**CENTRAL BANK OF CYPRUS**

**UNOFFICIAL TRANSLATION OF THE DIRECTIVES ISSUED TO CREDIT INSTITUTIONS FOR THE CREDIT GRANTING AND REVIEW PROCESSES (consolidated text)**

**AUGUST 2019**

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**DIRECTIVE ISSUED TO CREDIT INSTITUTIONS ON CREDIT GRANTING AND REVIEW PROCESSES**

**BUSINESS OF CREDIT INSTITUTIONS LAWS OF 1997 TO 2019**

**[66(I)/1997, 74(I)/1999, 94(Ι)/2000, 119(Ι)/2003, 4(Ι)/2004, 151(Ι)/2004, 231(Ι)/2004, 235(Ι)/ 2004, 20(Ι)/2005, 80(Ι)/2008, 100(I)/2009, 123(I)/2009, 27(I)/2011, 104(I)/2011, 107(I)/2012, 14(I)/2013, 87(I)/2013, 102(I)/2013, 141(I)/2013, 5(I)/2015, 26(Ι) of 2015, 35(Ι) of 2015, 71(Ι) of 2015, 93(Ι) of 2015, 109(Ι) of 2015, 152(Ι)/2015, 168(Ι)/2015, 21(I)/2016, 5(I) of 2017, 38(I) of 2017, 169(I) of 2017, 28(I) of 2018, 89(I) of 2018, 153(I) of 2018 and 80(I) of 2019]**

