

Republic of Panama Superintendency of Banks

**RULE N°. 3-2019
(dated 30 April 2019)**

“Whereby the Technical Appendix of Rule 11-2018 that prescribes new provisions on Operational Risk is amended”

THE BOARD OF DIRECTORS
in use of its legal powers and,

WHEREAS:

Due to the issuance of Decree Law 2 dated 22 February 2008, the Executive Branch re-edited Decree Law 9 dated 26 February 1998 and all its amendments as a consolidated text, and this text was approved by means of Executive Decree 52 dated 30 April 2008, hereinafter referred to as the Banking Law;

Pursuant to the provisions of paragraphs 1 and 2 of Article 5 of the Banking Law, safeguarding the soundness and efficiency of the banking system and strengthening and fostering favorable conditions for the development of the Republic of Panama as an international financial center are objectives of the Superintendency of Banks;

According to paragraphs 3 and 5 of Article 11 of the Banking Law, approving general criteria for the classification of assets at risk and rules for the provision of reserves against risk and establishing the administrative interpretation and scope of the legal provisions and regulations on banking matters are among the technical duties of the Board of Directors;

In accordance with Article 6 of the Banking Law, ensuring that banks maintain sufficient liquidity and solvency ratios to discharge their obligations is one of the duties of the Superintendency of Banks;

Pursuant to the provisions of Article 72 of the Banking Law, the Superintendency may take into account the presence of other risks that may serve to evaluate the need for capital funds, including market risk, operating risk, and country risk, in determining the capital adequacy ratios;

The Basel Committee on Banking Supervision's Core Principles for Effective Banking Supervision establishes that banks must have a comprehensive risk management process, including oversight by the board of directors and top management, to identify, quantify, assess, oversee, report and control or mitigate all substantial risks in a timely manner, as well as to assess capital and liquidity sufficiency associated with the risk profile;

By means of Rule 11-2018 dated 11 September 2018 new provisions on Operational Risk were prescribed;

During its working sessions, the Board of Directors determined it was necessary and advisable to add the accounts that are not part of the business index (IN, for its acronym in Spanish) calculation to the Technical Appendix for determining the entity's risk-weighted assets for operational risk under the updates made by the Basel Committee.

RESOLVES:

ARTICLE 1. The Technical Appendix of Rule 11-2018 shall read:

“TECHNICAL APPENDIX

The Business Index (IN) is defined as follows [(all acronyms are Spanish acronyms)]:

$$IN = CIAD + CS + CF$$

CIAD is the interest, leasing and dividend component

CS is the service component

CF is the financial component

At the same time, each of these components is defined as follows:

$$CIAD = \text{Min} (\text{ABS}(\text{IINT}-\text{GINT}); 0.0225 \times \text{SACD}) + \text{DIV}$$

ABS(x-y) is the absolute value of x – y within the parentheses

Min (x; y) is the value of the lesser of the two quantities x and y

Max (x; y) is the value of the greater of the two quantities x and y.

IINT is the amount of interest income

GINT is the amount of interest payment

SACD is the balance of credits and debt recorded in the assets

DIV is the amount of dividends collected

$$CS = \text{MAX} (\text{OIO}; \text{OGO}) + \text{Max} (\text{IHC}; \text{GHC})$$

OIO is other operating interest

OGO is other operating expenses

IHC is the income from fees and commissions

GHC is the expenses from fees and commissions

$$CF = \text{ABS} (\text{G}_{\text{CN}} - \text{P}_{\text{CN}}) + \text{ABS} (\text{G}_{\text{LB}} - \text{P}_{\text{LB}})$$

G_{CN} is the earnings from the trading portfolio

P_{CN} is the losses from the trading portfolio

G_{LB} is the earnings from the banking book

P_{LB} is the losses from the banking book

The description of the composition of the variables is as follows:

SACD is the amount of the balance of credits and debt recorded in the assets

$$\text{SACD} = \text{SD} + \text{SCR} + \text{SIV} + \text{SR}$$

SD is the balance of deposits in banks and other financial institutions

SCR is the balance of loans granted

SIV is the balance of investment in debt securities

SR is the balance of repos

The calculation of the Business Index for a given quarter will be made as follows:

- For the variables that are part of Profits, the amounts for each of the three months of the quarter will be added together and multiplied by four to annualize the value.
- For the variables that are Balance account items and are part of the SACD variable, the arithmetic average for the three months of the quarter will be calculated.

The following loss and profit account items do not contribute to any IN items:

- Insurance and reinsurance business income and expenses;
- Paid premiums and reimbursements/payments received from purchased insurance and reinsurance policies;
- Administrative expenses, including staffing, outsourcing fees paid for providing nonfinancial services (e.g. logistics, IT or human resources) and other administrative expense (e.g. IT expenses, utilities, telephone, travel, office supplies, mail service);
- Recovery of administrative expenses, including recovery of customer accounts payable (e.g. taxes charged to customers);
- Expenses of business locales and fixed assets (except those resulting from operating risk loss events);
- Amortization of tangible and intangible assets (except amortization related to operational leasing assets, which must be included in financial leasing and operational expenses);
- Provisions or reversal of provisions (e.g. pension disbursements, commitments and collateral provided) except for provisions related to operating risk loss events;

- Expenses for social capital refundable on demand;
- Deterioration of value or reversal of deterioration of value (e.g. financial assets, nonfinancial assets, investments in affiliated companies, joint ventures or related companies);
- Variation of the trading fund recognized in Profit;
- Corporate taxes (taxes on profits, including current and deferred taxes)."

ARTICLE 2. ENACTMENT. This Rule will become effective on the thirty-first (31st) day of December, two thousand nineteen (2019). The relevant reports must be submitted by the thirtieth (30th) day of January, two thousand twenty (2020).

Given in the city of Panama on the thirtieth (30th) day of April, two thousand nineteen (2019).

FOR COMMUNICATION PUBLICATION AND ENFORCEMENT.

THE CHAIRMAN,

THE SECRETARY,

Luis Alberto La Rocca

Joseph Fidanque III