency, or consumer protection, etc ;

- Any evidence that the Applicant and/or any of its Controllers have not been transparent, open and co-operative in their dealings with supervisory/regulatory authorities ;
- Any evidence that the Applicant and/or any of its Controllers have been refused registration, authorisation, membership, or licence to carry out a trade, business or profession or have had that registration, authorisation, membership or licence revoked, withdrawn or terminated ;
- Any evidence that the Applicant and/or any of its Controllers have been dismissed from employment or a position of trust, fiduciary relationship, or similar situation, or have been asked to resign from employment in such a position or have been disqualified from acting as a director.

The information requirements on which the CBC's assessment of integrity is based, may vary according to the nature of the person assessed (natural versus legal person, regulated or supervised entity versus unregulated entity).

If a Controller of an Applicant is a legal person, the integrity requirements must be satisfied by the legal person as well as by all of the persons who effectively direct its business.

The CBC when assessing the integrity of an Applicant and/or any of its Controllers, will also take into consideration the integrity of persons having close links with any of the Controllers and/or the Applicant.

(b) The **Professional Competence** assessment of the Applicant and/or any of its Controllers covers competence in management ("management competence") and competence in the area of banking/financial activities ("technical competence").

If a Controller of an Applicant is a legal person, the assessment of professional competence covers both the company itself and the persons who effectively direct its business.

The assessment of **management competence** of a legal person may take into account, but not limited to whether:

- its governing body is made up of individuals with an appropriate range of skills and experience to understand, operate and manage its activities ;

- If appropriate, whether its governing body, includes non-executive and/or independent representation, at a level which is appropriate for the control of its activities ;
- its governing body is organised in a way that enables it to address and control its activities, including those carried on by managers to whom particular functions may have been delegated.

In the case of a private/family owned or state owned foreign bank which is not listed wishing to establish either a branch or a subsidiary in the Republic, the assessment of management competence will, also, take into account whether its controlling shareholders respect the independence of its governing body, are not involved in the day to day management of the bank and its governing body is allowed to exercise its responsibilities independent of any influences which could lead to conflicts of interest.

The assessment of management competence of a natural person, may take into account but not limited, factors such as the person's previous experience in acting as a Manager/Director of financial institutions, and whether it may be demonstrated that the person has acted with due diligence and compliance with relevant standards.

The assessment of **technical competence** relates primarily to the banking/financial activities currently performed by the Applicant and/or by its Controllers.

In assessing professional competence, of Controllers of a bank to be incorporated in the Republic, the CBC takes into account the influence that the Controllers will exercise on the proposed bank. That is, competence requirements are reduced for Controllers who do not intend to exercise a decisive influence over the proposed bank and vice-versa.

The **Reputation requirement** (ie integrity and professional competence requirements) is generally presumed to have been met by a person (natural or legal) if:

- it is a person already considered by another E.U. regulator to be “of good repute” in his/its ability of exercising significant influence over another financial institution/bank which is supervised by another competent supervisor in another E.U. member state;
- it is a person already holding a post of a manager or director of a financial institution which is supervised by another competent supervisor in another E.U. member state; or
- it is a person regulated and supervised as a bank or financial institution by another competent authority in another E.U. member state.

If the person concerned is supervised by a competent supervisor in a third country, the CBC's assessment of integrity and professional competence may be based on an assessment of the substantial equivalence of the regulation concerning reputation in a third country. In this respect, the CBC may require to be provided with details regarding the assessment requirements of the relevant country, in order to form its own opinion.

In this context, when a foreign bank wishes to establish either a branch or a subsidiary bank in the Republic, the CBC, in assessing its reputation, will take into account, inter-alia, whether the said bank:

- Conducts its business with integrity and in compliance with accepted international banking standards ;
- has a competent and prudent management;
- can demonstrate that it will conduct its business in the Republic with due skill, care and diligence;
- is a listed company with an independent governing body or, alternatively, there is a widespread ownership, with no dominant personal interests.

3.2.3 Financial soundness of the Applicant³ and/or its Controllers

The financial soundness of the Applicant and/or its Controllers is understood by the CBC as the capacity of the latter to finance their participation in the proposed bank and to maintain its sound financial structure in the foreseeable future. This capacity should be reflected in the forecast financial objectives, consistent with the strategy identified in the business plan. The CBC, through its assessment, evaluates whether the financial soundness of the Applicant and/or its Controllers is strong enough to ensure the sound and prudent management of the proposed bank. When assessing this aspect the CBC will, also, take into account any available credit ratings assigned to the Applicant and/or its Controllers or to the group to which they belong, by international credit rating agencies.

