

State registration with the	Approved by
Ministry of Justice of Azerbaijan Republic	Resolution of September 1, 2005 by the Management Board of the Central Bank of Azerbaijan Republic
Registration No. 3190 September 23, 2005	Protocol No. 25
Minister _____ Fikret Mammadov	Governor of the Management Board _____ Elman Rustamov

**REGULATIONS ON DEVELOPMENT, SUBMISSION AND SUPERVISION OF  
CONSOLIDATED PRUDENTIAL STATEMENTS**

**(as amended on April 15, 2010)**

## 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», «On banks», other laws and regulations, and identifies the International Financial Reporting Standards-compliant (hereinafter referred to as IFRS) consolidated prudential reporting and supervision procedures for banks, including local branch offices of foreign banks (hereinafter referred to as banks), as well as holding companies.
- 1.2. The principal objective of this oversight is to assist the Central Bank of Azerbaijan Republic (hereinafter referred to as the Central Bank) in ensuring the safety and soundness of the banking system by identifying the impact of significant shareholders and other related parties of banks, who are not directly supervised by the Central Bank, on the current and future financial position, as well as safe and prudential management of such banks.

## 2. Definitions

The following terms and definitions are used herein:

- 2.1. **Subsidiary** — an entity where another entity (parent company) is entitled, by virtue of a priority equity investment in the subsidiary's paid-in capital, or by contract signed with the subsidiary's other shareholders, to exercise control over the subsidiary's decision-making process.
- 2.2. **Parent company (parent bank)** — the entity entitled, by virtue of a priority equity investment in the subsidiary's paid-in capital, or contract signed with the subsidiary's other shareholders, to exercise control over the subsidiary's decision-making process.
- 2.3. **Holding company** — a group incorporated by an individual (individuals) and/or a legal entity (entities) with an aim to own shares in, and control one or several subsidiaries, including commercial banks. For the purposes hereof, holding companies are divided into:
  - 2.3.1. **bank holding company** — a group with one or several licensed subsidiary banks, supervised by the bank regulator of the country where the group's head office is located.
  - 2.3.2. **financial holding company** — a group consisting of banks and other subsidiaries engaged only in the financial sector.
  - 2.3.3. **non-financial holding company** — a group consisting of one or more subsidiaries engaged in various economic sectors, including banks.
- 2.4. **Consolidated financial statements** — IFRS-compliant aggregated financial statements of the parent company and all of its subsidiaries.

## 3. Preparation of consolidated reports

- 3.1. Consolidated prudential reports shall be submitted to the Central Bank for evaluation of the bank's financial position. Financial statements attached to prudential reports shall be prepared in accordance with the IFRS and the Central Bank's «Regulations on preparation and submission of aggregated financial statements and accounting treatment of investments in subsidiaries by credit institutions». Financial statements shall be presented in the format defined by the Central Bank in consultation with the Ministry of Finance of Azerbaijan Republic.
- 3.2. Any parent bank that has a subsidiary operating in Azerbaijan Republic, as well as any

subsidiary bank of a holding company shall prepare consolidated reports.

3.3. In order to identify the characteristics of influence of all subsidiaries of holding companies and a parent bank, as well as related parties of a bank on the bank supervised by the Central Bank, such bank shall present to the Central Bank a diagram that presents the structure of the group and its equity investment in each subsidiary (both group members and other entities), as well as the equity investments of each subsidiary member of the group in other legal entities, by the end of the month following the end of the calendar year. The diagram shall be accompanied with the following:

3.3.1. information about shareholders who directly or indirectly hold (own) shares (equity) of the holding company;

3.3.2. the holding company's policy-making executive bodies and full names of their heads;

3.3.3. lines of business/activities of the bank's subsidiaries and other subsidiaries of the holding company the bank is a member of;

3.3.4. latest externally audited financial statements of the holding company, its subsidiaries and the bank's related parties;

3.3.5. name and address of the appropriate executive body (if applicable) controlling the holding company or any of its subsidiaries.

3.4. Consolidated reports shall be prepared by the 1<sup>st</sup> of January and the 1<sup>st</sup> of July of each year.

3.5. Financial statements attached to the financial year-end consolidated prudential reports shall be subject to external audit in accordance with the International Standards on Auditing.

3.6. The following financial statements shall be attached to the consolidated prudential reports submitted to the Central Bank:

3.6.1. the accounting balance sheet for the group;

3.6.2. the income statement for the group;

3.6.3. the cash flow statement for the group;

3.6.4. the statement of changes in equity for the group;

3.6.5. explanatory notes (including information on in-group cash flow).

3.7. Consolidated prudential reports shall include information on persons who have a direct or indirect equity investment each subsidiary of the holding group and the amount of their share (percentage and amount), as well as information about executive officers of the holding company's subsidiaries.

3.8. The following shall be attached to consolidated prudential reports submitted to the Central Bank, depending on the structure of the holding company:

3.8.1. For the subsidiary bank-member of the holding company:

3.8.1.1. information about the paid-in capital;

3.8.1.2. information about the total capital;

3.8.1.3. information about the adequacy of the total capital;

3.8.1.4. information about transactions with the bank's related parties;

3.8.1.5. information about large exposures.

3.8.2. If a financial holding company or a bank has insurance subsidiaries, for such subsidiaries:

3.8.2.1. information specified in sub-paragraphs 3.8.1.1 — 3.8.1.5 hereof;

3.8.2.2. information about the insurance subsidiary's (subsidiaries') compliance with the requirements set by the Ministry of Finance of Azerbaijan Republic.

