



CENTRAL BANK OF NIGERIA

REVISED GUIDELINES FOR DISCOUNT HOUSES

April 27, 2004

Revised Guidelines for Discount Houses

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A. INTRODUCTION

1. The following guidelines are set out to give effect to the provisions of Section 28 of the Central Bank of Nigeria (CBN) Act 1991 (No. 24) and Sections 56-61 of Banks and Other Financial Institutions Act (BOFIA) 1991(No.25) as amended. This circular supercedes the one dated April, 1999.
2. A discount house means any person in Nigeria who transacts a discount house business which in the main consists of trading in and holding of treasury bills, commercial bills and other securities and whose operations are in the opinion of the CBN those of a discount house.
3. Local Banks and other financial institutions including insurance companies with or without the participation of international finance institutions acceptable to the CBN can subscribe to the shares of a discount house business. However the maximum permissible equity holding for any single investor in a discount house is 40%.
4. The objectives and principal duties of a discount house shall be:
 - a. to promote rapid growth and efficiency of the money market in Nigeria;
 - b. *to act as an intermediary between the Central Bank of Nigeria and the licenced banks in OMO transactions and other eligible securities of not more than three years maturity as defined under the CBN's expanded discount window guidelines;
 - c. to facilitate the issue and sale of short term government securities and other eligible short-term commercial bills;
 - d. to provide discount/re-discount facilities for treasury securities and other eligible financial instruments;
 - e. to provide fund/portfolio management and financial advisory services;
 - f. to accept short term investments on an intermediary basis; and
 - g. other functions which may be prescribed by the CBN from time to time.

B. APPLICATION FOR LICENCE

1. Any person seeking a licence to establish a discount house in Nigeria shall apply in writing to the Governor of the Central Bank of Nigeria.
2. No proposed discount house shall incorporate/register its name with the Corporate Affairs Commission until approval-in-principle has been obtained from the CBN.

3. The application for licence shall be accompanied with the following:
 - a) A non- refundable application fee of N500,000 (five hundred thousand Naira) in bank draft payable to the Central Bank Of Nigeria.
 - b) Two copies of the detailed feasibility report disclosing information that will include:
 - i) the composition of the Board of Directors of the proposed discount house and the curriculum vitae of each member including other directorships held (if any);
 - ii) the organizational structure of the proposed discount house setting out in detail the functions and responsibilities of the top management team;
 - iii) the proposed training programme for staff and management succession;
 - iv) a five-year financial projection for the operation of the proposed discount house indicating its estimated growth and profitability;
 - v) details of the assumptions upon which the financial projections have been made; and
 - vi) the conclusions based on the assumptions made in the feasibility report.
 - c) Two copies of the draft Memorandum and Articles of Association of the proposed discount house.
 - d) A letter of intent to subscribe to the share capital of the discount house signed by two authorized signatories.
 - e) A list of proposed shareholders.
4. In considering an application for a licence, the CBN shall require to be satisfied as to the following:
 - a) The quality of the board and management of the proposed discount house.
 - b) The earnings prospect of the discount house.
 - c) The objects of the discount house as disclosed in the Memorandum and Articles of Association.
5. If satisfied, the CBN shall call upon the promoters to:
 - a) deposit in bank draft the minimum paid-up capital of ₦1,000,000,000 (One billion Naira) or as may be prescribed by CBN from time to time; and
 - b) Submit evidence of payment by each proposed shareholder.
6. Thereafter, the Governor may grant an approval-in-principle for the establishment of a discount house.
7. Before the issuance of the licence the CBN shall request the promoters to:

- a) deposit the licencing fee of ₦ 2,000,000 (Two million Naira) in bank draft payable to the CBN;
 - b) submit the curriculum vitae of the persons who shall occupy the specified top positions in the discount house; and
 - c) submit a copy of the Certificate of Incorporation.
8. If satisfied with 7a, b & c above, the Governor may grant a licence.

