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**Memorandum to Licensed Banks  
No. ( 4 / 2004 )**

**The Framework for Corrective Actions**

Within its efforts to enhance the soundness of the banking system, and activate the compliance with the laws, by-laws and instructions aiming to avoid the unsound and unsafe banking operations and policies, and in pursuit of the policies aiming at handling the weaknesses at early stages, and in support of transparency, the Central Bank of Jordan, by the virtue of the Banking Law No. (28) for 2000 and the Board of Directors resolution No. (1/2004) dated 7/1/2004, will impose the following penalties and corrective actions to achieve the aforementioned goals, in line with the following bases and standards:

**First: The Cases which Necessitate Corrective Actions**

These cases are categorized as follows:

- a. The bank's contravention of the provisions of the Banking Law or the by-laws, instructions and orders issued pursuant thereto.
- b. Conducting by the bank or one of its subsidiaries unsound and unsafe operations.
- c. The deterioration of the bank position based on CAMEL or ROCA rating system.
- d. The deterioration of the bank solvency or capital adequacy below the limits identified in the concerned instructions of the Central Bank.

**a. The bank's contravention of the provisions of the Banking Law or the by-laws, instructions and orders issued pursuant thereto.**

The Banking Law and the by-laws, instructions and orders issued based on its virtue included controls for the banking operations with the purpose of maintaining the soundness of the banking institutions and the banking system in general. Accordingly, the Central Bank, as a regulatory authority, will take the measures deemed necessary to guarantee the commitment of the banks by the Banking Law and the instructions and orders issued by its virtue.

**b. Conducting by the bank or one of its subsidiaries unsound and unsafe operations.**

It is vital to point out that the concept of the unsound and unsafe banking operations is wide and includes various activities in the bank. Therefore, appendix (1) points

out forms of such operations. However, it should be emphasized that the forms included in the above-mentioned appendix are just examples, which means that there are other operations which may be considered. Further, the forms displayed in the appendix are not necessarily unsound and unsafe banking practices operations at large and all facts should be taken into account to judge whether or not they are, including the position of the bank in general. To be more precise **the unsound and unsafe banking operations** can be defined as taking (or not-taking) a measure where taking (or not-taking) such measure is in contrast with the sound banking fundamentals, and there is a possibility that the implementation of this measure or its continuity will result in substantial losses that affect the bank or the shareholders or the depositors or the guarantors of deposits.

**c. The deterioration of the bank position based on CAMEL or ROCA rating system.**

- CAMEL or ROCA rating system represent a comprehensive evaluation for the situation of the bank as a whole. Therefore, their deterioration is an important indicator of unsound or unsafe position of the bank. Moreover, such situation reflects a contravention for the provision of article (36/b) of the Banking Law, and in light of the importance of this evaluation it has been designated in a separate item from the categories (a) and (b) listed above.
- In the case that the bank has been rated (3) according to the CAMEL or ROCA rating system, this reveals that it is facing weaknesses and troubles which if they have not been addressed could lead to further weakness or exaggeration of the existing troubles in away that could result in further deterioration in the level of bank's rating or solvency, which necessitates an intervention to deal with the aspects of weakness or the troubles. However, if the bank has been rated (4 or 5), this means that the corrective actions are becoming more pressing.

**d. The deterioration of the bank solvency or capital adequacy below the limits identified in the concerned instructions of the Central Bank**

The Central Bank has specified, through the Instructions for the Regulatory Capital and Capital Adequacy No. (16/2003), and the Instructions for the Minimum Capital for the Banks operating in Jordan No. (17/2003), the ratios of solvency and capital adequacy for the licensed banks. In effect, the deterioration in these ratios represents a violation for the Banking Law and the instructions issued by its virtue, in addition to reflecting an unsound and unsafe banking position. In light of the importance of this evaluation and the role of capital, it has been decided to separate as an item apart from the categories (a) and (b) listed above.

