भारतीय रिज़र्व बैंक
RESERVE BANK OF INDIA

RBI/DOR/2025-26/151

DOR.CAP.REC.70/21-01-002/2025-26 November 28, 2025

Reserve Bank of India (Commercial Banks- Prudential Norms on Capital Adequacy) Directions, 2025

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In exercise of the powers conferred by section 35A of the Banking Regulation Act (BR Act), 1949 the Reserve Bank of India being satisfied that it is necessary and expedient in the public interest and in the interest of banking policy so to do, hereby, issues the Directions hereinafter specified.

Chapter I
Preliminary

A Short title and commencement

1. These Directions shall be called the Reserve Bank of India (Commercial Banks - Prudential Norms on Capital Adequacy) Directions, 2025.

2. These Directions shall come into effect immediately upon issuance.

B Applicability

3. These Directions shall be applicable to Commercial Banks (hereinafter collectively referred to as 'banks' and individually as a 'bank').

   For the purpose of these Directions, 'Commercial Banks' means banking companies (other than Small Finance Banks, Payment Banks, and Local Area Banks), corresponding new banks, and the State Bank of India, as defined respectively under clauses (c), (da), and (nc) of Section 5 of the Banking Regulation Act, 1949.

C Definitions

4. In these Directions, unless the context states otherwise, the terms herein shall bear the meanings assigned to them below:

(1) 'Banking book' shall mean all items which are not included under trading book as per these Directions;

(2) 'Capital Market Exposure' shall have the same meaning as defined in Reserve Bank of India (Commercial Banks – Concentration Risk Management) Directions, 2025;

(3) 'Central Counterparty' (CCP) is a clearing house that interposes itself between counterparties to contracts traded in one or more financial markets, becoming the buyer to every seller and the seller to every buyer and thereby ensuring the future performance of open contracts. A CCP becomes counterparty to trades

with market participants through novation, an open offer system, or another legally binding arrangement. For the purposes of the capital framework, a CCP is a financial institution;

(4) ‘Clearing Member’ is a member of, or a direct participant in, a CCP that is entitled to enter into a transaction with the CCP, regardless of whether it enters into trades with a CCP for its own hedging, investment, or speculative purposes or whether it also enters into trades as a financial intermediary between the CCP and other market participants. For these Directions, where a CCP has a link to a second CCP, that second CCP is to be treated as a clearing member of the first CCP. Whether the second CCP’s collateral contribution to the first CCP is treated as initial margin or a default fund contribution shall depend upon the legal arrangement between the CCPs. In such cases, if any, the Reserve Bank shall be consulted for determining the treatment of this initial margin and default fund contributions;

(5) ‘Client’ in the context of transactions with a CCP is a party to a transaction with a CCP through either a clearing member acting as a financial intermediary, or a clearing member guaranteeing the performance of the client to the CCP;

(6) ‘Counterparty Credit Risk (CCR)’ is the risk that the counterparty to a transaction could default before the final settlement of the transaction's cash flows. An economic loss would occur if the transactions or portfolio of transactions with the counterparty has a positive economic value at the time of default. Unlike a bank’s exposure to credit risk through a loan, where the exposure to credit risk is unilateral and only the lending bank faces the risk of loss, CCR creates a bilateral risk of loss i.e., the market value of the transaction can be positive or negative to either counterparty to the transaction. The market value is uncertain and can vary over time with the movement of underlying market factor;

(7) ‘Credit Risk’ is defined as the potential that a bank's borrower or counterparty may fail to meet its obligations in accordance with agreed terms. It is also the possibility of losses associated with diminution in the credit quality of borrowers or counterparties;

(8) ‘Credit Valuation Adjustment’ is an adjustment to the mid-market valuation of the portfolio of trades with a counterparty. This adjustment reflects the market value

of the credit risk due to any failure to perform on contractual agreements with a counterparty. This adjustment may reflect the market value of the credit risk of the counterparty or the market value of the credit risk of both the bank and the counterparty;

(9) 'Cross Product Netting' refers to the inclusion of transactions of different product categories within the same netting set;

(10) 'Current Exposure' is the larger of zero, or the market value of a transaction or portfolio of transactions within a netting set with a counterparty that would be lost upon the default of the counterparty, assuming no recovery on the value of those transactions in bankruptcy. Current exposure is often also called Replacement Cost;

