



# Banking Regulation

# 2020

**Seventh Edition**

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# Mozambique

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## Introduction

Mozambique's banking sector continues to undergo significant legislative reform. Events of the recent past, such as the Bank of Mozambique's intervention in Moza Banco in September 2016 and the ongoing liquidation of Nosso Banco, amongst others, have exposed fragilities in the legal framework in force. As such, there have been noteworthy regulatory developments aiming at harmonisation with Basel core principles and addressing prudential concerns, such as capitalisation and liquidity requirements in the banking sector, as well as others addressed in this chapter.

The developments in place are expected to impact the current players in the sector and yet more legislative reform is foreseeable, including the introduction of more clear-cut proceedings for the liquidation of credit institutions.

The Mozambican banking system comprises 22 banks; however, most of the system's activity is focused on five large (and still operating) banks and, since 2015, has been subject to a series of interventions by the Central Bank (the Bank of Mozambique – *Banco de Moçambique* or the “**BM**”) in order to implement policies targeting concerns relative to foreign exchange reserves, inflation and currency devaluation, as well as rules and regulations pertaining to own funds and to structural liquidity and sustainability. In 2019, the interventions of the BM, in the area of banking supervision, resulted in the filing infringement proceedings that resulted in the imposition of fines unprecedented in the history of the Mozambican banking sector and which affected most of the banks operating in the national territory.

In terms of the capital markets, the Mozambique Stock Exchange recently registered a weak participation of local companies therein, therefore, they launched the Third Market Service (“**Service**”) with the purpose of revitalising the sector. This Service is expected to help overcome some of the obstacles faced with the implementation of the stock exchange legal framework in force and provide an optimistic perspective to local companies in the registration process before the Stock Exchange.

Thus, it is intended to have all relevant stake holders, such as the State-Owned Companies Institute (“**IGEPE**”), the Tax Authority, the Superior Institute of Accounting and Auditing as well as the Confederation of Economic Associations of Mozambique (“**CTA**”) for the successful and efficient implementation of this Service.

## Regulatory architecture: Overview of banking regulators and key regulations

The Bank of Mozambique is the Mozambican central bank and is the entity responsible for banking supervision and which serves as the regulatory authority. Its activity is subject to the

rules under its organic statute, set down by Law no. 1/92, of 3 January 1992. In all matters not expressly reserved for the Ministry in charge of the area of finance, the supervision, regulation and promotion of the securities market in Mozambique is within the competence of the BM. The central bank is incumbent as the banker of the Mozambican State, as advisor to the Government in financial matters, counsel and manager of monetary and exchange policies and of foreign exchange reserves. It also acts as intermediary in international monetary relations and as supervisor to financial institutions operating in the country.

Without prejudice to the above, it is worth noting that the activities of conducting securities investment services are entrusted to the supervision and regulation of the Exchange Commission (*Central de Valores Mobiliários* – the “CVM”). The Securities Market Code (*Código do Mercado de Valores Mobiliários* – the “CMVM”), approved by Decree Law no. 4/2009, of 24 July 2009, as amended from time to time, is the core legislation for securities, issuers, public offers, regulated markets, investment services in securities, as well as for related supervision and regulation.

Additionally, the supervisory role in Mozambique falls on the Mozambique Insurance Supervision Institute (*Instituto de Supervisão de Seguros de Moçambique* – the “ISSM”), which has the duty to regulate and supervise insurance companies and other entities that are authorised to pursue insurance-related activities, such as insurance mediation, reinsurance and management of complementary pension funds.

The current banking system in Mozambique is underpinned by an institutional model of supervision, and it is the BM itself that issues prudential and conduct standards.

The establishment and exercise of the activities of credit institutions and financial companies in Mozambique is regulated by Law no. 15/99 of 1 November 1999 (the Credit Institutions and Financial Companies Law), as amended from time to time, and further detailed by Decree no. 56/2004, of 25 December 2004 (Regulation of the Law Applicable to Credit Institutions and Financial Companies), as amended from time to time, which sets out the procedures and standards applicable to such entities as a whole, as well as the specific legal frameworks applicable to each type of entity. These legal instruments determine the general requirements for the incorporation of credit institutions and financial companies, as well as the procedure for their authorisation by the BM. Also, given that credit institutions in Mozambique are incorporated as public limited companies (*sociedades anónimas*), the rules established in the Commercial Code (*Código Comercial Moçambicano*) should also be taken into account. These are, therefore, the main sources of the regulatory framework that should be analysed in terms of regulation of banking and credit institutions in Mozambique. Nevertheless, and without prejudice to the points of focus set out in the following paragraphs, other regulations apply.

