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LICENSING AND SUPERVISION OF BANKING BUSINESS
Directives to Authorize the Business of
Interest Free Banking

Directives Number SBB/51/2011

WHEREAS there has been increasingly strong public demand for interest free banking products in Ethiopia;

WHEREAS supply of such products by banks has to be carried out in a safe and sound manner;

WHEREAS there has been lack of regulatory framework for interest free banking business;

NOW, THEREFORE, in accordance with Article 22(2) of Banking Business Proclamation Number 592/2008, the National Bank of Ethiopia hereby issues these directives.

1. Short Title

These directives may be cited as “Directives to Authorize the Business of Interest Free Banking No. SBB/ 51/2011”

2. Definitions

For the purpose of these directives, unless the context provides otherwise:

- 2.1 “bank” means a company licensed by the National Bank to undertake banking business or a bank owned by the Government;
- 2.2 “interest free banking business” refers to banking business in which mobilizing or advancing funds is undertaken in a manner consistent with Islamic finance principles and mode of operation that avoids receiving or paying interest;
- 2.3 “interest free banking window” refers to a unit within a conventional bank exclusively offering interest free banking services; and
- 2.4 “National Bank” means the National Bank of Ethiopia.

3. Scope

Provisions of these directives shall apply to all banks in Ethiopia engaged in interest free banking business.

4. Authorization

- 4.1 A bank shall obtain a written authorization from the National Bank to carry on interest free banking business.
- 4.2 A bank which wishes to obtain an authorization to carry on interest free banking business shall submit a duly completed application in the prescribed format together with documents specified below:
 - a) a report on resource mobilization and use;
 - b) planned balance sheet structure for interest free window and the whole bank;
 - c) maximum share of planned interest free business in total consolidated balance sheet of the bank;
 - d) risk management framework for all interest free banking products;
 - e) a statement on availability of adequate capacity and facilities to run interest free banking business;
 - f) accounting aspects, such as accounting policies to be followed and profit and loss sharing mechanisms;
 - g) evidence of financial strength as reflected in capital adequacy, asset quality, earnings capability, future earnings prospects, and current liquidity position and forecast for the next 12 months;
 - h) track records of adherence to prudential regulations, credit discipline, quality of customer services ;
 - i) a statement on the convenience as well as the needs of the population of the area to be served by interest free banking services;

j) methods of segregating the funds of interest free banking businesses from all other business ; and

k) such other information as required by the National Bank while processing the application.

4.3 The National Bank shall evaluate the application submitted by a bank in view of risk management, Banking Business Proclamation, applicable directives issued by it as well as other rules and regulations; and upon its satisfaction, may authorize the applicant to open an interest free banking window.

5. Prohibition

5.1 Banks shall not alter maximum share of interest free banking business in their consolidated balance sheet without prior approval of the National Bank.

5.2 Failure to comply with sub-article 1 of this article may result in the closure of interest free banking window.

6. Maintenance of Accounts and Financial Statements

Banks engaged in interest free banking business shall:

6.1 keep separate books of accounts in respect of interest free banking operations and ensure proper maintenance of records for all transactions for segregation of funds.

6.2 report their interest free banking business activities every month to the National Bank.

7. Compliance with Regulatory and Supervisory Requirement

7.1 In conducting interest free banking business, banks shall comply mutatis mutandis with all regulatory and supervisory requirements except National Bank's directives on interest rate.

7.2 Equity participation in a project or a company shall be in strict compliance with " limitation on Investment of Banks Directives No. SBB/12/96".

8. Effective Date

These Directives shall enter into force as of the 1st day of October 2011.