(11) 'Default Funds', also known as clearing deposits or guarantee fund contributions (or any other names), are clearing members' funded or unfunded contributions towards, or underwriting of, a CCP's mutualised loss sharing arrangements. The description given by a CCP to its mutualised loss sharing arrangements is not determinative of their status as a default fund; rather, the substance of such arrangements shall govern their status;

(12) 'Deferred Tax Assets' and 'Deferred Tax Liabilities' shall have the same meaning as assigned under the applicable Accounting Standards;

(13) 'Derivative' shall have the same meaning as assigned to it in Section 45U(a) of the RBI Act, 1934;

(14) 'General market risk' means the adverse movement in the price of an individual security due to general market conditions;

(15) 'Going-concern Capital', from regulatory perspective, is the capital which shall absorb losses without triggering bankruptcy of the bank;

(16) 'Gone-concern Capital', from regulatory perspective, is the capital which shall absorb losses only in a situation of liquidation of the bank;

(17) 'Initial margin' means a clearing member's or client's funded collateral posted to the CCP to mitigate the potential future exposure of the CCP to the clearing member arising from the possible future change in the value of their transactions. For the purposes of these guidelines, initial margin does not include contributions

to a CCP for mutualised loss sharing arrangements (i.e., in case a CCP uses initial margin to mutualise losses among the clearing members, it shall be treated as a default fund exposure);

(18) 'Investments in entities that are outside of the scope of regulatory consolidation' shall mean investments in entities that have not been consolidated at all or have not been consolidated in such a way as to result in their assets being included in the calculation of consolidated risk-weighted assets of the group;

(19) 'Legal risk' includes, but is not limited exposure to fines, penalties, or punitive damages resulting from supervisory actions, as well as private settlements;

(20) 'Leverage Ratio' is the capital measure (the numerator) divided by the exposure measure (the denominator), with this ratio expressed as a percentage;

$$\text{Leverage Ratio} = \frac{\text{Capital Measure}}{\text{Exposure Measure}}$$

(21) 'Market risk' means the risk of losses in on-balance sheet and off-balance sheet positions arising from movements in market prices;

(22) 'Member Lending Institutions (MLIs)' are as defined in respective schemes of the National Credit Guarantee Trustee Company Ltd (NCGTC);

(23) 'Netting Set' is a group of transactions with a single counterparty that are subject to a legally enforceable bilateral netting arrangement and for which netting is recognised for regulatory capital purposes. Each transaction that is not subject to a legally enforceable bilateral netting arrangement that is recognised for regulatory capital purposes shall be interpreted as its own netting set for the purpose of these rules;

(24) 'Offsetting transaction' means the transaction leg between the clearing member and the CCP when the clearing member acts on behalf of a client (e.g., when a clearing member clears or novates a client's trade);

(25) 'One-Sided Credit Valuation Adjustment' is a credit valuation adjustment that reflects the market value of the credit risk of the counterparty to the bank but does not reflect the market value of the credit risk of the bank to the counterparty;

(26) ‘Operational risk’ means the risk of loss resulting from inadequate or failed internal processes, people, and systems or from external events. This includes legal risk but excludes strategic and reputational risk;

(27) ‘Other approved securities’ shall have the same meaning as defined under the Reserve Bank of India (Commercial Banks – Cash Reserve Ratio and Statutory Liquidity Ratio) Directions, 2025;

(28) ‘Outstanding EAD’ for a given OTC derivative counterparty is defined as the greater of zero and the difference between the sum of EADs across all netting sets with the counterparty and the credit valuation adjustment (CVA) for that counterparty which has already been recognised by the bank as an incurred write-down (i.e., incurred CVA loss);

(29) ‘Qualifying central counterparty (QCCP)’ is an entity that is licensed to operate as a CCP (including a license granted by way of confirming an exemption) and is permitted by the appropriate regulator / overseer to operate as such with respect to the products offered. This is subject to the provision that the CCP is based and prudentially supervised in a jurisdiction where the relevant regulator / overseer has established, and publicly indicated that it applies to the CCP on an ongoing basis, domestic rules and regulations that are consistent with the CPSS-IOSCO Principles for Financial Market Infrastructures;

(30) ‘Securities financing transactions (SFTs)’ are transactions such as repurchase agreements, reverse repurchase agreements, security lending and borrowing, collateralised borrowing and lending (CBLO) and margin lending transactions, where the value of the transactions depends on market valuations and the transactions are often subject to margin agreements;

