

State registration with the	Approved by
Ministry of Justice of Azerbaijan Republic	Resolution of December 29, 2001 by the Management Board of the Central Bank of Azerbaijan Republic
Registration No. 2739 January 17, 2002	Protocol No. 26
Minister _____ F.F. Mammadov	Governor of the Management Board _____ E.S. Rustamov

**REGULATIONS
ON
RELATED PARTY TRANSACTIONS OF BANKS**

(as amended on November 24, 2003; June 28, 2004; and April 15, 2010)

BAKU - 2001

1. General provisions

1.1. These Regulations have been developed in accordance with the Laws of Azerbaijan Republic «On the Central Bank of Azerbaijan Republic» and «On banks», and serves the purpose of minimizing credit risks associated with related party transactions of all commercial (joint-stock commercial) banks and local branch offices of foreign banks (hereinafter referred to as banks) operating in Azerbaijan Republic.

1.2. The purpose of regulating such debts is to ensure that related parties of banks are treated as any other user of banking services, irrespective of their position with the bank, or whether or not they have the authority to control or influence the bank's operations, and to increase public confidence in the banking system.

The following terms and definitions are used herein:

1.3. Related parties of banks include:

- a) the bank's administrators;
- b) the bank's business unit managers;
- c) other employees of the bank involved in decision-making;
- d) individuals who have close family relation to the persons specified in sub-paragraphs a), b) and c) above (spouses, parents, including the spouse's parents, grandparents, children, including foster children, siblings);
- e) any person who has a significant share/equity investment in the bank;
- f) a legal entity where the bank has a significant share/equity investment;
- g) any person who has a significant share/equity investment in the legal entities specified in sub-paragraphs e) and f) hereof;
- h) executive officers of the legal entities specified in sub-paragraphs e), f) and g) above.

1.4. A person is considered *a person acting on behalf of a related party of the bank* if, based on the nature of the relationships between them, such person acts at instructions from the bank's related party, or if the bank's related party benefits from an agreement with such person. *Persons acting on behalf of a related party of the bank include:*

- a) a person authorized by a contractual arrangement to act on behalf of a related party of the bank;
- b) a legal entity capable of exercising significant influence on the bank's related party;
- c) a representative of the bank's related party.

1.5. *Administrator* — members of the bank's Supervisory Board, Audit Committee and Management Board, as well as the bank's chief accountant (accounting service manager), internal audit staff, executives and chief accountants of the bank's branch offices, divisions and representative offices.

1.6. Removed.

1.7. Related parties of the bank and persons acting on their behalf are deemed to *exercise significant influence* on a legal entity if any of the following applies:

- this person has a significant shareholding/equity investment in the legal entity;
- this person is able to control or manage the significant shareholder of the legal entity, or the members of the entity's Supervisory Board, Audit Committee, Financial Inspection Committee, Management Board or other executive officers under a contract or otherwise, or to control or manage the operations of such legal entity in any other manner;
- this person is a subsidiary liability shareholder of the legal entity.

1.8. *Significant share/equity investment* - direct or indirect ownership of 10 or more percent of the shareholder capital or voting rights, or a share that provides the ability to exercise significant influence over the decision-making process of the legal entity where such equity investment is

made under a contract.

1.9. Loans to related parties of a bank and persons acting on their behalf shall mean the following, for the purposes hereof:

- principal amount of all current and past due loans (loans, factoring and financial leases;
- off-balance sheet liabilities, including commitments to open lines of credit, guarantees, letters of credit and commitments to provide other forms of security;
- overdrafts (regardless of whether they are pre-agreed or not);
- any debt charge-off (other than debts charged-off due to a court-ruled liquidation of the borrower's liability under bankruptcy proceedings initiated, or due to expiry of a court appeal);
- other rights associated with purchase of debt securities with discount or interest and claims on funds granted under a contract in any form.

Such indicators of the bank's related parties and persons acting on their behalf considered risky for the bank shall be hereinafter referred to as *the bank's credit exposures*.

1.10. *Low quality assets (loans)* include:

- assets reported as «sub-standard» in accordance with the Central Bank's «Asset Classification and Possible Loss Provisioning Regulations» as a result of an evaluation or by the bank;
- non-accrual assets;
- assets with principal or interest delinquency over 30 days;
- assets rolled-over or restructured because of the obligor's financial difficulties.