As for the foreign exchange market, it is regulated by Law no. 11/2009, of 11 March 2009 (“**Foreign Exchange Law**”), and by Notice no. 20/GBM/2017, of 27 December 2017, published by the BM in the exercise of its role as the Foreign Exchange Authority of the Republic of Mozambique.

The regulation of the financial system in Mozambique has been under development for the past few years and several matters have, therefore, become subject to further (or first efforts at, in some cases) regulation. Examples are:

1. the prevention and combat of money laundering and of the financing of terrorism (implemented by Law no. 14/2013, of 12 August and further developed by Decree no. 66/2014);
2. the deposit guarantee mechanism, which has been established for the protection of depositors in commercial banks (as per Decree no. 49/2010);

3. on microfinance matters, the incorporation and functioning of entities allowed to operate in the microfinance market may be found in the Regulation of Microfinance, approved by Decree no. 57/2004; and
4. in terms of structural subjects, banking activities and credit institutions' regulations should also be noted, especially when referring to minimum capital requirements and rules (as set out by BM Notice 07/GBM/2017), bank card regulation (as per Notice of the BM, no. 10/GBM/2017), interbank clearing and settlement subsystem regulation (as per Notice of the BM, no. 02/GBM/2019), information duties in relation to the receipt of bank deposits regulation (as per Notice of the BM, no. 01/GBM/2019), and requirements for the identification of domestic credit institutions of systemic importance in the Mozambican banking system regulation (as per Notice of the BM, no. 10/GBM/2018), which assumes a special relevance in a developing market such as Mozambique's.

Similarly to the internationally prevalent practice, banks established and authorised in Mozambique are allowed to engage in a variety of financial activities – as permitted by law, such as: accepting deposits from the general public; entering into credit transactions, including the granting of guarantees, and payment transactions; undertaking the issuance and management of means of payment (such as credit cards, travellers' cheques and credit letters), as well as other transactions relating to money market instruments, financial instruments or foreign exchange instruments, whether for their own account or the account of others; activities related to the issue and placing of securities; safekeeping, administration and management services for securities portfolios; precious metal trading; and insurance marketing relations.

Banking or credit institutions that are established in Mozambique are also allowed to undertake analogous activities, insofar as they are not prohibited by law, such as finance leasing and factoring services, subject to prior BM authorisation.

### **Recent regulatory themes and key regulatory developments**

In its capacity as regulator and supervisor of the Mozambican financial system, the BM has issued, from time to time, several Notices designed to address the specific needs of the Mozambican banking sector. To this end, various regulatory changes have been introduced, of which the following are of particular relevance: (i) changes to the rules and procedures relating to foreign exchange transactions; (ii) changes to the requirements and rules on the ratios and prudential limits of credit institutions; (iii) changes to the rules relating to own funds of credit institutions subject to the BM's supervision; (iv) the introduction of prudential limits to the exposure of credit institutions; and (v) the introduction of a formula to be used in order to identify credit institutions of systemic or quasi-systemic relevance.

Attention should also be drawn to the introduction of new minimum capital requirements for credit institutions, financial companies and microfinance companies, as well as to the rules applicable to the payment of overseas transactions via international bank cards, as referred to in the following paragraphs.

It is important to highlight Notice no. 20/GBM/2017, which approves the standards and procedures for foreign exchange transactions, and to draw attention to the changes introduced with respect to the registration and authorisation of such transactions, which underscore the growing liberalisation and digitisation of these transactions. The implementation of a framework specific to the mining sector must also be highlighted, as this sector was not previously covered.