3.8.3. If a non-financial holding company includes an insurance subsidiary, for such subsidiaries:

3.8.3.1. information specified in sub-paragraphs 3.8.1.1 — 3.8.1.5 hereof;

3.8.3.2. information about calculation of net assets of non-financial sector subsidiary (subsidiaries) (mismatch between balance sheet assets and balance sheet liabilities).

3.8.4. If a non-financial holding company includes insurance subsidiaries, information specified in sub-paragraphs 3.8.1., 3.8.2 and 3.8.3 hereof.

3.9. Depending on the lines of business/activities of subsidiaries of a holding company, the

bank's parent company and its subsidiaries, the Central Bank may require the bank to provide other necessary management and current performance reports for such entities in order to be able to discharge its supervisory functions and verify the accuracy of financial information.

3.10. If a legal entity engaged in lines of business that are not in conflict with the Law «On banks» of Azerbaijan Republic in order to satisfy its liability requirements becomes a subsidiary of a bank, the operations of such legal entity shall be reported in the parent bank's consolidated prudential reports in accordance with IFRS 27.

3.11. A subsidiary's financial statements shall not be included in the consolidated prudential reports if any of the following applies:

3.11.1. the bank has a direct or indirect shareholding in a wholesale or retail trade, production, transportation, agricultural, field production, construction businesses with the Central Bank's permission, in order to satisfy its liability requirements;

3.11.2. the bank assumes control over a legal entity by repossessing the obligor's (third party's) property not used in the business of banking (this asset is booked as an asset repossessed in satisfaction of a liability);

3.11.3. the subsidiary's assets constitute less than 1% of the holding company's assets;

3.11.4. the bank's assets exceed 95% of the holding company's assets, except subsidiaries of commercial banks.

#### **4. Submission of consolidated reports**

4.1. Consolidated prudential reports shall be submitted to the Central Bank by the holding company's subsidiary bank, as well as the parent bank owning a subsidiary.

4.2. If a holding company has several subsidiary banks, one principal bank shall be selected from among the holding company's banking subsidiaries for submission of consolidated prudential reports to the Central Bank.

4.3. Consolidated prudential reports shall be submitted to the Central Bank together with the reports and information specified in Article 3 hereof by the parent bank or by the bank selected in accordance with paragraph 4.2 hereof for each subsidiary of the holding company, the bank's parent company.

4.4. Consolidated prudential reports as of July 1 shall be submitted to the Central Bank no later than within 3 months from the end of the reporting period.

4.5. Annual consolidated prudential reports shall be submitted to the Central Bank no later than within 5 months from the end of the financial year. These reports shall include the parent company's and each subsidiary's financial statements audited by an external auditor in accordance with the International Standards on Auditing, and the auditor's opinion.

A foreign holding company that has a subsidiary bank (banking subsidiary) in Azerbaijan shall submit annual prudential reports, including its financial statements audited by an external auditor in accordance with the International Standards on Auditing and the auditor's opinion, to the Central Bank no later than within 8 months from the end of the financial year.

4.6. A foreign holding company or a foreign legal entity that has a subsidiary bank (banking subsidiary) in Azerbaijan shall properly legalize and present its consolidated prudential reports required hereunder to the Central Bank in Azerbaijani.

4.7. If any changes occur in the equity investment/shareholding of any subsidiary covered by consolidated prudential reports or such subsidiary is liquidated, a notice to this effect shall be provided to the Central Bank within 30 days.

#### **5. Discharge of supervisory functions**

- 5.1. The supervisory process shall assess the impact each subsidiary of the holding company has on the bank's financial position, as well as evaluate the bank's risks on a consolidated basis that arise as a result of relationships between the holding company's subsidiaries. All banking subsidiaries of a holding company and all parent banks that have subsidiaries shall manage their risks in accordance with the Law of Azerbaijan Republic «On banks» and the Central Bank's «Regulations on management of exposures to a single borrower or a group of connected borrowers» and «Regulations on transactions with related parties of banks». Bank holding companies shall also adhere to the Central Bank's «Regulations on calculation of bank capital and its adequacy».
- 5.2. Supervisory reports and additional information, as well as appropriateness of their preparation shall be checked using the information available at banks.
- 5.3. The supervisory process shall include appropriate inspections of each subsidiary of a bank holding company and banks owning subsidiaries in accordance with the Law of Azerbaijan Republic «On banks».
- 5.4. For supervisory purposes, the Central Bank shall collaborate with state authorities responsible for regulation and supervision of holding companies or their member subsidiaries.

## **6. Requirements to bank policies and procedures**

- 6.1. Banks shall have internal written procedures in place to ensure that information required hereunder is provided by the holding company's subsidiaries for the purposes of consolidated prudential reporting.
- 6.2. Banks shall have internal written procedures for IFRS-based consolidated prudential reporting, as well as for evaluation of assets and liabilities of all subsidiaries of a holding company.
- 6.3. If any event taking place at any subsidiary of the holding company poses risks to the bank, the bank shall assess the impact of such event on the financial position of other subsidiaries of the holding company, as well as its own financial position.

## **1. Final provisions**

- 7.1. A major shareholder of a bank that is in breach of any provision hereof may be required to dispose of his shareholding/equity investment or the bank may be required to redeem such equity investment, or the bank may be required to limit, suspend or liquidate its own equity investments in other legal entities, and any other enforcement measures and sanctions may be applied as provided for in the Law of Azerbaijan Republic «On banks».
- 7.2. These Regulations shall take effect as of the date of state registration.