1.11. The bank's total capital shall be calculated in accordance with the Central Bank's «Regulations on calculation of bank capital and its adequacy».

2. Maximum exposure to related parties of banks and persons acting on their behalf

2.1. Unless otherwise provided herein, direct or indirect maximum credit exposure of a bank to related parties or persons acting on their behalf shall not exceed the following norms (limits):

- a) for legal entities, 10 percent of the bank's total capital;
- b) for individuals, 3 percent of the bank's total capital.

2.2. The bank's total credit exposures to related parties and persons acting on their behalf shall not exceed 20 percent of the bank's total capital.

2.3. Credit exposures to related parties and persons acting on their behalf shall be secured as follows:

- providing that its market value is not less than 125 percent of the loan value, if the collateral consists of securities issued by the government of Azerbaijan or central governments or central banks of member countries of the Organization for Economic Cooperation and Development (OECD);
- providing that its market value is not less than 150 percent of the loan value, if the collateral is provided in any other form.

2.4. If the market value of collateral is below the level specified in sub-paragraph 2.3 above, this collateral must be replaced or completed within 10 business days.

2.5. Banks may accept credit exposures within the limits defined in paragraphs 2.1 and 2.2 above only in exceptional cases. Banks are recommended to adopt lower levels of such requirements in their internal written procedures.

2.6 Related parties and persons acting on their behalf may not claim invalidity of loans granted in accordance with the provisions hereof.

3. Prohibitions on transactions with related parties and persons acting on their behalf

3.1. If proposed unrelated party transactions are not useful for the bank, such transactions must not be executed with related parties and persons acting on their behalf either. Such transactions include:

- any transaction not conducted with unrelated parties because of high risk levels or other adverse indicators;
- interest rates or commission fees charged for loans granted to related parties or persons acting on their behalf are below the interest rates and commission fees charged for loans granted to unrelated parties or the deposit rates are higher than the current market rates;
- fees paid to the bank's related parties and persons acting on their behalf are higher than fees paid to unrelated parties;
- fees are paid to related parties and persons acting on their behalf while no fees are paid to unrelated parties;
- loans granted to the bank's related parties and persons acting on their behalf are rolled-over or restructured, while loans granted to unrelated parties cannot be rolled-over or restructured;
- the cost of property purchased from the bank's related parties and persons acting on their behalf is higher than the cost of the same property that can be purchased from unrelated parties;
- the cost of property sold to the bank's related parties and persons acting on their behalf is lower than the cost of the same property that could be sold to unrelated parties;
- the value of collateral required from the bank's related parties and persons acting on their behalf is lower than the value of collateral required from unrelated parties;
- bad assets (loans) are taken from the bank's related parties and persons acting on their behalf or such assets are accepted as collateral for a loan;
- investments are not made in an unrelated party's business due to high risks, while investments are made in the business of related parties and persons acting on their behalf that has the same characteristics and risk profile;
- the bank's related parties provide the bank's shares issued or their equity investment in the bank as collateral for a loan.

3.2. In addition to the normative requirements, limitations and prohibitions imposed hereunder, all transactions with related parties and persons acting on their behalf shall be conducted in accordance with the safe and sound banking criteria and procedures. Such procedures must be as favourable for the bank as the procedures regulating transactions with unrelated parties.

3.3. Related parties or persons acting on their behalf should refrain from using the bank's services and the bank must avoid any transactions with such parties that may damage the bank.

4. Decision-making procedures regarding transactions with related parties and persons acting on their behalf

4.1. Any transactions with related parties or persons acting on their behalf, other than deposit transactions, shall be subject to approval from the Supervisory Board and the Management Board's unanimous decision. Such transactions shall be appropriately recorded in the minutes of meetings (meeting protocols) of the Supervisory Board and the Management Board. Members of the Supervisory Board and Management Board shall not take part in discussion of the following matters, nor shall such matters influence the decisions of the Supervisory Board and the Management Board:

- a) themselves;
- b) any of their own close relatives of the bank's related party;
- c) any legal entity where any of their own close relatives of the bank's related party has a significant share or any power to exercise significant influence ;
- d) any person acting on behalf of the persons specified in sub-paragraphs a), b) and c) above.

