



SUPERVISORY AND REGULATORY GUIDELINES: 2003-2
Letters of Comfort
15th August, 2003

MINIMUM STANDARDS FOR LETTERS OF COMFORT

I. INTRODUCTION

The Central Bank of The Bahamas (*“the Central Bank”*) is responsible for the licensing, regulation and supervision of banks and trust companies operating in and from within The Bahamas pursuant to The Banks and Trust Companies Regulation Act, Chapter 316 of the revised Statute Laws of The Bahamas, 2001, and The Central Bank of The Bahamas Act, Chapter 351 of the revised Statute Laws of The Bahamas, 2001. Additionally, The Central Bank has the duty, in collaboration with financial institutions, to promote and maintain high standards of conduct and management in the provision of banking and trust services.

All licensees are expected to adhere to the Central Bank’s licensing and prudential requirements and ongoing supervisory programmes, including periodic on-site inspections, and required regulatory reporting. Licensees are also expected to conduct their affairs in conformity with all other Bahamian legal requirements.

II. PURPOSE

During the license application process or subsequent to the granting of a licence, The Central Bank of The Bahamas may require a letter of comfort to be issued from the parent institution (the *issuer*) in favour of the licence applicant/ licensee (the *beneficiary*). By issuing a letter of comfort, the *issuer* signifies its willingness and commitment to provide such support as the *beneficiary* may need, should unforeseen contingencies impact on its ability to maintain adequate capital and liquidity levels to meet its obligations and regulatory requirements.

These Guidelines specify the criteria that the Central Bank will apply in assessing the acceptability of letters of comfort from an *issuer* to its *beneficiary*.

III. APPLICABILITY

This supervisory guideline applies to the use of letters of comfort issued to all bank and/or trust licensees.

IV. ACCEPTANCE CRITERIA

1. In order for a letter of comfort to be acceptable, The Central Bank of The Bahamas must be satisfied that the *issuer* has, and will continue to have, a strong commitment to support the *beneficiary* and is financially sound enough to fulfil its commitment under the letter.
2. As the letter of comfort is not a guarantee, it is particularly important to ensure that the following criteria are met on a continuing basis:
 - a) The *issuer* is a licensed financial institution from a jurisdiction which supervises banks in compliance with the Basel Capital Accord and Core Principles for Effective Banking Supervision;
 - b) The issuer is a controller of the *beneficiary*, normally a majority shareholder controller but possibly a minority shareholder controller;
 - c) The letter of comfort is issued under a resolution of the Board of Directors of the issuer;
 - d) The home supervisory authority of the issuer is aware of the letter of comfort and does not object to its issue by the issuer;
 - e) The issuer has and will continue to have, the financial strength to support its obligations under the letter of comfort;
 - f) The issuer exercises effective oversight over the beneficiary's large exposures; and
 - g) The home supervisory authority supervises the capital adequacy and large exposures of the issuer on a consolidated basis and the position of the beneficiary is taken into account in such supervision.

V. FORM AND CONTENT

1. There is no specific format for letters of comfort but there are essential elements that should feature in their contents:-
 - a) The letter of comfort should acknowledge the purpose and should express clearly the nature and extent of the *issuer's* commitment to support the *beneficiary*;
 - b) It should set out the shareholding relationship between the issuer and the beneficiary;

- c) The issuer should undertake to inform the Central Bank immediately of any change in the relationship with the beneficiary and to consult with the Central Bank in advance of any proposed decrease in the percentage of shares held in the beneficiary;
- d) It should confirm that the issuer exercises effective oversight over the beneficiary's large exposures and will ensure that it is informed of all exposures covered by the letter on a timely basis; and
- e) It should state that the letter has been authorized by a resolution of the Board of Directors of the *issuer* and a copy of the Resolution should be included.

VI. FACTORS FOR CONSIDERATION

1. The Central Bank will take into account the following factors:
 - a) The financial strength and background of the *issuer*. The financial strength of the *issuer* will be assessed in the light of, *inter alia*, its consolidated shareholder's funds.
 - b) The extent to which the issuer's capital adequacy and credit risk profile (including those of the beneficiary) are subject to consolidated supervision by its home supervisory authority and the degree of oversight and control exercised by the issuer over the beneficiary's large exposures;
 - c) The financial strength of the beneficiary; and
 - d) The sources of funding of the beneficiary and the degree of its reliance on deposits from the public to fund its operations.

VII. CONDITIONS

The Central Bank may, if appropriate, attach conditions to the letter of comfort, either generally or in any particular case.

VIII. REVIEW BY THE CENTRAL BANK OF THE BAHAMAS

To monitor whether the *issuer* of a letter of comfort continues to be financially sound and able to honour its obligations under the letter of comfort, The Central Bank will conduct a review of the financial condition of the *issuers* of letters of comfort, at least annually.

To facilitate the annual review, The Central Bank will require the *issuer* to submit the following information:

- a) Its latest audited financial statements on an annual basis;
- b) Statement of good standing from the *issuer's* home supervisor.

IX. CANCELLATION OR VARIATIONS IN THE TERMS OF THE LETTER OF COMFORT

The *beneficiary* of a letter of comfort should notify The Central Bank within 7 working days of (a) the cancellation, or (b) any variations in the terms, of a letter of comfort issued to it.