**Issued by virtue article 41**

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| 66(I) of 199774(I) of 199994(Ι) of 2000119(Ι) of 20034(Ι) of 2004151(Ι) of 2004231(Ι) of 2004235(Ι) of 200420(Ι) of 200580(Ι) of 2008100(I) of 2009123(I) of 200927(I) of 2011104(I) of 2011107(I) of 201214(I) of 201387(Ι) of 2013102(I) of 2013141(Ι) of 20135(Ι) of 201526(Ι) of 201535(Ι) of 201571(Ι) of 201593(I) of 2015 109(I) of 2015152(Ι) of 2015168(Ι) of 201521(I) of 20165(I) of 2017 38(I) of 2017 169(I) of 2017 28(I) of 2018 89(I) of 2018 153(I) of 2018 80(I) of 2019.  | The Central Bank of Cyprus, by virtue of the powers vested on it by section 41 of the Business of Credit Institutions Laws of 1997 to 2019, issues this Directive to Authorised Credit Institutions and to credit institutions that operate in the Republic under Section 10A of the Law. |
|  | **PART I - TITLE, SCOPE OF APPLICATION, PURPOSE AND INTERPRETATIONS** |
| Short title. | 1. This Directive will be referred to as the Credit Granting and Review Processes Directives of 2016 to 2019. |
| Scope. | 2. (1) The provisions of this Directive are applicable to all Authorised Credit Institutions and to credit institutions that operate in the Republic under Section 10A of the Business of Credit Institutions Laws of 1997 to 2016, which for the purpose of this Directive they are all referred to as credit institutions or CIs. |
|  | (1A) This Directive does not apply for credit agreements related to syndicated loans. |
|  | (2) This Directive does not replace the detailed credit policies and procedures that CIs are obliged to have in place in accordance with the “Guidelines on the management of credit risk” issued by the Central Bank of Cyprus on 25 July 2008. |
|  | (3) The Central Bank of Cyprus may require from a specific CI to apply stricter criteria where significant weaknesses exist. |
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| Purpose. | 1. The purpose of this Directive is:
 |
|  | (a) to prescribe best practices to be followed by the CIs during the processes of assessing applications for new and for reviewing existing performing credit facilities; |
|  | (b) to provide examples of the documentation that CIs should consider obtaining during the process of assessing the application for a new credit facility or reviewing existing performing credit facilities ,always applying the principle of proportionality having regard to the complexity and risk of each case and exercising judgment on the completeness and adequacy of the information which is readily available, and |
|  | (c) to incorporate therein the minimum requirements regarding the assessment of creditworthiness of borrowers as these are set out in the EBA Guidelines on creditworthiness assessment of 19 August 2015. |
|  |  |
| Definitions. | 4. (1) For the purposes of this Directive, the interpretations referred to in the Law must apply, unless the context otherwise requires.  |
|  | (2) Without prejudice to subparagraph (1), the following interpretations are applicable for the purposes of this Directive: |
|  | “annual percentage rate of charge” or “APRC” means the total cost of the credit to the borrower, calculated according to the methodology set out in Annex 1 (D); |
|  | “connected persons” has the meaning of “a group of connected clients” as this is defined in point (39) of article 4 of Regulation No. 575/2013/EE; |
|  | “credit analyst”means the officer of the CI who is authorised to carry out the assessment of the application for a new or of the renewal of an existing credit facility; |
|  | “credit facility” means the granting to a borrower of a loan or a current or overdraft account or financial guarantee and includes the discounting of a promissory note or of a bill of exchange for which the borrower is liable of either as a payee or as an endorser, the undertaking of financial responsibility or liability on behalf of a borrower, the undertaking of commitment for any of the above, including any of the above that is granted for the benefit of a third person with the guarantee of the borrower; |
|  | “durable medium” means any instrument which enables the user to store information addressed personally thereto in a way that will be accessible for future reference for a period of time that is adequate for the purposes of this information and which allows for the accurate retrieval of the information stored; |
|  | “European loan” means a credit facility subsidised by European funds; |
|  | “foreign currency loan” means, for the purposes of this directive, a credit agreement which is:  |
|  | (a) denominated in a currency other than that in which the borrower receives his income or holds the assets from which the credit facility is to be repaid, or |
|  | (b) denominated in a currency other than that of the country in which the borrower is resident, |
|  | Point (b) does not apply in cases of granting credit facilities to legal entities where the credit facility is denominated in the same currency as the currency in which the legal entity receives its income or holds the assets from which the credit facility is to be repaid;  |
|  | “gross exposure” means the sum of the funded and non-funded commitment; |
|  | “Law” means the Business of Credit Institutions Laws of 1997 to 2016; |
|  | “loan approving authority” means a committee or any persons of the credit institution that are authorised by the management body to approve the granting, the disbursement and the renewal of credit facilities; |
| Official Journal of the EU:L 124, 20.5.2003, p. 36 | “micro enterprise” has the meaning attributed to this term in paragraph 3 of Article 2, of the Annex to the Commission’s Recommendation of 6 May 2003 in relation to the definition of micro enterprise (2003/36/EC);  |
|  | “syndicated loan” means a type of lending where a group of credit institutions collectively provide one loan to one borrower. |
|  | **PART II – FUNDAMENTAL PRINCIPLES** |
| Fundamental principles. | 5. (1) The basic principle when assessing the granting of new and when reviewing a credit facility is the determination of the repayment capacity of the borrower. |
|  | 1. The value of collateral is not a decisive factor in the CI’s assessment of an application for a credit facility. Collateral may only serve as a secondary source of repayment and must be assessed as such.
 |
|  | 1. CIs must ensure that the level of own contribution by the applicant is satisfactory and reflects the level of risk of the credit facility.
 |
|  | **PART III - RESPONSIBILITY OF THE MANAGEMENT BODY** |
| Responsibility of the Management Body. | 6. The Management Body ensures that: |
|  | 1. the provisions laid down in this Directive are incorporated in the internal guidance, policies and procedures of the CI and that they are communicated to the relevant staff in a transparent and clear manner;
 |
|  | 1. sound processes are established to assess the borrower’s ability to meet obligations under existing and new credit agreements, that these processes are reviewed at regular intervals and that up-to-date records of those procedures are maintained;
 |
|  | 1. the policies and procedures for the monitoring of credit facilities are commensurate with the level and complexity of the credit facilities;
 |
|  | 1. staff involved in the credit granting and review processes is sufficient in terms of full time employment and adequately trained and experienced so as to duly apply the provisions of this Directive;
 |
|  | 1. the IT systems facilitate and support the effective implementation of the credit granting, monitoring and review processes as prescribed in the credit policies of the CI and in accordance with this Directive;
 |
|  | 1. the credit granting andreview policy and the implementation of the provisions of this Directive is part of the regular audit program of the internal audit department of the CI; and
 |
|  | 1. the implementation of the provisions of this Directive is part of the regular audit program of the external auditors of the CI.
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|  | **PART IV - INFORMATION PROVIDED AND COLLECTED BY THE CIs** |
| Pre-contractual information to applicants. Annex I. | 7. (1) Credit institutions must provide the applicant for a credit facility with all the necessary explanations regarding the characteristics and risks inherent in the credit facility, explain and provide the applicant and, where applicable the guarantors and collateral providers, with the information that is based, as appropriate and according to the principle of proportionality, on the data listed in the table of Annex I, except: |
| 106(Ι) of 2010176(Ι) of 201240(Ι) of 201350(Ι) of 2013.39(Ι) of 2001166(Ι) of 200134(Ι) of 200277(Ι) of 200233(Ι) of 200492(Ι) of 2007126(Ι) of 2009 107(Ι) of 2010. | (a) where credit facilities fall within the scope of the Consumer Credit Act of 2010 to (No 2) of 2013 or the Retail Mortgage Credit Agreements and Hire Purchase Law of 2001 to 2010, as amended, corrected or replaced, credit institutions shall comply with the provisions of these Laws using the forms that may be provided by these Laws; |