The CBC may, in its discretion, refuse to grant a banking business licence if it concludes, based on its analysis of the information received, that the Applicant and/or

its Controllers is/are likely to face financial difficulties, in the foreseeable future. The CBC also takes into account the ability/commitment of the Applicant and/or its Controllers to provide further financial support to the proposed bank, in case of liquidity or solvency problems. Factors such as an established track record of growth, and strong financial position of the Applicant and/or its Controllers, will, therefore, have a positive impact on the assessment carried out by the CBC. On the other hand, a declining track record of growth and profitability, or the taking of excessive risks (high risk appetite), may have a negative impact on the assessment. The involvement of the Applicant and/or any of its Controllers in high risk financial activities or in non-financial activities and other interests, which may potentially expose the proposed bank to excessive risks, will also be viewed with caution by the CBC.

The depth of the assessment and the information required to be submitted by the Controllers of an Applicant will depend, among other, on the percentage participation of the Controller and on the legal status of the Controller, for example whether it is a financial institution subject to prudential supervision, a legal entity other than a financial institution, or a natural person.

In this context and drawing from past experience, the CBC considers that it is more likely that an application from a foreign bank wishing to establish either a branch or a subsidiary bank in the Republic, will be successful if the said bank fulfils certain characteristics, some of which may be:

- It is of good financial standing, with an established track record of growth and profitability, has adequate internal control systems and satisfactory solvency and liquidity ratios;
- Its balance sheet does not exhibit any material concentration in lending and deposits;
- The foreign bank or the group of which it forms part, enjoy reasonably high ratings by an international credit rating agency;
- The foreign bank is above a medium sized bank in its country of incorporation, and, preferably, of systemic importance. The CBC may, therefore, take into

³ In case the Applicant is a legal person established outside Cyprus, regulated and supervised as a bank, the assessment of financial soundness extends both to the legal person as well as to its controllers.

account criteria such as its market share in terms of loans, deposits and total assets;

3.2.4 Suspicion of money laundering or terrorist financing⁴

If the CBC has reasonable grounds to suspect that the Applicant and/or any of its Controllers, is/are involved or attempted to be involved in money laundering operations, or is “listed” as being a terrorist, or has financed terrorism, the application will be rejected. The term “reasonable grounds” plays an important role in the assessment of the CBC. Missing information or information regarded as incomplete, insufficient or liable to give rise to suspicion (for example, capital movement not accounted for, cross-border relocation of headquarters, reshuffles in management or legal-person owners, previous association of the owners, or of the management of the company with criminals), will trigger increased caution and diligence and will lead the CBC to request further information.

The CBC may also reject an application if the Applicant and/or any of its Controllers and/or the group of which it forms part, is/are incorporated in a country or territory considered by the Financial Action Task Force to be of “high risk” or “non-cooperative”, or more broadly, in a country or territory that has not taken sufficient measures to comply with robust anti-money laundering and anti-terrorist financing procedures in accordance with internationally accepted standards⁵.

In case the application is for a locally incorporated bank it is also essential to establish that the funds used for the participation in the share capital of the proposed bank, originate from legitimate sources.

3.3 Minimum capital

In accordance with section 4(2)(b) of the Law, the CBC shall not grant a banking licence if a locally incorporated bank has an initial capital of less than €5 million.

⁴Where the applicant is a legal person, regulated and supervised as a bank, the assessment with regard to the suspicion of money laundering or terrorist financing applies to both the Applicant as well as to its Controllers.

⁵ Such standards are the revised Forty Recommendations for combating money laundering (http://www1.oecd.org/fatf/pdf/40Recs-2003_en.pdf) and the nine Special Recommendations against terrorist financing of the Financial Action Task Force (http://www1.oecd.org/fatf/pdf/SRecTF_en.pdf).

Moreover, section 20 of the Law provides that a locally incorporated bank shall maintain at all times a minimum capital base not less than the above amount or such higher amount that the CBC might determine.

In accordance with section 21 of the Law, the CBC is empowered to set a minimum capital adequacy ratio for each locally incorporated bank individually, having regard to its specific circumstances (in the form of a minimum capital base in relation to a bank's risk weighted assets). The CBC, therefore, retains the right to require newly established banks to maintain their capital adequacy ratios at higher levels than the minimum ratio which is in force at the time, depending on a number of factors (e.g. the type of business undertaken).