(31) ‘Specific risk’ means the risk of an adverse movement in the price of an individual security owing to factors related to the individual issuer;

(32) ‘Subsidiary’ shall mean an enterprise that is controlled by another enterprise (known as the parent). The definition of ‘control’ shall be as given in the applicable Accounting Standards;

(33) ‘Trade exposures’ include the current exposure and potential future exposure of a clearing member or a client to a CCP arising from Over-the-counter (OTC) derivatives, exchange traded derivatives transactions or SFTs, as well as initial

margin. The current exposure of a clearing member includes the variation margin due to the clearing member but not yet received;

(34) 'Trading book' shall include all instruments that are classified as 'Held for Trading' as per Reserve Bank of India (Commercial Banks – Classification, Valuation, and Operation of Investment Portfolio) Directions, 2025;

(35) 'Tranche' means a contractually established segment of the credit risk associated with an exposure or a pool of exposures, where a position in the segment entails a risk of credit loss greater than or less than a position of the same amount in another segment, without taking account of credit protection provided by third parties directly to the holders of positions in the segment or in other segments.

Explanation - Securitisation notes issued by the SPE and credit enhancement facilities available shall be treated as tranches;

(36) 'Tranche maturity' means the tranche's effective maturity in years and is measured as prescribed in paragraphs 107 to 109;

(37) 'Tranche thickness' means the measure calculated as detachment point (D) minus attachment point (A), where D and A are calculated in accordance with paragraphs 102 to 106; and

(38) 'Variation margin' means a clearing member's or client's funded collateral posted on a daily or intraday basis to a CCP based upon price movements of their transactions.

The terms appearing in paragraphs 88 to 126 on 'Securitisation Exposures' shall bear the meanings assigned to them under Reserve Bank of India (Commercial Banks – Securitisation Transactions) Directions, 2025, unless stated otherwise herein.

5. All other expressions unless defined herein, shall have the same meaning as have been assigned to them under the applicable Acts, rules / regulations made thereunder, or any statutory modification or re-enactment thereto or as used in commercial parlance, as the case may be.

Chapter II

Board approved policies and scope of application of capital adequacy framework

A Instructions regarding Board approved policies and documents to be reviewed by the Board

6. A bank shall have a Board approved policy on the following matters pertaining to capital adequacy:

   (i) The structure, design and contents of a bank's Internal Capital Adequacy Assessment Process (ICAAP) should be approved by the Board of Directors to ensure that the ICAAP forms an integral part of the management process and decision-making culture of a bank;

   (ii) A bank shall have an explicit Board-approved capital plan which should spell out the institution's objectives in regard to level of capital, the time horizon for achieving those objectives, and in broad terms, the capital planning process, and the allocated responsibilities for that process;

   (iii) A bank shall have a formal disclosure policy approved by the Board of Directors that addresses a bank's approach for determining what disclosures it shall make and the internal controls over the disclosure process.

7. A bank's Board of Directors shall assess and document, at least once a year, whether the processes relating to the ICAAP implemented by a bank successfully achieve the objectives envisaged by the Board.

B Scope of application of capital adequacy framework

8. The scope of application of capital adequacy framework shall be as under.

(1) A bank shall comply with the capital adequacy ratio requirements at two levels:

   (i) the standalone ('Solo') level capital adequacy ratio requirements, which measure the capital adequacy of a bank based on its standalone capital strength and risk profile;

   (ii) the consolidated ('Group') level capital adequacy ratio requirements, which measure the capital adequacy of a bank based on its capital strength and

risk profile after consolidating the assets and liabilities of its subsidiaries / associates / joint ventures, etc., except those engaged in insurance and any non-financial activities.

Accordingly, overseas operations of a bank through its branches shall be covered in both the above scenarios.

(2) The components, elements, and eligibility criteria of the regulatory capital instruments for a foreign bank operating in India under the Wholly Owned Subsidiary (WOS) model shall be applicable as they are to the other domestic banks as stipulated in these Directions. The WOS of a foreign bank operating in India shall meet the Basel III requirements on a continuous basis from the time of its entry / conversion. The WOS shall, however, maintain a minimum capital adequacy ratio, on a continuous basis for an initial period of three years from the commencement of its operations, at 10 per cent. In addition, the WOS shall maintain the Capital Conservation Buffer (CCB) and other buffers as applicable.