|  | (b) where the applicant for a credit facility is a legal entity that does not fall within the definition of a micro enterprise, credit institutions may proceed with a letter of offer, which contains all relevant information regarding the credit facility and the terms and conditions under which the credit facility will be granted; |
|  | (c) where the applicant for a credit facility is a legal entity that falls within the definition of a micro enterprise, credit institutions may proceed with the letter of offer, which contains all relevant information regarding the credit facility and the terms and conditions under which the credit facility will be granted, unless the applicant requests pre-contractual information; |
|  | (d) where a credit facility relates to a total amount of credit that does not exceed five thousand euro (€5.000), credit institutions may proceed with the letter of offer, which contains all relevant information regarding the credit facility and the terms and conditions under which the credit facility will be granted. |
|  | (3) For applicants who obtain pre-contractual information, a reflection period of ten (10) working days is granted which is calculated from the date the pre-contractual information the characteristics of which are the same as those in the binding offer is provided, so that the applicants are given the opportunity to compare the information received from various credit institutions and to thoroughly assess the obligations, risks and consequences of the new credit facilities they intend to obtain, in order to make an informed decision that they will be able to serve those credit facilities. |
|  | Provided that in case where the applicants are satisfied with the pre-contractual information received, they may inform the credit institution that they agree to proceed with the conclusion of the credit agreement for the credit facility applied for before the end of the ten (10) working day period. |
|  | (4) The provisions of this paragraph apply mutatis mutandis and in relation to the credit facility requested. |
| 197(Ι) of 20038(Ι) of 20047(Ι) of 2006 58(Ι) of 2015. | (5) In case personal guarantees are obtained, the CIs must inform the potential guarantors that their responsibilities emanating under their guarantee are exactly the same as those of the borrower. This information must be given along with the information required according to The Protection of a Specific Category of Guarantors Laws of 2003 to 2015. |
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| Letter of offer. | 8. (1) For applicants who receive pre-contractual information, who have decided to proceed with the conclusion of the credit agreement, the credit institution then provides a letter of offer that is binding on the credit institution. The letter of offer is provided on paper or on another durable medium. |
|  | (2) Where the characteristics of the offer are different from those of the pre-contractual information previously provided to the applicant, the credit institution either: |
|  | 1. provides the pre-contractual information again, or
 |
|  | 1. indicates to the applicant the differences between the pre-contractual information and the letter of offer.
 |
|  | (3) Credit institutions specify on the letter of offer the period for which the offer is valid and in case pre-contractual information, the characteristics of which are the same as those of the letter of offer, was not previously provided, grant a reflection period of at least five (5) working days before the conclusion of the credit agreement. |
|  | It is provided that the borrower may accept the offer and conclude the contract for the requested credit facility at any time during the reflection period of five (5) working days. |
|  | (4) The CIs must specify on the letter of offer that in case the applicant accepts the offer, the period granted to the applicant for exercising the right of withdrawal after the conclusion of the credit agreement.  |
|  | Provided that the credit facility is not activated before the expiry of the withdrawal period or before the exercise of the right of withdrawal, whichever comes first. |
| Obtaining adequate information for credit granting and review. | 9. (1) (a) For both the credit granting and review processes, CIs must collect adequate information and documentation in order to evaluate the income of the applicant / borrower, to assess the ability to repay the new and existing credit facilities, to assess the value of the collateral, where applicable, and, with regard to new credit facilities, to verify the purpose and to properly assess the new risks undertaken.  |
|  | * + - 1. In deciding on the extent of the documentation and information to be requested from applicants and borrowers, for the purposes of subparagraph (a), the credit analyst must always exercise judgment having due regard to the complexity of each case, the assessed risks and the adequacy of information and documentation already available.
 |
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| Annex II | (2) The financial information and documents referred to in subparagraph (1) that may be relied upon to provide evidence of the income and repayment capacity of the applicant / borrower and which may be requested directly from the applicant / borrower, could include those set out in Annex II. |
|  |  |
|  | (3) CIs must obtain from the Mechanism for the Exchange, Collection and Provision of Data, which is set up in accordance with the provisions of the Law, the following data with regard to credit facilities that the applicant or borrower enjoys from other third parties: |
|  | 1. Original amount or limits of credit facilities, as applicable.
 |
|  | 1. Current balance.
 |
|  | 1. Duration and dates of maturity of the credit facilities.
 |
|  | 1. Installment amounts, installment payment frequency and grace period, if any.
 |
|  | e. Amounts and days in arrears, if any. |
|  | f. Collaterals, if applicable. |
|  | (4) The credit analysts must obtain information from any other source that could be useful for the assessment of the repayment capacity of the applicant / borrower, including the following: |
|  | 1. Information from the local market;
 |
|  | 1. Information from the Central Information Register for the Issuers of Dishonoured Cheques (CIR).
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|  | **PART V - ASSESSMENT OF APPLICATION FOR CREDIT FACILITIES**  |
| Verification of the borrower’s income. | 10. (1) When assessing a borrower's prospect to meet the obligation under the credit agreement, the CI must make reasonable enquiries and take reasonable steps to verify the borrower's underlying income capacity, the borrower’s income history and any variability over time. |
|  | (2) In the case of borrowers that are self-employed or that have seasonal or other irregular income, the CI must make reasonable enquiries and take reasonable steps to verify information that is related to the borrower's ability to meet the obligations under the credit agreement. |
|  |  |
| Documentation and retention of information. | 11.(1) The CI must maintain complete documentation of the information that leads to credit approval and must maintain this documentation for at least the duration of the credit agreement. |
|  | (2) The CI must ensure that a record with an adequate explanation of the verification of income and assessment of repayment capacity is readily available to the Central Bank.  |
|  |  |
| Identification and prevention of misrepresented information. | 12. To reliably carry out creditworthiness assessments, the CI must design loan documentation requirements in a way that helps to identify and to prevent misrepresentation of information by the borrower and by staff of the CI that is involved with the assessment of the application. |
| Assessment of repayment capacity. | 13. For the purpose of assessing the repayment ability of applicants, natural and legal persons, CIs follow, as appropriate the process outlined in Annex III. |
|  |  |
| Assessment of collateral. | 14. (1) (a) The ability to repay a credit facility is the main criterion for deciding for any new funding. When assessing the applicant’s ability to repay the credit facilities, the CI must place emphasis on applicant’s current income and future cash flows and not on available collateral.  |
|  | (b) Collateral by itself must not under any circumstance be a criterion for approving a credit facility and cannot by itself justify the approval of any credit facility. Collateral must only be considered as the CI’s second way out in case of default and not as the primary source of repayment.  |
|  | (2) Credit facilities are only collateralised as a safety net in case of future adverse deviations in the servicing ability of borrowers.  |
|  | (3) CI’s must ensure that: |
|  | 1. each collateral is obtained exclusively for the purpose of collateralising specified credit facilities;
 |
|  | 1. in no case should any collateral be used to cover “all present and future” obligations of the borrower whether these derive from other credit facilities granted to that borrower or from credit facilities guaranteed by the borrower and
 |