A branch is not required to have its own minimum capital as opposed to a locally incorporated bank.

3.4 Business plan

Pursuant to Section 4(2)(a) of the Law, all applications for a banking business licence must be supported by a business plan including, inter alia, a description of the activities to be conducted by the proposed bank, its organisational structure and any other information and documents the CBC might require. For detailed information on the issues that need to be addressed please refer to Part II of this document.

All Applicants must pay particular attention when preparing the business plan, since through this evaluation, the CBC may determine whether the proposed bank will satisfy and continue to satisfy the suitability criterion in respect of having competent and prudent management and exercising due skill, care and diligence as well as its ability to comply with all prudential requirements, including capital requirements and liquidity requirements.

The business plan must be such so that the CBC be satisfied, inter-alia, that the Applicant has clearly defined and adequately researched objectives, and that the proposed operations are consistent with the Law and the CBC's licensing and prudential supervisory requirements.

The business plan, therefore, should, among other: (a) demonstrate the capability to maintain the financial soundness of the proposed bank on an on-going basis, and (b) reflect a robust internal governance framework⁶, including a clear organizational structure with well defined, transparent and consistent lines of responsibility, effective processes to identify, manage, monitor and report all potential risks to which it might be exposed, as well as adequate internal control mechanisms, including sound administrative and accounting procedures.

In case the application is for the establishment of a locally incorporated bank, the composition of the proposed bank's board of directors must be such that it will enable the formation and appropriate composition of all necessary committees required by the CBC's Directive titled "A Framework of Principles of Operation and Criteria of Assessment of Bank's Organisational Structure, Internal Governance and Internal Control Systems of 2006 to 2009".

3.5 Close links

Section 4(1) (e) of the Law provides that where close links, as defined in Part I of the Law, exist between the bank to be licensed in the Republic and other natural or legal persons, the CBC shall only grant a licence if such links do not prevent the effective exercise of its supervisory function.

Section 4(1) (f) of the Law provides, among other, that the CBC shall not grant a licence if the laws, regulations or administrative provisions of a third country governing one or more natural or legal persons with which the bank to be licensed in Cyprus has close links, prevent the effective exercise of its supervisory function.

The CBC requires all banks to provide it with all relevant information required to monitor compliance with the above provisions on a continuous basis.

Accordingly, the CBC, in assessing an application for a banking business licence, is naturally concerned about the potential of persons over whom it does not have a

⁶ The provisions of the CBC Directive 'A Framework of Principles of Operation and Criteria of Assessment of Banks' Organisational Structure, Internal Governance and Internal Control Systems" of 2006-2009, should be taken into account.

direct regulatory control, to pose a threat to the CBC supervising the licensed bank and, therefore, preventing it from achieving its statutory objectives.

The CBC, during the licensing stage takes into account, among other things, relevant matters such as whether:

- The structure and geographical spread of the Applicant, makes it possible to exercise effective supervision, exchange information with the competent authorities, and determine the allocation of responsibilities among competent authorities. Factors which may hinder these flows, include the fact that there may be branches or connected companies in territories which supervise companies to a different standard, or territories with laws which restrict the free flow of information;
- The Applicant and the group to which it belongs will be subject to supervision on a consolidated basis;
- It is possible to assess with confidence the overall financial position of the Applicant's group at any particular time; factors which may make this difficult include lack of audited consolidated accounts for a group, if companies in the same group as the Applicant have different financial years and accounting dates and if they do not share common external auditors.
- It is likely that the CBC will receive, at all times (i.e. at the licensing stage as well as on a continuous basis), adequate information from the Applicant and those persons with whom the Applicant has close links.

The group of which the Applicant forms part and/or the Applicant, must have a transparent ownership structure, so that all close links are easily identifiable, and the relationship of the Applicant with other undertakings under common control, must not be such as may result in the CBC being unable to supervise the proposed bank effectively. In this respect, any ownership of the group of which the Applicant forms part and/or of the Applicant, must not be held via bearer shares or instruments, without accountability to the ownership structure and to any close links which may exist.