## **Second: The Corrective Actions which will be taken in the above mentioned Cases.**

### **1- Money Penalties**

- a. Money penalties will be imposed if the bank violates the Banking Law or any of the by-laws, instructions and orders issued by its virtue, including any written directives issued to the bank, or any corrective program presented by the bank, or any instructions to cease and desist any of its activities or any unsound or unsafe practices and activities.
- b. The aforementioned money penalties could come separate or with other measures taken by the Central Bank to correct the position of the bank in case the standards of these measures were found applicable on the concerned banks.
- c. The Central Bank will take into consideration the following factors when deciding the size of the money penalty :
  1. The frequency of violations and their duration.
  2. The continuation of the violation after addressing a written warning or imposing a penalty on the bank.
  3. The cooperation or non- cooperation with the Central Bank in correcting the violations.
  4. The existence of proof that the bank is trying to cover its violation.
  5. The size of damage or loss that was caused by the violation of the bank
  6. The existence or non-existence of a corrective program and its effectiveness.

**In addition to other factors which will be included in the relevant detailed instructions concerning the money penalties to be issued by the Central Bank later on.**

### **2- Instructing the concerned bank to submit a satisfactory program of measures to be taken to eliminate the violations and rectify the situation.**

- This procedure measure is usually employed with the banks which have been given a rating of (3) according to the CAMEL or ROCA rating system.
- **The Program could take one of the following forms:**
  - a. **Board of Directors' decisions to the executive management to put an end to the violation or rectify the areas of deficiency or weakness.**

The decisions should be devised in a way which will not only rectify the consequences and symptoms of the trouble but also rectify its reasons. Further, the Board of Directors must follow up the executive management to make sure of the commitment in implementing the decisions.

### **b. Submitting a satisfactory corrective program**

The program should be devised in a way which will not only rectify the consequences and symptoms of the trouble but also rectify its reasons. Further, the Board of Directors must follow up the executive management to make sure of their commitment in implementing the program. It also should include a time frame and measurable targets. The above-mentioned program should be signed by the Board of Directors of the bank and its general manager for the Jordanian banks. In case of foreign banks, the program should be signed by the regional manager of the bank in Jordan and the head quarters in the parent country..

### **3- Orders to cease and desist certain activities**

- a. These orders aim to stop the violation or the unsound and unsafe practices, adjust their consequences as well as preventing further deterioration in the bank's performance as a result of the violation.
- b. These orders are not confined to the bank as one unit only, but they could also include directors, officials or employees managing the bank.
- c. In case of no compliance to these orders, the Central Bank has the right to introduce more strict procedures or impose money penalties on the bank.
- d. The activities that could be ceased or limited depend mainly on the position of the bank and could include, for instance, granting credit facilities to certain bodies, or the growth of credit facilities, or accepting deposits, or imposing restrictions on interest rates. The procedures related to the deterioration in the solvency include more examples.

### **4- Instructing the bank to temporarily suspend from service any administrator, other than a member of its board of directors, or to dismiss such administrator, depending on the gravity of the violation, or removing the chairman or any member of the board of directors of the bank.**

- The main reasons that could push the Central Bank to take the above-mentioned measures include:
  - a. The direct or indirect, violation of the person to be dismissed or temporarily suspended from the employment to the Banking Law or any of the by-laws, instructions and directives issued by the virtue of the Law, including any written directives to the bank, or the corrective program submitted to the Central Bank, or any orders to cease or limit the activities, or conducting any unsound or unsafe banking operations or performing practices in contrast with his/her duties towards the bank.