|  | 1. Upon settlement of the secured credit facility, the relevant collateral must be immediately released and a clean title delivered to the borrower or holder of the collateral.
 |
|  | (4) CI’s must specify in their credit policy the level and type of collateral that is appropriate to be required for different types of credit facilities. |
|  | (5) CIs must include in their credit policies adequate guidance of how to assess the value of collateral of assets pledged to several CIs. Such policies must ensure that the value assigned to such collateral is prudently assessed, is based on the provisions relating to ranking priorities, takes into account the total level of credit facilities to all CIs concerned, and that there are safeguards for not double counting.  |
|  | (6) In case the credit facility is denominated in foreign currency, the CI, where applicable, must register the charge in the same currency as the credit facility.  |
|  | (7) A registration of a floating charge on company’s assets, which is especially appropriate in cases of the finance of the working capital of the company, must be commensurate to the level of borrowing. |
|  |  |
| Pricing of a new credit facility. | 15. The pricing of a new credit facility must reflect funding cost, legal and administrative cost, cost of capital, credit risk, liquidity risk and any other real costs of the CI.  |
|  |  |
| Disbursement process. | 16. CIs must ensure that appropriate controls are in place to ensure that all conditions laid down in the credit facility approval are met prior to any disbursement. Furthermore, it must ensure that: |
|  | * + - * 1. Subject to the principle of proportionality, there is adequate segregation of duties and responsibilities between staff involved in the Loan documentation, Loan disbursement and Loan approval processes.
 |
|  | * + - * 1. The Loan agreement / contract is prepared in accordance with the terms of approval and the letter of offer given to the applicant and is duly signed by the applicant, and where applicable, the guarantor and the collateral provider in the presence of the CI’s authorised signatories who will sign as witnesses to the above signatures.
 |
|  | (c) All other documents required (for example mortgage documents, property insurance, cash collateral pledging) are checked for full compliance with the Loan approval conditions, are completed and duly signed by all the involved parties before the disbursement of the credit facility; |
|  | 1. In case of a credit facility with partial disbursements then the relevant provisions of this directive must be applied.
 |
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|  | **PART VI REVIEW OF EXISTING CREDIT FACILITIES** |
| Reassessment of repayment ability. | 17. (1) (a) CIs must review credit facilities on a regular basis, depending on the level of risk of the borrower and the industry in which it operates.  |
|  | (b) CIs may use automated processes for the review of the accounts of natural persons with regular cash inflows in their accounts. |
|  | (c) In the case of borrowers that are legal entities, depending on the CI’s assessment of the complexity and the risks involved, a review shall be carried out every year. |
|  | (d) In the case of natural persons with no regular inflows in their accounts, the review should indicatively be carried out as follows: |
|  | (i) every two years for natural persons with gross exposure equal to or over three hundred thousand Euro (€ 300.000); and  |
|  | (ii) every three (3) years for natural persons with gross exposure less than three hundred thousand Euro (€ 300.000). |
|  | (2) (a) CIs must inform the borrower of the upcoming review process and provide a reasonable deadline for the submission of relevant documentation. |
|  |  (b) CIs must ensure that the depth of the review should be commensurate to the type of the borrower, the risk level and the total amount of the borrower’s credit facilities. |
|  | (3) During the review process the CIs must reassess the borrower's ability to repay credit facilities to the CI and to other CIs, taking into account other non-banking obligations and commitments, e.g. taxation; For this purpose and depending on the level of risk of the borrower, the past performance and prospects of the industry where it operates, CIs shall: |
|  | (a) in accordance with the provisions of paragraph 9(1), obtain updated information relating to the borrower, such as demographics, financial, tax and business information as well as information of any problems encountered by the borrower;  |
|  | (b) analyse the financial information obtained and update the borrower’s credit rating; and  |
| Official Journal of the EU: L176, 27.06.2013, p.0001-0337. | (c) where applicable review the value of the collateral relating to the borrower’s credit facility in accordance with paragraph 14 and comply with the provisions of article 208 of Regulation 575/2013/EE. |
|  | (4) In case the borrower is a member of a group of Connected Persons, the CI must review the credit facilities of the whole group. |
| Annex ΙΙΙ(Ι) N.4862, 03.04.2015, R.A.A.107/2015 | (5)(a) The review process laid down in this paragraph applies to borrowers with credit facilities that do not present excesses or arrears. The review process of borrowers with facilities presenting excesses / arrears is governed by the provisions of the Directive on Arrears Management of 2015. |
|  | (b) In the case of borrowers who fall within the scope of the Code of Conduct that is annexed to the Arrears Management Directive, the credit facilities must be reviewed and the required financial information must be updated in accordance with the time plan provided for in the Code of Conduct. |
| Monitoring of values of collaterals. | 18. CIs must regularly monitor the values of collateral held. In cases of monitoring collateral value of performing loans, such monitoring does not burden borrowers by any means.  |
|  | 1. In the case of mortgages over immovable property, CIs must monitor the “Loan to Value” ratio (LTV) that is defined as the ratio of:
 |
|  |  x100% |
|  | In calculating the LTV the following is taken into account: |
|  | 1. CIs may use the Property Price Index developed by the CBC for the monitoring of the value of residential and commercial properties.
 |
|  | 1. Revaluations of properties, when deemed necessary inaccordance with the provisions of article 208 of Regulation 575/2013/EE, may be carried out by independent valuers or by a department of the CI that is independent from the credit decision process. In both cases, the valuers must possess the necessary qualifications, ability and experience to execute the valuation.
 |
|  | 1. In case of projects under construction, monitoring must include:
 |
|  | * + The up to date cost of construction where the property value to be used in calculating the LTV is the open market value of the land plus the cost of construction to date;
 |
|  | * + The (revised) estimated cost of completion where the property value to be used in calculating the LTV is the open market value of the land plus the cost of construction to date plus the estimated remaining cost to completion;
 |
|  | * + the open market value of the project at the stage of construction; and
 |
|  | * + the estimated open market value upon the completion of construction works of the property.
 |
|  |  iv) The calculation of the cost of construction does not include transfer fees, mortgage fees, advertising costs, administrative costs and other similar costs. |
|  |  v) In the case of a mortgage by a borrower that purchases property under development, the value to be used for calculating LTV during the monitoring process is the estimated open market value of the purchased property if sold at the current stage of construction.  |
|  |  |
|  | **PART VII - SPECIAL LENDING CASES** |
| Lending in foreign currency. | 19. (1) CIs must provide borrowers with adequate information regarding the risks involved in foreign currency lending. Such information must be sufficient to enable borrowers to take well-informed and prudent decisions and must at least encompass the impact on installments due to fluctuations of exchange rates or of a severe depreciation of the currency of the borrower’s income.  |
|  | (2) In case of foreign currency lending, CIs must examine and evaluate the additional credit risk involved as well as additional risks inherent in foreign currency lending including, but not limited to, the risks of fluctuation of the exchange rate and of increase of the interest rates as well as to the country risk.  |
|  | (3) (a) Where a credit facility relates to a foreign currency loan, the borrower has a right, under conditions that are specified in the credit agreement, to convert the credit facility into an alternative currency which must be a currency that the credit institution trades with and which is either: |
|  | 1. the currency in which the borrower primarily receives income or holds assets from which the credit is to be repaid, as indicated at the time the most recent creditworthiness assessment in relation to the credit facility was made; or
 |
|  | ii) the currency of the country in which the borrower either was resident at the time the credit facility was granted or is currently resident. |