C. CONDITIONS PRECEDENT TO THE COMMENCEMENT OF OPERATIONS

1. The promoters of a discount house shall submit the following documents to the CBN before such discount house is permitted to commence operations:
 - a) the shareholders' register in which the equity interest of each shareholder is properly reflected;
 - b) a copy of the share certificate issued to each shareholder;
 - c) two certified true copies of Form CO2 (Return of Allotments) filed with the Corporate Affairs Commission;
 - d) two certified true copies of Form CO7 (Particulars of Directors), and written confirmation that the Board of Directors approved by the CBN has been installed;
 - e) two certified true copies of the Memorandum and Articles of Association filed with the Corporate Affairs Commission;
 - f) the opening statement of affairs audited by a firm of accountants practicing in Nigeria;
 - g) two copies of Certificate of Incorporation of the company (together with the original for sighting purposes only); and
 - h) two copies of letters of offer and acceptance of employment indicating that the management team approved by the CBN has been installed.
2. The discount house shall inform the CBN in writing of the location and address of its Head Office for the purpose of inspection.
3. The discount house shall be informed in writing by the CBN that it may commence business.
4. A copy of the licence shall be displayed in a conspicuous position in the Head Office of the discount house.

5. The discount house shall inform the CBN in writing of the date of commencement of business.

D. MANAGEMENT REQUIREMENTS

The following minimum qualifications and experience are mandatory for officers who may occupy the key/ top management positions in a discount house;

1. *Managing Director/Chief Executive — university degree or professional qualification acceptable to the CBN with at least 15 years post-qualification cognate experience (five years of which must be at top management level).
2. Departmental Head - a university degree or professional qualification acceptable to the CBN with at least 10 years post-qualification cognate experience.
3. Three copies of annual audited accounts of a discount house shall be submitted not later than three months after the end of the accounting year in the forms prescribed by the CBN from time to time.
4. Such annual audited accounts of a discount house shall be published in at least two acceptable national dailies in the form approved by the CBN.
5. Every discount house shall display in a prominent position in every office of its business a copy of its latest duly audited abridged accounts.

E. SOURCES OF FUNDS

1. Equity - Paid-up Capital and Reserves.
2. Call money and short-term borrowings of not more than three years maturity.
Call money placed by banks with discount houses shall form part of the specified liquid assets of the respective banks for the purpose of the liquidity ratio requirement.
3. A discount house that is short of funds may:
 - a) obtain from the CBN an overnight advance against acceptable collateral. However such an advance shall not exceed 20 percent of the total assets of the discount house and shall not in any event be granted if the discount house has exceeded the borrowing limit as prescribed by CBN;
 - b) sell short-term bills and/or other securities to the CBN. The CBN shall provide rediscounting facilities for treasury and other eligible securities; and

c) enter into Repurchase transactions with the CBN using eligible securities.

F. STRUCTURE OF ASSETS

The short-term nature of the liabilities of a discount house requires that its assets be substantially liquid. The assets of a discount house shall consist of the following:

- a) Treasury Bills;
- b) Treasury Certificates;
- c) Negotiable Certificates of Deposit (NCDs);
- d) Bankers' Acceptances;
- e) Commercial Papers (eligible);
- f) Asset-Backed Securities (of not more than three years to maturity);
- g) Federal Government Development Stocks (development stocks not exceeding five years);
- h) Eligible State Bonds (bonds with not more than five years to maturity);
- i) Promissory Notes issued by State Governments; and
- j) Any other securities that may from time to time be approved by the CBN.

G. PRUDENTIAL REQUIREMENTS

Every discount house shall:

- 1. transfer to the statutory reserve a minimum of 15 percent of profit after tax if the reserve fund is less than the paid-up capital and a minimum of 10% if the reserve fund is equal to or more than the paid-up capital;
- 2. maintain capital funds to risk assets ratio of 1:13 and CAR of 10% or as may be prescribed by the CBN from time to time;
- 3. not exceed a maximum ratio of 50:1 between its total borrowing and capital plus reserves without the prior approval of the CBN;
- 4. not grant to any bank, facility of more than 75% of its shareholders' funds unimpaired by losses without the prior approval of the CBN;
- 5. (a) at all times maintain not less than 60% of total borrowing in government securities;

- (b) Any discount house which fails to maintain the 60% of borrowings to government securities is guilty of offence and liable to fine as stipulated in Section 15(4)(b) of BOFIA as amended.
6. shall classify and make provision for its risk assets in line with prudential guidelines for banks;
 7. maintain proper books of accounts;
 8. every discount house shall display its daily rates or interest in a conspicuous position in all its offices;
 9. changes in the discount house's top management and Board of Directors shall be subject to the prior approval of CBN;
 10. every discount house shall appoint an auditor approved by the CBN whose duties shall be to make to the shareholders a report of their annual balance sheet and profit and loss account. The qualifications, duties, powers and responsibilities of the approved auditors shall conform to the provisions of Section 29 of BOFIA 1991, as amended; and
 11. all repurchase transactions (Repos) by discount houses shall be reported on the balance sheet if the securities used are owned by the discount houses with the affected assets remaining in the books of the sellers (discounting houses), while the cash received by them shall be recognized as a liability.