**(And)**

- b. What took place in item (a.) above, resulted or could result in losses or notable damage to the bank or depositors or that the party who committed the violation has benefited directly or indirectly. from that violation.
- It is worth noting that the Central Bank will not allow the appointment/reappointment the member of the board or the general manager or any of the executive managers, who have been dismissed or suspended, from any banking institution in the future.
- 5- Dissolving the Board of Directors of the bank and placing the bank under the management of the Central Bank.**
  - 6- Merging the bank with another bank.**
  - 7- Revoking the license of the bank.**

**Third: The Corrective Actions which will be taken for each case mentioned in First above**

- 1- The Corrective Actions for the bank's contravention of the Banking Law or any by-laws, instructions and orders issued by the virtue of the Law.**
  - a. The money penalties are the main corrective actions that can be taken by the Central Bank in this situation.
  - b. The Central Bank can take any of the corrective actions (3-7) identified in second above instead of or in addition to the money penalties in light of :
    - 1. The material impact of the violation on the bank.
    - 2. The bank solvency and the effect of the money penalty on it.
    - 3. The Central Bank's consideration of violation as unsound or unsafe banking practice.
    - 4. The conviction of the Central Bank that the money penalty will prohibit the bank from perpetrating similar violations in the future.
- 2- The Corrective Actions concerned with the practice of the bank or one of its subsidiaries of unsound or unsafe banking operations.**

In light of the nature of the unsound or unsafe banking operations and their wide concept which covers all the bank activities, the Central Bank will specify the size and nature of the corrective actions based on the nature of the practice, its circumstances as well as its impact on the bank.

**3- The Corrective Actions concerned with the deterioration of the bank rating based on CAMEL or ROCA rating system.**

**(3/a) The Corrective Actions in case the bank has been rated (3) according to the CAMEL or ROCA rating system**

**a. The measures which can be taken:**

1. The decisions of the Board of Directors of the concerned bank.
  2. Submitting a satisfactory corrective program to the Central Bank.
- b. The measure taken with any bank within this category will not be less than any of the measures identified in (a) above.
- c. The non compliant bank with the measures identified in (a) above will be the base for imposing more strict measures against the bank or any of its executives. In contrast, the commitment to correct the violations and weakness areas will be the base for the success of these measures and, accordingly, for not taking any further measures.

**(3/b) The Corrective Actions in case the bank has been rated (4) or (5) according to the CAMEL or ROCA rating system, or non compliance with corrective program or not taking, in general, the required corrective actions.**

**a. The measures which can be taken:**

1. Orders to cease or limit certain activities.
  2. Instructing the bank to temporarily suspend from service any administrator, other than a member of its board of directors, or to dismiss such administrator, depending on the gravity of the violation, or removing the chairman or any member of the board of directors of the bank.
  3. Dissolving the Board of Directors of the bank and placing the bank under the management of the Central Bank.
  4. Merging the bank with another bank.
  5. Revoking the license of the bank.
- b. The measure taken in the cases specified in (3/b) will not be less than orders to cease or limit certain activities.

**4- The Corrective Actions concerned with the deterioration of the bank solvency or capital adequacy below the acceptable limits**

- These are amongst the main measures the Central Bank will take because the most serious danger facing any bank is the deterioration of its solvency due to the fact the capital is the cushion between the funds of depositors and any losses could be incurred by the bank.

- The principle of the measures concerned with the deterioration in the bank solvency below the acceptable levels is based on two main issues; **first** is the ranking of banks into five categories based on the solvency and capital adequacy and **second** is the identification of the measures to be taken depending on that.

**(4/1) – The standards of ranking banks based on the solvency and capital adequacy**

- The Central Bank has specified, through the Instructions of the Regulatory Capital and Capital Adequacy No. (16/2003), and the Instructions of the Minimum Capital for the operating Banks in Jordan No. (17/2003), the ratios of solvency and capital adequacy for licensed banks; the aforementioned instructions links the previous instructions within a comprehensive framework to measure the solvency and capital adequacy. It is worth noting in this regard that a compound standard will be used to measure the solvency of the bank, including the capital adequacy ratio, the ratios of core capital to the weighted risk assets and the ratio of capital to total assets. Accordingly, the banks will be ranked into five categories as demonstrated in table (1) which summarizes the principles of ranking.