3.6 Prior consultation with the competent supervisory/regulatory authorities of the parent undertaking

In accordance with sections 4(8) and 4(9) of the Law, there must be prior consultation with the competent authorities of the member state of the EU in the case where the proposed bank is:

- (a) a subsidiary of a bank or of an insurance or investment firm, authorised in another member state; or
- (b) a subsidiary of the holding company of a bank or of an insurance or investment firm, authorised in another member state; or
- (c) controlled by the same persons, whether natural or legal, who control a bank or an insurance or investment firm, authorised in another member state.

In case where the bank to be licensed is a subsidiary or a branch of a bank established in a third country (“parent bank”), then in accordance with Basel Committee recommendations, the CBC, as the host country authority, requires that the competent home supervisory/regulatory authorities of the parent bank:

- (a) are aware of and support the application,
- (b) assume the responsibility of exercising consolidated supervision, and
- (c) a Memorandum of Understanding is signed so that information may be exchanged on a timely manner.

In this respect, the CBC’s policy is to contact directly the parent bank’s home licensing and banking supervisory authority and obtain, inter-alia, its written consent as well as undertaking that it will exercise consolidated supervision over the global activities of the parent bank, including the operations proposed to be carried out by the prospective branch/subsidiary in the Republic.

The CBC may also seek to obtain directly from the home supervisor, information regarding, inter-alia, the market share of the parent bank in terms of total assets, deposits and loans as well as its financial standing, solvency and liquidity, adequacy of internal control systems, corporate governance etc. In addition, it requires to be informed whether the parent bank is systemically important in its home jurisdiction or, alternatively, highly specialised in nature.

In this respect, the CBC may also seek to ensure through the signing of a “Memorandum of Understanding” in the field of banking supervision with the home supervisory authority of the parent bank, that all necessary information concerning the management and ownership of the parent bank will be supplied on an on going basis. In addition the CBC requires a commitment from the home supervisor of the parent bank that it shall be duly notified, on an on-going basis, about:

- any supervisory measures to be taken in respect of the parent bank;
- any changes in the capital adequacy, liquidity or other indicators which could have a negative effect on the stability of the parent bank and, subsequently on the proposed bank;
- any amendments to prudential banking supervision regulations and any other conditions that could significantly affect the operations of the parent institution and subsequently, the proposed bank;
- any changes in the bank secrecy requirements in the parent bank’s home country, which may affect the transactions of the licensed bank;
- any sudden occurrence of insolvency or over-indebtedness of the parent bank.

3.7 “Fitness and properness” of Directors, Chief Executives and Managers

Section 18 of the Law provides that Directors, Chief Executives and Managers of the prospective bank or the prospective branch, as appropriate, have to satisfy the CBC that they are “fit and proper” persons to be involved in the provision of banking services. The Fitness and Probity (Assessment Criteria) of Directors and Managers of Banks Directive of 2006 and 2007 issued by the CBC, refers. The considerations which the CBC takes into account when determining “fitness and properness”, include the above persons’ integrity, competence, skills and experience in relevant financial operations commensurate with the intended activities of the bank to be licensed in the Republic as well as good reputation and character (e.g. no record of criminal activities or adverse regulatory judgements). The above matters are assessed, to the extent

possible, by means of detailed questionnaires which are required to be completed by the persons concerned, before their appointment to the relevant post.

The above is an on-going requirement and, therefore, each and every time a licensed bank wishes to appoint new Directors/Chief Executive Officers/Managers, they are required to complete an appropriate personal questionnaire, which may be found in Part II of this document.

3.8 “The four eye” principle

According to section 19 of the Law, at least two persons are required to participate and concur in the effective direction and management of the business of the bank. According to the provisions of the CBC’s Directive “A Framework of Principles of Operation and Criteria of Assessment of Bank’s Organisational Structure, Internal Governance and Internal Systems of 2006-2009”, in case of locally incorporated banks, the individuals concerned must be Executive Directors. In addition, eligible individuals must be involved in all decisions relating to the determination of strategy and general direction of the bank to be licensed in the Republic and must demonstrate knowledge of and be able to influence the way in which strategy will be implemented through day to day policy.

In the case of a branch of a bank established in a third country, the Branch Managers must be persons granted executive powers, reporting directly to the bank’s senior executive management.