H. OTHER REQUIREMENTS

1. Every discount house shall:
 - a) After settlement each day, send two copies of its returns on
 - i.) assets composition;
 - ii.) borrowing rates;
 - iii.) lending rates;
 - iv.) After settlement each day, submit in a prescribed form two copies of daily returns on its activities to the CBN.
 - b) submit in a prescribed form two copies of weekly returns on its assets and liabilities not later than the third working day of the following week, as may be required by the CBN from time to time;

- c) submit in a prescribed form two copies of the monthly, quarterly, semi-annual returns on assets and liabilities within the first seven days of the reporting period
2. A discount house desiring to open or close any office shall seek the prior approval in writing of the CBN.
3. All advertisements shall be subject to the approval of the CBN.
4. Every discount house shall seek and obtain the approval of the CBN in writing for any proposed:
 - a) arrangement for the sale of its shares or business;
 - b) scheme of reconstruction; and
 - c) scheme to amalgamate with any other company.
5. With the approval of the CBN, a discount house may acquire or hold part of the equity capital of any financial institution subject to the following conditions:
 - a) the shareholding by the discount house in the equity of any financial institution shall not exceed 10% of its shareholders funds unimpaired by losses.
 - b) The aggregate equity investment of a discount house at any time shall not exceed 20% of its paid up capital and statutory reserves.” **BSD/11/2002**

I. PROHIBITIONS

A discount house shall not:

1. grant loan facilities to its directors or the general public;
2. deal in gold or foreign exchange, including the opening of letters of credit;
3. pay any dividend on its shares until all its preliminary expenses and other non-capitalised expenses have been completely written off. For this purpose, an issue of bonus shares out of profits shall be deemed to be a payment of dividend.
4. accept any money or deposit or loan which is repayable on demand by cheque, draft or any other instrument drawn by the depositor on the discount house (cannot open current account); and
5. engage in any business other than those for which it was licensed.

J. CONDITIONS FOR REVOCATION OF LICENCE

The grounds for revoking a licence granted to a discount house may include any of the following:

1. submission of false information/ data during and after the processing of the application for licence;
2. engaging in functions/ activities outside the scope of the licence;
3. persistent failure to comply with any of the guidelines or directives of the CBN or provisions of the BOFIA 1991 as amended;
4. engaging in activities prejudicial to the Nigerian economy;
5. having insufficient assets to meet its liabilities; and
6. any other act(s) which in the opinion of the CBN constitutes a violation of any of the provisions of these guidelines and the BOFIA 1991, as amended.

K. GENERAL

1. Any director who is involved in the management of a licensed discount house shall cease to hold office if:
 - a) he is declared bankrupt by a competent court;
 - b) he is convicted of any offence involving fraud or dishonesty;
 - c) he is of unsound mind.

2.
 - a. No person who had been a director, or been directly involved in the management of a failed licensed discount house, a bank or any other financial institution shall without the express authority of the Governor of the Central Bank of Nigeria act or continue to act as a director or be directly involved in the management of any other licensed discount house.
 - b. Except with the approval of the Bank, no discount house shall have as a director any person who is a director of more than two financial institutions.
 - c. No discount house shall be managed by a person who is:
 - i. a director of any other company not being a subsidiary of a discount house.
 - ii. engaged in any other business.

3. Any person who, being a director or manager of a licensed discount house shall be guilty of an offence if he:
 - a) fails to take reasonable steps to secure compliance by the licensed discount with any provisions of the BOFIA 1991 as amended; and
 - b) fails to take reasonable steps to ensure the accuracy of any statement or information submitted to the CBN in accordance with these guidelines.
4. Banks and other approved financial institutions holding shares in discount houses shall not participate directly in the daily running and management of such discount houses.
5. The penalties for any breach of these guidelines or other regulations of the CBN shall be as set out in the relevant provisions of the CBN Act 1991 and the BOFIA 1991 as amended.

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