As a result of this Notice, credit institutions are now responsible for the registration of all foreign exchange transactions, and the requirement for prior authorisation for a considerably

larger number of capital transactions has been simplified, in such a manner that, subject to the fulfilment of certain criteria, the same transactions may be deemed pre-approved by the BM. This evidences the commitment to the simplification of, and the reduction in the bureaucracy related to, foreign exchange transactions and, more generally, increasing procedural speed. Regarding the dispositions which determine the ratio and prudential limits of credit institutions, we also highlight that Notice no. 08/GBM/2017 increases the solvency ratio for banks (from 8 per cent to a minimum of 12 per cent by 2020), which is a clear attempt to align with the Basel II recommendations, aiming to ensure adequate liquidity and solvency levels. Notice no. 07/GBM/2017 approved the minimum capital requirements for credit institutions, financial companies and operators; it affects commercial banks only and raises minimum capital requirements from 70,000,000 MT to 1,700,000,000 MT, to better address the risks inherent to their business as well as current trends in the national economy. For overseas payments using international bank cards, such Notice has also introduced relevant regulation. The BM has, additionally, restarted the process of liberalising the use of international bank cards for overseas payments, withdrawing the annual 700,000 MT limit for such transactions. Prior to that, as a response to the 2008 crisis, and to prevent and mitigate negative financial impacts and/or crises in the banking sector, the BM issued Notice no. 02/GBM/2013 to promote financial stability and to safeguard depositor interests, and the Mozambican banking system more generally.

Additional international relevance may be indicated in light of Notice no. 03/GBM/2013, which regulates Emergency Liquidity Assistance and aims to ensure the proper operation of solvent commercial banks, which continue to attract deposits but face temporary liquidity issues, as well as to mitigate any issues which could cause systemic problems in, and compromise the normal functioning of, the banking system.

It should be further noted that the BM has established, under Notice no. 5/GBM/2018, of 6 June, having article 8(3) repealed by Notice no. 7/GBM/2019, certain prudential limits to the exposure of credit institutions to other entities. Pursuant to the same Notice, which specifically targets the concern over concentration of exposure, limits are imposed which vary based on the nature of the relationship between the credit institutions and other entities. Further, the same prudential limits are determined based on what percentage of the credit institution's own funds each exposure to a given entity represents.

In order to increase its level of supervision, it is worth mentioning that the BM introduced the requirement for banks to regularly disclose information relating to their solvency and liquidity levels, as well as introduce a system under which credit institutions and financial companies which are sanctioned for offences are also publicly disclosed, so as to deter non-compliance and foster stability.

For the future, the BM intends to reinforce its supervision of such entities in order to avoid potential risks, and to adopt measures designed to ensure that institutions, as a whole, align with international practice and comply fully with all standards and recommendations, so as to safeguard the financial health of financial institutions. In the context of market stability maintenance measures, regulatory reform aligned with Basel II is anticipated which will reinforce supervision of the cross-border activity of institutions. A reform of the Credit Institutions and Financial Companies Law to include a framework for the resolution of banks, tailored to the Mozambican financial sector, is also anticipated.

Further, it should be noted that, pursuant to Notice no. 10/GBM/2018, 22 October 2018, the BM has introduced a formula to be used for the purpose of identifying all credit institutions

of systemic importance within the Mozambican banking system. The formula is based on: (i) the **size** of the credit institution, in terms of market share within the domestic banking system; (ii) its **interconnectedness** with other credit institutions; and (iii) its **substitutability**, and it is to be applied annually to each credit institution. Thereafter, the BM shall compile a list including all banks of systemic or quasi-systemic importance and publish it, annually. It is expected that further legislation will follow concerning duties specifically applicable to entities included in the said list, the current legislation imposing only certain additional capital requirements for same institutions.

Lastly, under this category, the BM published Notice no. 8/GBM/2019, of 8 August 2019, which sets forth the method applicable to the calculation and creation of mandatory reserves for credit institutions and financial companies, repealing Order no. 12/GBM/2017, of 9 June 2017. The new rules came into effect on 9 August 2019. This Notice shall confer more flexibility to the liquidation management of the credit institutions involves.

### **Bank governance and internal controls**

Banking financial institutions must be incorporated using one of the legal forms established by Mozambican law, which is in the form of a private limited liability company by *shares (sociedade anónima)*. Shares representing the relevant share capital are required to be nominative, thus allowing knowledge of the identity of the holder, and the share capital must be fully issued and paid-up at the time of the incorporation. These and other additional legal requirements, including the composition of the boards and senior management of banks, are set out in Law no. 9/2004, of 21 July 2004 (“**Law no. 9/04**”).