4.2. The decision of the bank's Supervisory Board and Management Board concerning execution of transactions with the bank's related parties or persons acting on their behalf shall specify the terms and conditions and execution of all such previous transactions, as well as the terms of all current transactions. For example, when the Supervisory Board decides to grant a loan, the protocol must specify any previous loans granted to such person, their repayment details, the proposed loan amount, interest rate, the obligor's financial information ascertaining his ability to repay the loan and information evidencing the value of the proposed collateral for the loan. Asset sales and purchase information shall include information specifying the purchase value and the asset's value (for example, report of appraisal made in accordance with the Central Bank's applicable regulations or a market survey report). When such persons provide services to the bank or the bank purchases assets from such persons, the bank shall obtain information about the proposed service or asset based on purchase of the same service or asset from a third party (source) without a direct or indirect relation to the bank.

4.3. After a decision is made to grant a loan to the bank's related parties or persons acting on their behalf, the loan shall be granted in accordance with the bank's internal lending procedures, in compliance with the requirements hereof. Banks shall monitor equity investments in related parties or persons acting on their behalf and shall regularly evaluate such investments as per the methodologies and criteria used for evaluation of equity investments in unrelated parties.

5. Documentation and reporting of transactions with related parties and persons acting on their behalf

5.1. Banks shall present reports on the bank's related parties and persons acting on their behalf to the Central Bank of Azerbaijan Republic in the format attached hereto (Annex 1) no later than within 5 business days of the month following the reporting month. The report shall specify the names of the bank's related parties and persons acting on their behalf, a brief summary of the transaction, including its amount, terms and duration.

5.2. All banks shall document compliance with the requirements hereof. Such documents shall specify all related parties and persons acting on their behalf the bank granted loans to, as well as the amount, maturity period and conditions of the loan and all associated operations.

5.3. All banks shall keep records of transactions with their own administrators, the bank's related employees and their close relatives, as well as persons acting on behalf of such parties, in the format attached hereto (Annex 2).

As it takes effect, these Regulations shall void paragraph 9 of the Central Bank's Regulation No.2, dated May 21, 1997, «On supervision of credit institutions». These Regulations shall take effect on January 1, 2002.

Annex 1
to the
Regulations on Related Party Transactions of Banks

Name of bank _____

As of « _____ » _____ 200 ____

Related Party Transactions Report

	Name and relation with the bank of related parties and persons acting on their behalf (r.p. and p.a.r.p.)	Transaction amount (AZN mil)	Nature of transaction	Date of extension	Maturity/Repayment period	Interest rate
1	Relation A	xxx	xxx	xxx	xxx	xxx
	Individual AA (r.p.), Chairman of the Supervisory Board					
	Individual AB (p.a.r.p.), brother of the Chairman of the Supervisory Board					
	Company AX, Chairman of the Supervisory Board owns 15% of the company's shares					
2	Relation V					
	VV - Individual who owns 12% of the bank's shares (r.p.)					
	VX — Individual who owns 20% of the company's shares (r.p.)					
N						

Chairman of the Supervisory Board
Chief accountant

(full name)
(full name)

Corporate Seal

Annex 1
to the
Regulations on Related Party Transactions of Banks

Name of bank _____

As of « _____ » _____ 200 ____

Information about the bank's related parties and persons acting on their behalf

1. Administrators and their close relatives/immediate family members

	<i>Full name of the bank's related party</i>	Position at the bank	Full name of the relative/family member
1.			
2.			
3.			

2. Entities where the administrators and their close relatives/immediate family members exercise significant influence

	<i>Full name of the bank's related party</i>	Position at the bank	Name of enterprise
1			
2			
3			

3. Close relatives/immediate family members of business unit managers and other decision-making staff

	<i>Full name of the bank's related party</i>	Position at the bank	Full name of the relative/family member
1			
2			
3			

4. Entities where close relatives/immediate family members of business unit managers and other decision-making staff exercise significant influence

	<i>Full name of the bank's related party</i>	Position at the bank	Name of enterprise
1			
2			
3			