|  | (b) The exchange rate at which the conversion is carried out for the purposes of subparagraph (a) is the market exchange rate applicable on the day of application for conversion ,unless otherwise specified in the credit agreement. |
|  | * + - 1. In case where the loan of a borrower is denominated in a foreign currency, the CI must warn in writing the borrower on a regular basis , at least where the value of the total outstanding amount repayable by the borrower or where the regular instalments payable by the borrower, varies by more than 20%, compared to what it would have been, had the exchange rate of the currency in which the loan agreement was concluded and the currency in which the borrower receives his income or holds his assets from which the loan will be repaid, remained the same as that which was applicable at the time of the conclusion of the credit agreement. The warning must inform the borrower of a rise in the total amount payable by the borrower, set out the right to convert to an alternative currency and the conditions for doing so and explain any other applicable mechanism for limiting the exchange rate risk to which the borrower is exposed.
 |
|  | (d) CIs must disclose the arrangements applicable under this paragraph to the borrower in the letter of offer and in the credit agreement. Where there is no provision in the credit agreement to limit the exchange rate risk to which the borrower is exposed to a fluctuation in the exchange rate of less than 20%, the letter of offer must include an illustrative example of the impact of a 20% fluctuation in the exchange rate. |
|  | 1. CIs must establish an adequate IT system for the purposes of sub-paragraph (c) and for the support of regular monitoring of foreign exchange risk. CIs that do not have appropriate and reliable monitoring tools may not grant credit facilities in foreign currency.
 |
|  | (4) In case of lending in foreign currency, the CIs must encourage the borrowers to obtain advice on hedging against foreign currency risk. |
|  | (5) Products offered in foreign currency, if appropriate, must also be offered in Euro.  |
|  |  |
| Grace period. | 20. (1) Grace period may only be granted in very exceptional cases.(2) CIs must meticulously justify the cases where the repayment programme of a credit facility includes a grace period. |
|  |  |
|  | (3) Grace period must, in general, not exceed twelve (12) months, except in cases of projects with construction period that lasts over twenty four (24) months. In such a case, grace period must not exceed the construction period. |
|  | (4) CIs must include appropriate terms and conditions in the loan contract that clearly lay down the proportion of the sales proceeds that may be allocated to construction cost as, own contribution, and the proportion that is used for repayment of loans.  |
|  |  |
| Specialised lending. | 21. (1) Specialised credit facilities such as shipping loans and syndicated loans, entail high risk and thus require handling by an adequate number of staff with the appropriate experience, qualifications and expertise to deal with such lending.  |
|  | (2) CIs must establish sound credit policies for the assessment and approval of specialised lending which must provide at least for the following: |
|  | 1. assessment whether the prevailing market conditions are favourable for such lending,
 |
|  | 1. assessment of macro-economic factors,
 |
|  | 1. requirements for on-going monitoring,
2. the use of an adequate IT system and analytical tools, and
 |
|  | 1. establishment of an appropriate MIS.
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|  | 1. The basis for the calculation of the interest rate of a European loan may be the same as the basis for the calculation of the interest rate of the corresponding European fund.
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|  | **PART VIII - PROCEDURES OF FINANCING IMMOVABLE PROPERTY AND LAND DEVELOPMENT** |
| Lending to purchasers of immovable property from developers.Annex V | 22. In order to safeguard that the proceeds of a loan granted to a borrower for the purchase of immovable property from a developer, are utilised for the repayment of the credit facility granted to the developer for the specific project, CIs must follow the procedure that is set out in Annex V.  |
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| Credit policies for lending to developers.Annex VI | 23. CIs must implement sound and robust credit policies regarding lending to developers or project finance that support the granting, disbursement and monitoring stages. Annex VI lays down the basic requirements that these credit policies must include. |
|  | **PART IX - VALUERS AND VALUATION REPORT** |
| Valuers criteria. | 24. (a) CIs must maintain a properly approved panel of valuers using appropriate selection criteria. CIs must carry out an ongoing assessment of the performance of the valuers and decide whether each valuer remains or not in the panel. |
|  | (b) CIs must annually review whether the valuers included on the panel have adequate and valid professional indemnity insurance. |
|  | (c) The immovable property must be valued by an independent valuer listed in CI’s approved panel of valuers and the CI must require valuers to disclose whether they are connected to either the buyer or the seller of the property and whether they have any interest in the valuation of this property before accepting the engagement. |
|  | (d) CIs must set a limit on the valuations to be performed by each valuer or firm of valuers.  |
| Annex VII. | (e) CIs must have a clear policy and lay down the procedures regarding the assignment of valuations to valuers and the assessment of the valuation. Annex VII lays down the main procedures relating to the assignment and assessment of valuations. |
|  | **PART X - BEST PRACTICES** |
| Governance. | 25. CIs shall endeavor to adhere at least to the following sound governance requirements when undertaking credit risk:  |
|  | (a) Applying the principle of proportionality, CIs must ensure that there is segregation of duties among the staff involved in the loan granting process. Especially, credit analysts must not have any approving authority.  |
|  | 1. The targets must focus on credit quality rather than on loan expansion and in no case should any target on loan expansion apply to the loan approving authorities.
 |
|  | 1. CIs must avoid approving any excesses to overdraft accounts, instead, they may examine the approval of temporary limits which must then be entered in the CIs’ computerised systems; approvals for temporary limits must be fully justified and their repayment must be closely monitored.
 |
|  | 1. CIs must monitor the operation of overdraft accounts and if an overdraft account presents hardcore borrowing, this must be converted to a loan with a regular repayment programme.
 |
|  | **PART XI - SPECIAL PROVISIONS** |
| Exceptions policy. | 26. CIs must specify in their credit policy whether they may examine and approve any credit facility that does not align with the credit facilities that are granted under the approved credit policies of the CI. In case the CI adopts this approach, then it must include it in its credit policy and follow an “Exception to Policy” process, for example, granting of a housing Loan to a borrower without regular income, but with substantial irregular cash inflows. CIs must establish detailed procedures and limits for "Exception to Policy" in order to allow such exceptions only to the extent that they are prudent and have received explicit and justified approval by the appropriate approving authority, but in no case should such exception introduce a loophole in the lending policy of the CI. |
| Automated processes. | 27. The use of automated processes for certain retail products such as credit cards, may help to minimise operational cost and are not precluded by the provisions of this Directive. However, CIs must ensure that these processes lead to consistent and high quality credit assessment and approval decisions. In cases of automated processes, CIs must put in place criteria for automated identification of triggering of credit events, servicing as early warning signals, to be duly investigated by the relevant credit officers. |
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|  | **PART XII - FINAL PROVISIONS** |
| Repealing of existing Directive. | 28. The Directive on Loan Origination and Review Processes of 2013 is hereby cancelled. |
| Entry into force. | 29. (1) Subject to the provisions of subparagraph (2), this Directive shall enter into force from the date of its publication in the Official Gazette of the Republic. |
|  | (2) The method of calculation of interest on the basis of 365/365 days (366/366 days for leap years) in relation to credit facilities that do not fall within the definition of consumer as the term «consumer» is defined in relevant legislation, shall apply for new credit facilities with effect from 1 April, 2016. |
|  | (3) The Central Bank may grant, where it deems necessary, a transitional period for the compliance with a specific provision of this Directive. |