Law no. 9/04 stipulates the requirement of adequate experience for the performance of the specific role of those holding positions of responsibility in credit institutions and financial companies, in particular the members of the board of directors and members of the audit committee. Experience is deemed adequate when the person in question has previously and competently held positions of responsibility in the financial sector, or has a recognised degree of competence in economic, legal or management matters. The duration, responsibilities and nature of the prior experience must be commensurate with the nature and size of the financial institution in question.

The internal control structure applicable to credit institutions and financial entities has been primarily established by BM Notice no. 11/GGBM/99. Risk management and compliance rules are then further developed by BM Notice no. 9/GBM/2017 which, in addition to the internal regulation of accounting practices, business risk and adequate organisational structuring policies, imposes the adoption of prudential limitations and ratios, including limits to the concentration of risks that ought to be duly observed by the banks. Furthermore, BM Notice no. 04/GBM/2013 is a crucial piece of legislation, as it establishes the guidelines for risk management (*Directrizes de Gestão do Risco*) in order to guarantee the safe and robust operation of credit institutions in general, and for their risk-management systems in particular.

One of the most important roles of management is to create and maintain an effective control system, including adherence to reporting lines and the appropriate division of tasks such as between negotiation, custodial and back-office tasks. In effect, the appropriate division of tasks is an essential element to a robust, internal, risk-management-control system. Shortcomings in the implementation and maintenance of an adequate system for the division of tasks could lead to substantial losses, or in other ways compromise the financial health of the institution. The previously mentioned guidelines for management of such centralised services are, from time to time, reviewed by the BM, as the supervisory entity of financial banking institutions.

In this sense and according to such guidelines, institutions must develop risk-management systems which should be reviewed at least once a year and should take into account the control and mitigation of the following risks: credit risk; liquidity risk; interest rate risk; foreign exchange rate risk; operational and strategic risks; and reputational, compliance and IT risks.

As influenced by European and American best practices, it is imperative that risk-management processes implemented by financial banking institutions in Mozambique should pursue the optimisation of the risk/return ratio with which such institutions are faced, and not risk minimisation as it is commonly understood, mainly by implementing four key processes:

- (i) Identification: Financial banking institutions must be able to identify existing or foreseeable risks.
- (ii) Measurement: Once identified, risks shall be measured in order to determine their impact on the returns or capital of the institution.
- (iii) Control: Once measured, the institution must establish and disclose risk-mitigation policies, standards and procedures, which should define responsibilities and lines of authority and together control exposure to the various risks inherent to the institution's activities.
- (iv) Monitoring: Institutions are required to implement an information and management system which effectively monitors risk levels and facilitates the timely adjustment of risk positions and exceptions.

### **Bank capital requirements**

Banks established in Mozambique, in line with other jurisdictions, notably in Europe, are required to comply with a number of requirements and rules to ensure an adequate level of liquidity and solvability. Previously mentioned Notice no. 04/GBM/2013, of 18 September (“**Notice no. 04/GBM/2013**”), further develops the minimum levels of own funds, ratios and prudential limits which have been developed in order to ensure the sustainability of banking activities.

By way of introduction, the Mozambican financial system adopted the Basel II *core principles*, in the terms incorporated by BM Notice no. 03/GBM/2012, of 13 December (fully applicable since 2014), aiming to implement in the Mozambican financial and banking sector more sophisticated risk-assessment techniques, particularly with regard to credit, market and operational risk. Such internationally harmonised principles have already been developed, in a primary form, by the Mozambican legislation, namely regarding minimum capital requirements and limitations; having adopted the Basel II principles, it is foreseeable that, in the future, the Regulator will focus on developing risk-assessment matters, especially regarding credit, operational and market risk, as well as market discipline rules, in line with the principles established in the abovementioned BM's Notice.

Through Notice no. 04/GBM/2013, the BM began implementing prudential rules aligned with the Basel II principles. It established a set of guidelines, based on international best practice, regarding the categories of risk inherent to the most relevant banking activities in Mozambique, namely: credit; liquidity; interest rate; foreign exchange rate; operational; strategic; reputational; compliance; and IT risks.