**Table (1): Classification of banks into five categories based on the level of solvency and capital adequacy**

<b>Solvency or Capital Adequacy Category</b>	<b>Capital Adequacy Ratio</b>	<b>Tier 1 Core Capital to Risk Weighted Assets (on and off-balance sheet)</b>	<b>Leverage Ratio</b>
<b>First Category: Well Capitalized</b>	14% or more And	8% or more And	7% or more
<b>Second Category: Adequately Capitalized</b>	12% or more And	6% or more And	6% or more
<b>Third Category: Undercapitalized</b>	Less than 12% Or	Less than 6% Or	Less than 6%
<b>Fourth Category: Significantly Undercapitalized</b>	Less than 8% Or	Less than 4% Or	Less than 4%
<b>Fifth Category: Critically Undercapitalized</b>	If the tangible capital to total assets equal to or less than 3%		

The tangible capital means the shareholders equity excluding any intangible assets such as goodwill or similar assets.

- Re-categorizing the bank to a lower category concerning solvency or capital adequacy**

- The vital importance of the level of solvency of the bank necessitates not only considering its current level but also the future level in light of the risks which the bank is exposed to.
- Having said that, the Central Bank could re-categorize the bank in a lower category concerning solvency or capital adequacy in the cases where the bank is in unsound or unsafe situations such as poor asset quality or conducting unsound or unsafe banking operations in general.
- Within the aforementioned framework, the Central Bank has the right to re-categorize the banks which fall in categories (4) and (5) according to the CAMEL or ROCA rating system from the first category (Well Capitalized) to the second category (Adequately Capitalized) or from the second category to the third category (Undercapitalized).

**(4/2) – The measures to be taken based on the level of solvency or capital adequacy**

**a. The banks within the first and second categories (well capitalized and adequately capitalized):**

These banks should commit to not making any distributions from the capital accounts or pay any rewards to the administrators or the board of directors members, should such action result in categorizing the bank in the category of (undercapitalized).

**b. The banks within the third category (undercapitalized):**

- These banks are subject to the measures concerned with the banks in the first and second categories which mean that they should not provide any rewards to the administrators or the board of directors because this will deteriorate the solvency of the bank.
- The concerned bank should submit a capital restoration plan to the Central Bank no later than 45 days, and the plan must include direct steps to improve the bank's solvency, the time frame for achieving this target, and the mechanism to be used for this purpose.
- The categorization of the bank in a higher category in the area of solvency depends on the implementation of the capital restoration plan as well as removing the factors which led to the deterioration in the capital or the solvency.
- It is not allowed for the bank to distribute dividends for the shareholders.
- The Central Bank has the right to put restrictions on the growth of the bank's assets or any of its components.
- The Central Bank has the right to request the bank to get a prior consent before acquiring new assets or introducing new products, in addition to any other activities identified by the Central Bank.
- The bank could be subject to the additional measures imposed on the banks in the fourth category (significantly undercapitalized)



- Any other measures deemed necessary by the Central Bank to achieve the target of rectifying the deterioration in the level of solvency or capital adequacy

**c. The banks within the fourth category (significantly undercapitalized):**

- These banks will be subject to all measures imposed on the banks in the third category (undercapitalized)
- The bank will be subject, at least, to one of the following additional measures:
  1. The merger with another bank in case the bank failed to raise its capital.
  2. Putting constraints on the interest rate on deposits to be in line with the prevailing rates of the markets.
  3. Not accepting deposits from correspondent depository institutions
  4. Stringent constraint on the growth of assets or part of them or requesting to downsize their volume
  5. Ceasing or limiting any activity which could expose the bank to high risks.
  6. Instructing the bank to temporarily suspend from service any administrator, other than a member of its board of directors, or to dismiss such administrator, or removing the chairman or any member of the board of directors of the bank based on the principles identified in (Second/4).
  7. Putting constraint on the bank operations with any subsidiary or affiliate if there is a risk of insolvency on the side of such companies which could result in exposing the bank for material risks.
- Any other measures deemed necessary by the Central Bank to achieve the target of rectifying the deterioration in the level of solvency or capital adequacy.