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| **Annex I** – Pre - contractual Information - *See separate document* |
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| **Annex II – Financial Information to be obtained from applicants**

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| **A. Financial information** |
| The following financial information may be requested directly from the applicant / borrower and may be relied upon to provide evidence of the income and repayment capacity of the applicant / borrower in accordance with paragraph 9: |
|  |
|  (a) Natural persons - employees |
| * + 1. Original salary slips for the last three (3) months and
 |
| * + 1. Documents supporting any other type of steady income, for example alimony income, interest income, income from immovable property, income from welfare benefits.
 |
|  |
| (b) Self-employed natural persons: |
| * + 1. confirmation of income by the applicant’s accountant or auditor, or
 |
| * + 1. social insurance statement;
 |
| * + 1. if registered for VAT, a copy of VAT statements submitted since last balance sheet date,
 |
| * + 1. documents supporting any other type of income and
		2. tax declaration.
 |
|  |
| (c) Legal entities: |
| i) Audited financial accounts for the last three (3) financial years. In case the applicant has no audited financial accounts for the last financial year, then unaudited financial accounts must be provided for that year. |
| ii) The financial accounts as at the end of the relevant quarter of the current year for listed legal entities. |
| * + 1. The management accounts, as at the end of the relevant quarter of the current year for non-listed legal entities.
 |
| * + 1. Original of income tax clearance for the last two years (2) available.
 |
| * + 1. Copy of Value Added Tax (VAT) statements submitted since last balance sheet date, if registered.
 |
| * + 1. A business plan with budgeted cash flows for the life of the project financed, if applicable, and at least for the next two (2) years for other cases, in all cases based on reasonable assumptions, including likely and stress scenarios, verified by accountants / auditors.
 |
| * + 1. Where applicable, details of projected income to be generated by the use of the requested Loan, supporting that this Loan will add to the profitability and enhance the cash flow of the business; for example, if borrowing will be used for the purchase of a new site or a new piece of equipment or raw materials.
 |
|  |
| (d) Project finance: |
| In case of project finance, a feasibility study, prepared by qualified professionals as appropriate, of the project which must include as a minimum: |
| i) A profitability study of the project; |
| * + 1. Cost analysis by a quantity surveyor;
 |
| * + 1. A business plan;
 |
| * + 1. Future forecast with analysis of the assumptions and
 |
| * + 1. Sensitivity and worst case scenario analysis with respect to both cost and income.
 |
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| **B. Supplementary information** |
| CIs must request the following documents from applicants, as appropriate: |
| (a) An application form that is fully completed and duly signed by the applicant in the presence of staff of the CI who sign as witnesses to the signature of the applicant;  |
| (b) Documents that substantiate the Loan purpose, for example written offer or proforma invoices or purchase agreement contract;  |
| (c) In relation to applications for credit facilities for the purchase or construction of immovable property: |
| (i) Proof of down-payment, if applicable;. |
| (ii) Letter of intent of release of mortgage by current owner and letter of intent of Consent of mortgagee CI, if applicable; |
| (iii) (a) For the property to be financed, the CI must ensure that the following documents are submitted the latest before the first disbursement from the approved loan: |
| * + - 1. Title deed of current owner.
 |
| * + - 1. Building permit.
 |
| * + - 1. Planning permit.
 |
| * + - 1. Letter of release of mortgage by current owner and Consent of mortgagee CI, if applicable.
 |
| (b) In case where the property to be mortgaged is different from the property to be financed the CI must ensure that the title deed is submitted the latest before the first disbursement from the approved loan.(iv) In case of construction or completion of construction or renovation of immovable property, a detailed cost analysis and time plan signed by a professional quantity surveyor or other qualified professional, as appropriate. In case of renovation or repairs for estimated total costs that do not exceed €75.000 where a quantity surveyor or other qualified professional is not employed, the original invoices and payment receipts must be submitted by the applicant. The CI must make disbursements only on the basis of this documentation. |
|  |
| **C. Collateral Information** |
|  (1) When the CI obtains collateral over immovable property, then the CI : |
| (a) Obtains a valuation of the immovable property that is carried out by a valuer who is independent of the applicant and who must comply with the provisions of Part IX;  |
| (b) Carefully and thoroughly examines the valuation report of the property, and ensures that all factors affecting the value of the property are adequately considered;  |
| (c) in case the collateral is a property other than the one to be financed, requires a valuation report for both properties;  |
| (d) ensures that the property is properly insured and the insurance contract is assigned to the CI for the purpose of the credit facility; and |
| (e) in the case of a property under construction, requires that a contractor all risk insurance, to cover all the construction period of the project, is made and assigned to the CI for the purpose of the credit facility. |
| (2)(a) When a CI registers a floating charge over the assets of a company, it must obtain an insurance contract where the assets under the floating charge are properly insured and must ensure that the insurance contract is assigned in favour of the CI.  |
| (b) In case of registration of multiple floating charges by multiple CIs, the insurance contract must clearly indicate that it is assigned in favour of all CIs in the proportion of the amounts of the floating charges and in the same ranking priority as the registrations. |
| (3) In cases where personal guarantees are obtained, CIs must collect the documents mentioned in Part A depending on whether the Guarantor is a natural person or a legal entity.  |