4. FURTHER GUIDANCE TO APPLICANTS WHICH ARE LEGAL PERSONS ESTABLISHED IN THE REPUBLIC, THE CONTROLLERS OF WHICH ARE NOT PART OF A REGULATED BANKING/FINANCIAL GROUP

The CBC is willing to assess applications from unregulated commercial (non-financial) entities and/or joint ventures between natural and legal persons on a case-by-case basis and shall determine whether the Applicant can meet all statutory criteria, as described in this document. It must be noted, however, that, in case of such applications, the CBC may make its granting of a licence conditional on an active participation by way of shareholding interest and/or by way of management by an already licensed and established bank of repute. In addition, the CBC’s assessment of the proposal will have regard to any additional risks arising from the non-financial,

unregulated ownership structure and in this respect, a person (whether natural or legal) may not be allowed to own, directly or indirectly, more than 20% of the capital of the bank to be licensed in the Republic.

In considering a proposal where ownership of a bank would rest in an unregulated non-financial group or a joint venture between natural persons and an unregulated non-financial group, the CBC has regard to the fact that any newly-formed bank, can be susceptible to early difficulties which may arise from lack of relevant expertise, or from ill-constructed and insufficiently tested business strategies.

The CBC may, therefore, grant a licence with restrictions. Examples of limitations are restrictions on:

- (a) the type of client that the proposed bank may deal with, for example limiting its activities to market counterparties and intermediate customers only;
- (b) the number of clients of any particular type that the proposed bank may deal with, either in absolute terms or on a roll-out basis related to the development of the proposed bank's systems; or
- (c) the specified investment activities which the proposed bank may carry on.

5. POSSIBLE REASONS FOR REFUSING TO GRANT A BANKING BUSINESS LICENCE

The CBC will only grant a licence if it is satisfied that all statutory eligibility criteria, as indicated above, are satisfied and all information, documents and reports requested as indicated in this Policy Statement, have been provided.

In summary, therefore, the CBC shall, in its discretion, reject an application, if, inter-alia:

- it has not been satisfied as to the suitability of the Applicant and/or its Controllers and/or the group to which it belongs;

- it has reasonable grounds to suspect money laundering or terrorist financing by the Applicant and/or any of its Controllers ;
- the information provided by any of the Applicant's Controllers, does not disclose clearly their identity and their business activities and, in the case of Controllers which are legal entities, the identity and business activities of persons having direct or indirect control over them, have not been stated clearly;
- the business plan submitted has not satisfied the CBC that the Applicant has clearly defined and adequately researched objectives, nor that the proposed operations are consistent with the Law and the CBC's licensing and prudential supervisory requirements.
- the information made available to the CBC, indicates that the activities and transactions carried out by the Applicant and/or by any of its Controllers, are such that the proposed bank may not be able to carry out its activities in accordance with legal provisions and with the requirements of prudent and sound banking practices;
- close links exist between the Applicant and other natural or legal persons, which may prevent the effective exercise of the CBC's supervisory function;
- the corporate structure of the group of which the Applicant is part, or its relationship with other undertakings under common control, is not clear and transparent and is such that may result in the CBC being unable to exercise effectively its supervisory responsibilities;
- the source of funds to be used for acquiring the participation in the share capital of the proposed bank cannot be clearly established;
- the Applicant and/or any of its Controllers, have not been transparent, open and cooperative in their dealings with the CBC or other regulatory authorities;
- some or all of the Controllers of the Applicant or the Applicant itself, are/is established in a jurisdiction which does not impose the mandatory holding of accounting records and/or publishing of financial statements, the

maintenance of shareholders' registers and/or which allows the preservation of anonymity regarding the identity of shareholders and persons charged with the management of the bank;

- it has not been satisfied as to the fitness and propriety of the Applicant's directors and managers;
- it has reasonable grounds to believe that there is no willingness and a capacity on the part of the Applicant to comply with its licensing and supervision requirements, on a continuous basis.
- the home supervisor of the parent bank seeking to establish a subsidiary/branch in the Republic does not, in the opinion of the CBC, exercise adequate supervision in accordance with internationally accepted minimum standards, including supervision on a consolidated basis;
- there is no legal basis, or possibilities of cooperation, for exchange of information with the parent bank's home supervisor;
- the parent bank and/or the group of which it forms part is/are incorporated in a country or territory considered by the Financial Action Task Force to be of "high risk" or "non cooperative" or more broadly in a country or territory that has not taken sufficient measures to comply with robust anti-money laundering and anti-terrorist financing procedures with internationally accepted standards.
- the consent of the parent bank's home supervisor has not been provided;
- the Applicant does not have sufficient technical means or financial and human resources for the type or volume of transactions which it intends to carry out in the Republic, and/or its activities are such that the stability or control of the proposed bank in Cyprus may be affected by the high risk of such activities.