That said, in terms of relevant rules in this respect, the minimum share capital requirement of 70,000,000 MT, as established by Notice no. 4/GGBM/2005, of 29 December, has been repealed by Notice no. 07/GBM/2017 and was, thereby, increased to 1,700,000,000 MT. This increase is a clear result of Basel II and, in short, seeks to implement a set of reforms



designed to increase the quantity and quality of capital, to reduce leverage and pro-cyclicality, and to improve liquidity management. The understanding is that, together, these measures will achieve increased transparency of the financial system, an improved loss-absorption capacity and a significant reduction in the assumption of risk, which will result in a stronger, more resistant banking system in the face of adverse conditions, thus promoting the necessary confidence to foster sustainable economic growth.

Regulatory capital and liquidity requirements in Mozambique are derived from international standards, as the abovementioned Basel II rules, which should be understood as the new international accord on capital adequacy. Like its predecessor, this new regulatory framework defines its scope in three distinct pillars: Pillar 1 – Capital Requirements (capital, risk cover and leverage control); Pillar 2 – Risk Management and Supervision; and Pillar 3 – Market Discipline.

This being the case, Basel II encompasses a set of reforms conducive to the overall strengthening of capital, which are principally reflected in the composition of financial institutions' capital, not only through the increase to minimum requirements in terms of own funds, but also through the creation of capital standards, as envisaged by this new regulatory framework. In the same vein, the introduction of a new leverage ratio, together with the guidelines regarding counterparty credit risk and systemic risk, share the same objective.

### **Rules governing banks' relationships with their customers and other third parties**

For many years, there was no specific legal framework addressing the relationship between a bank and its customers in Mozambique. The Credit Institutions and Financial Companies Law did, however, contain a number of general duties with which banks had to comply with regard to their relationship with their customers.

Banking institutions in Mozambique were required to provide customers in each line of business with high levels of technical competence through the necessary human resources and materials for the provision of services, with an appropriate standard of quality and efficiency. Their actions must be organised in the light of principles of diligence, independence, loyalty, discretion and respect for the interests of clients and of the bank itself, with which they are entrusted, as well as compliant with applicable disclosure requirements (relating to rates applicable to lending and borrowing transactions and the cost of services rendered).

Further, the Mozambican Association of Banks (*Associação Moçambicana dos Bancos* or “AMB”), a non-profit organisation which pursues the development of technical, economic and social activities of banks operating and authorised in Mozambique, and of which all such banking institutions are members, published in 2006 a Banking Code of Conduct (*Código de Conduta Bancária*) which sought to govern the relationship between AMB credit institutions, as well as the relationship of those institutions with their customers.

Most recently, the BM has enacted Notice no. 02/GBM/2018, of 14 April, under which the Code of Conduct for Credit Institutions and Financial Companies is set. Pursuant to the same code, which is legally binding, the conduct of the abovementioned entities shall be governed by principles of: (i) assistance to the client; (ii) celerity; (iii) clarity; (iv) competence and credibility; (v) integrity; (vi) legality; (vii) non-discrimination; and (viii) respect for good banking practices. The aforementioned code of conduct sets down certain specific duties for financial entities related to, *inter alia*, information to clients (e.g., about financial products), data protection, as well as abusive contractual clauses and practices.

The Mozambican banking sector includes a variety of credit institutions, each with its own scope of activity (such as financial leasing companies, credit cooperatives, investment

companies, etc.). In spite of that, banking financial institutions are specifically authorised to undertake all activities within the scope of other credit institutions, as well as accepting deposits, credit and payment transactions, money market transactions, financial and foreign exchange transactions, and investment services.

In terms of specific authorised activities towards customers, similarly to other jurisdictions, namely in Europe, deposit-taking is an activity which only four categories of credit institutions may undertake: banks; microfinance institutions; credit cooperatives; and credit and savings organisations. Among them, only banks and microfinance institutions are authorised to take deposits from the general public, whilst credit cooperatives and credits and savings organisations may only take deposits from their members. As well as banks, investment companies, microfinance institutions, credit cooperatives and microfinance operators can also undertake credit transactions.

Banks and brokerage firms are the only entities which may undertake money-market transactions for their own account. There is no banking ombudsman in Mozambique, nor does the concept of a class action exist.

It should also be mentioned that the Mozambican banking system has in place a Deposit Guarantee Fund (*Fundo de Garantia de Depósitos*) (the “FGD”), as established by Decree no. 49/2010, the objective of which is to refund deposits made in credit institutions, which cannot make such refunds, whether for reasons directly related to their financial situation or because their licence has been revoked. This fund is financed through periodic contributions made by credit institutions. The FGD currently guarantees up to 20,000 MT per depositor per credit institution.