**Annex IIΙ – Assessment of Application for Credit Facilities**(Paragraph 13)

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| **A. Application Assessment**When assessing the repayment ability of applicants CIs should : |
| * + - 1. (a) Assess the completeness of the financial information submitted by the applicant and
 |
| (b) Critically assess the reasonableness of the data presented in the financial information submitted by the applicant. |
| (2)(a) The credit analysts have the responsibility of performing a thorough assessment of the financial situation of the applicant and to clearly justify their proposal to approve or decline the application for granting credit facilities. |
|  (b) The credit analysts and the credit approving authority must take into account the CI’s credit policy and especially the CI’s risk appetite, concentration limits and diversification efforts, and the relevant directives and circulars issued by the Central Bank. |
| (c) The credit analysts and the credit approving authority, when assessing a credit application must: |
| i) examine the applicant’s income, future cash flows, and source of repayment in order to evaluate the applicant’s ability to repay: |
| * 1. In case the applicant is a member of a group of Connected Persons, the assessment must also be carried out at group level, especially where reliance for repayment is placed on cash flows emanating from other connected parties in order to avoid the situation in which a viable group becomes a non-viable group by reason of granting the new credit facility;
 |
| b. The CIs must ensure that the borrower’s ability to meet loan obligations is not based on an expected significant increase in the borrower’s income unless there is sufficient evidence. In this context, they may only consider estimated future cash flows when there are available, reliable and reasonable assumptions. |
| ii) assess the applicant’s financial position and, where applicable, financial indicators, for example leverage ratio and cost to income ratio,  |
| iii) calculate the applicant’s scoring / rating, where applicable, |
| iv) in case the credit facility will be used for financing the purchase of an asset, assess whether the credit facility can be repaid over the useful life of the asset financed; |
| v) have due regard to the prevailing market conditions and their estimated impact on the industry segment in which the applicant operates and on the applicant’s own financial situation; |
| vi) evaluate other qualitative elements such as, an assessment of the applicant’s corporate governance including dividend policy, compliance with the audit requirements for financial accounts and compliance with tax obligations. |
| (3) The credit analysts must include in their proposal a full analysis of the applicant’s repayment ability and in case of a positive recommendation this must be fully justified. |
| (4) The credit approving authority must fully justify their decision to approve or decline an application. |
|  |
| **B. Debt servicing amount** CIs must calculate the total debt servicing amount for each borrower as follows: |
| i) Debt servicing amount is defined as the installment amount of the credit facility to be granted plus all other installments (Loan installment, overdraft and credit card installment) of existing credit facilities with the same and with other CIs. |
| ii) The overdraft servicing amount is calculated as the overdraft limit multiplied by the interest rate charged divided by twelve (12). |
| iii) The credit card installment amount is calculated as the credit card limit multiplied by the interest rate and divided by twelve (12). |
| iv) The debt servicing amount must be adjusted by using the long term average relevant interest rates for variable interest rate loans to enable the repayment assessment when interest rates fluctuate. |
|  |
| **C. Repayment ability of natural persons**CIs must calculate the *“Total Monthly Income”* on the basis of the calculations presented on the excel worksheet entitled “Personal Financial Statement (PFS)” which is annexed to this Directive as Appendix IV. |
| 1. In the case of self-employed / freelancers who have no monthly salary, CIs must calculate the annual income using the PFS and divide it by twelve (12) for the purpose of computing the total monthly income.
 |
| 1. CIs must verify borrower’s total monthly income presented on the PFS to the documents submitted under paragraph9. Income such as interest income, alimony and any other income such as overtime, bonuses and other exceptional income may only be taken into consideration, after the CI has confirmed and verified to its full satisfaction that it is steady and recurring.
 |
| 1. If the loan term extends past the borrower’s expected retirement age, the CI should take appropriate account of the adequacy of the borrower’s likely income and ability to continue to meet loan obligations in retirement.
 |
| 1. In case where loan installments are gradually increasing, then CIs must assess repayment ability on the corresponding estimated future income.
 |
| 1. CIs must assess the reasonableness of the net disposable income.
	* + - 1. In assessing the repayment ability of the applicant, the total debt servicing amount should be limited to 80% of the Net Disposable Income.
				2. In the case of loans in foreign currency, the total debt servicing amount should be limited to 65% of the Net Disposable Income.
 |
| The Net Disposable Income is calculated as the difference between the “Total Monthly Income” and the “Total Monthly Expenditure” presented in column “Average Monthly Charge” –on the PFS. |
| CIs must verify, on a best effort basis, that the information presented on the excel worksheet “Section C - Expenditure” of the PFS is as accurate as possible. For this purpose CIs must: |
| (i) take into account relevant factors that could influence the borrower’s ability to meet loan obligations, without inducing undue hardship and over-indebtedness. These factors may include on a best effort basis other servicing obligations, their interest rates, and the outstanding principal on such debt, evidence of any missed payments, as well as directly relevant taxes and insurance; |
|  make reasonable allowances for committed and other non-discretionary expenditures, such as the borrower‘s actual obligations, including consideration of the living expenses of the borrower and |
| make prudent allowances for potential negative scenarios in the future, including for example, a reduced income in retirement; an increase in benchmark interest rates in the case of variable rate mortgages; negative amortisation, balloon payments, or deferred payments of principal or interest. |
| (8)(a) In cases where the debtor of a credit facility is more than one, the debt servicing amount is the total of the debt servicing amounts of all debtors on the credit facility. |
| (b) In the case where the co-debtor is the spouse, the assessment of repayment ability and the calculation of the debt servicing amount must take into account the total income and expenditure of the household and for this purpose a single PFS may be completed by the spouses. |
|  |
| **D. Repayment ability of legal entities** For the purpose of assessing the repayment ability of legal entities, CIs examine all the financial data collected from the applicant and obtained by the CI and in particular:  |
| (1) (a) When carrying out the assessment procedure, CIs must carefully examine, challenge and, if possible, verify the sources of repayment as these are presented on the documentation submitted by the applicant. |
| (b) In the case of new projects, CIs must critically assess the reasonableness of the assumptions and estimates of cash flow forecasts before placing reliance on them for the purpose of assessing repayment capacity. |
| (c) Projected cash flows must be compared with data from previous periods as depicted in borrower’s audited financial accounts. In cases where borrower’s predictions for future cash flows deviate substantially from the actual figures to date, then these predictions must be supported by reasonable evidence and realistic assumptions. |
|  |
| (2)(a) CIs compute the debt servicing amount of the borrower in order to estimate whether the borrower will be in a position to service the new and existing credit facilities.  |
| * + - * 1. The debt servicing amount must be calculated, on a best effort basis, for the whole term of the credit facility, on the basis of the projected cash flows.
 |
|  |
| (3) (a) CIs must incorporate requirements for scenario analysis in their credit policy and they must outline a range of scenaria that may be appropriate for different cases. |
| (b) CIs must carry out different scenario analysis in order to assess the repayment capacity of the borrower and take into account their impact during the decision making process.  |
| (c) The scenarios must include inter alia, the following: |
| i) The impact on the debt servicing amount due to an increase in the basic interest rate, such as assuming that interest rates move towards their long term average level; |
| * + 1. A fall in the estimated cash flow generating capacity of the applicant, under the most probable and worst case scenaria combining all the adverse effects;
		2. The impact on the debt servicing amount due to an adverse change in the exchange rate of at least 20%;
 |
| * + 1. In the case of project finance, simultaneous fall in estimated sales proceeds and increase in estimated costs of construction, under the most probable and worst case scenaria combining all the adverse effects.
 |
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**Annex IV – Personal Financial Statement (PFS)** - *See separate document***Annex V - Lending to purchasers of immovable property from developers**