**d. The banks within the fifth category (critically undercapitalized):**

1. The Central Bank will merge the concerned bank with another bank or revoke its license within a time interval not to exceed 270 days from the date of classifying the bank in this category.
2. The Central Bank has the right to extend the above-mentioned period by additional 270 days in case:
  - The shareholders equity is positive for the bank, and
  - The notable bank commitment to the capital restoration plan, and
  - The bank achieve profits or constant and sustainable improvement in the bank's revenues, noting that such revenues are not extraordinary and non-recurrent, and
  - The Central Bank is convinced that the bank is not on the verge of bankruptcy and the decision of extension is the least expensive, in general, and for the Deposit Insurance Corporation in particular.

3. During the periods mentioned in (1) and (2) above:

- The bank will be subject to the measures imposed on the banks in the fourth category (significantly undercapitalized).
- The bank activities will be constrained to the maximum level possible.
- The prior approval of the Central Bank is necessary before conducting the following:
  - Any important activity aside from the usual activities of the bank.
  - Extending credit to a high-indebted party.
  - Introducing a material change to the accounting procedures.
  - Paying big compensations or rewards.
  - Paying interest rate on liabilities in away that makes the average weighted cost on liabilities higher than the one prevailing in the market.
  - Any other measures deemed necessary by the Central Bank to achieve the target of rectifying the deterioration in the level of solvency or capital adequacy.

#### **Fourth: Concluding Remarks**

- **The Central Bank will keep the right to disclose to the public any of the above-mentioned measures imposed on any bank**
- **These instructions are in force from the date of issuing this memorandum**

**Please accept the assurance of my high esteem and consideration**

**Governor  
Dr. Umayyah Toukan**

## Appendix (1)

### Examples of the unsound or unsafe banking procedures and practices

#### a) Banking procedures if not taken are considered unsound or unsafe

1. Lack of sufficient internal control to prevent the employees of the bank from conducting unsound or unsafe banking operations or violating the existing laws, by-laws and regulations.
2. Failure to build sufficient provision for non-performing loans.
3. Lack of correct accounting treatment of transactions or lack of documented and precise data for accounts, or clients, or collaterals for credit facilities
4. Inability to impose suitable settlement programs to collect the non-performing loans

#### b) Banking procedures if taken are considered unsound or unsafe

1. Failure to meet the minimum acceptable capital level, taking into consideration the quality of the bank's assets.
2. Conducting unsound practices in the areas of extending, following up and collecting credit facilities, including, but not limited to:
  - Extending credit facilities without appropriate collateral
  - Extending credit facilities before collecting full and updated information on the counter party.
  - Extending credit facilities in overdraft accounts without sufficient controls.
  - The concentration in credit facilities<sup>1</sup>
3. Conducting the banking activity without appropriate level of liquidity.
4. Conducting the banking activity without internal monitoring and control systems which guarantee amongst others:
  - Monitoring and controlling non-issued cheques and certificates of deposits
  - Segregation of duties within the bank.
5. Pursuing an investment policy which includes high risk speculations and practices

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<sup>1</sup> Including the concentration in certain sector, or certain country or certain client, or any other form of concentration

**c) Unsound or unsafe banking positions**

1. Retaining a notable low interest rate margin
2. High administrative expenses in comparison with the volume of the bank activity
3. High ratio of non-performing, or under supervision loans to total loans or equity
4. Increasing bad loans
5. Increasing ratio of non-performing assets
6. Concentration in fund resources

**d) Contravention of the provisions of the Banking Law or the instructions and the directives issued by its virtue.**