Finally, due to the risk of money laundering activities being undertaken through cross-border bank transfers, the applicable legislation expressly requires that banks: (i) identify and verify the identity of the correspondent bank; (ii) gather sufficient information pertaining to the correspondent bank in order to understand the nature of its business and determine, in light of publicly available information, its reputation and the nature of its supervision; (iii) obtain necessary approvals from the correspondent bank’s management in order to establish the correspondent relationship, and document in writing the responsibilities of the correspondent and client bank; (iv) ensure that the client bank verifies the identity of, and applies all continuous monitoring measures regarding, clients with direct access to accounts in the correspondent bank; as well as (v) ensure that the bank is authorised to disclose the necessary identification details of its customers.

Law no. 14/2013, of 12 August, (which approves the Law on the Prevention of Money Laundering) establishes the legal framework and preventative and suppression measures with regard to the use of the financial system and non-financial entities for the purpose of money laundering and financing terrorism. In essence, the Law establishes certain duties on financial institutions, such as the duty: to identify and verify the identity of their customers; to notify the Mozambican Financial Information Office (*Gabinete de Informação Financeira de Moçambique*) (the “GIFiM”) of any suspicious transactions; to refrain from effecting transactions in the event there are grounds to suspect a crime; and to cooperate with the legal authorities, among others.

Additionally, Decree no. 66/2014, of 29 October 2014 (Regulation on the Prevention of Money Laundering) establishes the procedures to implement the prevention and suppression measures laid down in the Law on the Prevention Money Laundering. In this regard, it is worth mentioning that the BM issued Notice no. 04/GBM/2015, of 17 June, which establishes the guidelines for, and steers financial institutions in regard to, the prevention of these types of crime.

## **Other financial actions carried out by the BM in 2019**

This year, the Bank of Mozambique reduced its benchmark interest rate from 15 to 12.75 per cent, which, according to the Governor, contributed to the interest rate of commercial banks, applied to preferred customers, from 20.20 to 18 per cent.

Further, following the blackout in the payments system, the BM enacted Notice no. 03/GBM/2019, of 8 March, regarding intraday credit, Notice no. 04/GBM/2019, of 8 March, regarding the real-time wholesale transfer settlement subsystem and the clearing and the interbank settlement subsystem. With the approval of these Notices the BM will make the payment system more reliable and in line with international practices.

In the foreign exchange outlook, the BM has increased the proportion of foreign currency deposits that commercial banks are required to maintain in the regulator from 27 per cent to 36 per cent, and has introduced reforms, such as Notice no. 11/GBM/2018, of 07 December, regulating the conditions for buying and selling foreign currency in the domestic market, temporarily suspending transactions using forward exchange rates.

Also, in this outlook, the BM carried out the implementation of the Term of Commitment of Banking Intermediation of Importation of Goods, “thus marking another step in the fulfilment of the duty to use banks in foreign trade operations”.

In the context of financial stability, the BM approved Notice no. 01/GBM/2019, of 1 February, that establishes the information obligations on deposit reception, before and during the term of deposit agreements with commercial banks.

## **Acknowledgment**

The authors would like to thank Isabel Ferreira dos Santos for her invaluable assistance in writing this chapter. Isabel joined VdA in 2017. She is an Associate at the Banking & Finance practice where she has been involved in several transactions. Isabel is admitted to the Portuguese Bar Association.

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Guilherme Daniel is the Founder of Guilherme Daniel & Associados in 2016. In such capacity, he is actively involved in several matters mainly in Corporate, Energy and Natural Resources (particularly, Oil & Gas) and Infrastructure.

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Gonçalo joined Guilherme Daniel & Associados in 2017, as an Associate, and has concentrated his practice on matters related to Banking, Exchange Control, Corporate and Energy & Natural Resources. He worked with Uría Menéndez – Proença de Carvalho as a Trainee Lawyer and later as a Junior Associate, between 2014 and 2017, in the departments of Litigation, Corporate and Finance.

Gonçalo holds an LL.M. degree from the University of Cambridge and a Law Degree from Universidade Católica Portuguesa. He is admitted to the Mozambican Bar Association.

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