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| 1. If the purchaser and the developer are borrowers of the same CI: |
| (a) the CI must credit the funds from the loan granted to the purchaser in the loan account that relates to the specific project of the developer; |
| (b) the CI must provide confirmation of this transaction to the purchaser and must keep a copy in the credit files of the developer. |
| 2. If the purchaser and the developer are not borrowers of the same CI: |
| (a) the CI of the developer must inform the CI of the purchaser of the loan account of the developer that relates to the project and which is secured by a mortgage on the property purchased by the borrower. |
| (b)the CI granting the loan to the purchaser must transfer each amount disbursed from the purchaser’s loan account, either by wire transfer or by a bank draft, to the account of the developer as indicated by the CI of the developer; |
|  |
| 3. In case of wire transfer, the CI of the purchaser must state details of payment in the name of the purchaser, the name of the developer, the account number of the developer’s loan and details of the project. In case a bank draft is issued, the CI must accompany the draft with a letter stating the name of the purchaser, the name of the developer, the account number of the developer’s loan to be credited and details of the project. |
| 4. The CI of the developer after receiving the wire transfer / bank draft must inform the purchaser and the CI of the purchaser by a letter confirming that the said amount has been credited to the Mortgage Loan account of the developer from which the specific project was financed. The CI of the purchaser must keep this letter in the purchaser’s credit file together with a copy of the wire transfer or bank draft. |

**Annex VI – Minimum requirements for the assessment of the industry**

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| **1. Minimum requirements for the assessment of the industry** |
| (a) a description of the risks entailed in these types of financing; |
| (b) examination and evaluation by the risk management committee of the prevailing market conditions and whether these are favourable for this type of development; |
| (c) the assessment by the risk management committee of the macro-economic factors that may affect the market conditions in the short, medium and longer term; |
| (d) the risk management committee must elaborate and explain to all Loan Approving Authorities and staff engaged in the assessment of granting credit facilities to developers, the assessments provided for in items (a) to (c).  |
|  |
| **2. Minimum operational requirements**  |
| CIs must ensure that : |
| * + - * 1. staff engaged in the assessment of granting credit facilities to developers has the appropriate experience, qualifications and expertise to deal with such lending;
 |
| * + - * 1. there are procedures for engaging with the Quantity Surveyor of the borrower and that these require a report laying down the following information:
 |
| (i) The estimated total duration of the construction. |
|  (ii) The estimated duration of each stage of construction or phase of the project. |
| (iii) Estimate of the analytical cost of the project. |
| * + - * 1. disbursements from the loan may only be made upon applications by borrowers which must be accompanied by a work in progress certificate prepared by the Quantity Surveyor.
 |
| (d) the appropriate approving authority examines the following before taking a decision to approve each disbursement: |
| (i) Borrower’s own contribution is made according to the terms of the loan agreement; |
| (ii) the proceeds of up-to-date disbursements were utilised for the purpose of the project and in accordance with the certificate of the cost of completion prepared by the Quantity Surveyor and verified by the borrower’s accountant;  |
| (iii) a comparison of the cost of the completed stage to the budgeted cost up to that stage as prepared by the Quantity Surveyor and verified by the borrower’s accountant with justification for any deviations and explanations of the method of their financing;  |
| (iv) the reasonableness of the proposed method of finance of any cost overruns and an assessment of the resulting profitability and viability of the project in order to enable the taking of immediate remedial actions;  |
| (v) that Loan disbursements do not cover cost overruns mainly in order to avoid a situation where the Loan is fully disbursed but the project is not completed.  |
| (e) there is evidence of close monitoring of the progress of sales of the project as well as of related receivables and that all sales proceeds are credited to the loan account of the project financed; |
| (f) there is an MIS system that facilitates and supports the monitoring of the rate of completion of the construction compared to the different deadlines set out in the time plan provided by the Quantity Surveyor.  |

**Annex VII – Valuation report**

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| CIs procedures relating to the assignment and assessment of valuations may include the following: |
| (a)Valuation instructions to valuers must be clear and written.  |
|  (b) Valuation reports must be addressed to the CI and not to the borrower but copies of the valuation reports must always be given to the borrower by the CI. |
| (c) Valuations should be carried out in accordance with the RICS Valuation Standards (Red Book) or European Valuation Standards (Blue Book) or International Valuation Standards (White Book). |
| (d) CIs must assess the appropriateness of the method of the valuation. This method must be according to the type of the property and must be clearly stated in the valuation report, for example, a hotel may be valued using the cost of replacement method, or the future profitability method as applicable.  |
| (e) There must be clear evidence that the valuer carried out an on-site inspection of the property for the purposes of the valuation. |
| (f) The valuation report may be standardised so as to allow for comparison and accurate analysis of the project / property.  |
| (g) In case of material change (either positive or negative) for example changes in planning zones or planning permission, a revised valuation must be carried out. |
| (h) Any cost of valuations carried out for capital requirements purposes or during the credit facility review process is borne by the CI unless it is otherwise specified in the credit facility agreement. |
| (i) Credit risk staff and the Loan appraisal and approving authorities must be trained in understanding and assessing the property valuation reports, especially as regards references to constraints in the sale of the property.  |
| 1. CIs must set criteria specifying the cases where more than one valuation must be obtained. Criteria must take into consideration both the credit facility amount and the property value.
 |
| (k) In the case of granting credit facilities for development or project finance then the valuation report must clearly state the values and main characteristics of each unit - if sold separately and the value if the whole project is sold. |

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