Capital adequacy at solo level

(3) While assessing the capital adequacy of a bank at solo level, all regulatory adjustments indicated in paragraph 28 are required to be made. In addition, investments in the capital instruments of the subsidiaries, which are consolidated in the consolidated financial statements of the group, shall be deducted from the corresponding capital instruments issued by the bank.

(4) In case of any shortfall in the regulatory capital requirements in the unconsolidated entity (e.g., insurance subsidiary), the shortfall shall be fully deducted from the Common Equity Tier 1 (CET1) capital.

Capital adequacy at group / consolidated level

(5) For capital adequacy at consolidated level, all banking and other financial subsidiaries except the subsidiaries engaged in insurance and any non-financial activities (both regulated and unregulated) shall be fully consolidated.

(6) The insurance and non-financial subsidiaries / joint ventures / associates of a bank shall not be consolidated for the purpose of capital adequacy. The equity and other regulatory capital investments in the insurance and non-financial subsidiaries shall be deducted from consolidated regulatory capital of the group.

The Equity and other regulatory capital investments in the unconsolidated insurance and non-financial entities of a bank (which also include joint ventures / associates of the parent bank) shall be treated in terms of paragraphs 28(8) and 74 respectively.

(7) All regulatory adjustments indicated in paragraph 28 shall be made to the consolidated capital of the banking group as indicated therein.

(8) Minority interest (i.e., non-controlling interest) and other capital issued out of consolidated subsidiaries as per paragraph 8(5) that is held by third parties can be recognised in the consolidated regulatory capital of the group subject to certain conditions as stipulated in paragraph 27.

(9) A bank shall ensure that majority owned financial entities that are not consolidated for capital purposes and for which the investment in equity and other instruments eligible for regulatory capital status is deducted, meet their respective regulatory capital requirements. In case of any shortfall in the regulatory capital requirements in the unconsolidated entity, the shortfall shall be fully deducted from the CET1 capital.

(10) The capital adequacy at group / consolidated level shall also include application of consolidated capital adequacy norms to the Non-Operative Financial Holding Company (NOFHC) after consolidating the relevant entities held by it in terms of paragraph 8(1)(ii) above.

(11) NBFCs promoted by the parent / group of a foreign bank, having presence in India in branch mode, which is a subsidiary of the foreign bank's parent / group, or where the parent / group is having management control shall be treated as part of that foreign bank's operations in India and brought under the ambit of consolidated supervision. This foreign bank shall consolidate the NBFCs with the bank's Indian operations on a line-by-line basis for capital adequacy by adopting the principles of AS 21 as applicable to consolidation of subsidiaries. Where a foreign bank is holding between 10 per cent and 50 per cent (both included) of the issued and paid-up equity of an NBFC, it shall be required to demonstrate that it does not have management control in case the NBFC is to be kept outside the ambit of consolidated prudential regulations.

Chapter III

Regulatory capital

A Composition of regulatory capital

A.1 General

9. The capital adequacy framework shall be based on three components or three Pillars. Pillar 1 is the Minimum Capital Requirement while Pillar 2 and Pillar 3 are the Supervisory Review and Evaluation Process (SREP) and Market Discipline, respectively. A bank shall maintain a minimum Pillar 1 Capital to Risk-weighted Assets Ratio (CRAR) of 9 per cent on an on-going basis (other than capital buffers) as prescribed under these Directions. The Reserve Bank will take into account the relevant risk factors and the internal capital adequacy assessments of each bank to ensure that the capital held by a bank is commensurate with its overall risk profile. This would include, among others, the effectiveness of the bank's risk management systems in identifying, assessing / measuring, monitoring, and managing various risks including interest rate risk in the banking book, liquidity risk, concentration risk, and residual risk. Accordingly, the Reserve Bank will consider prescribing a higher level of minimum capital ratio for each bank under the Pillar 2 framework on the basis of the bank's risk profile and risk management systems. Further, in terms of the Pillar 2 requirements, a bank is expected to operate at a level well above the minimum requirement. A bank shall compute Basel III capital ratios in the following manner:

$$\text{Common Equity Tier 1 capital ratio} = \frac{\text{Common Equity Tier 1 Capital}}{\text{Total Risk Weighted Assets (RWAs)}}$$

$$\text{Tier 1 capital ratio} = \frac{\text{Eligible Tier 1 Capital}}{\text{RWAs}}$$

$$\text{Total Capital (CRAR)} = \frac{\text{Eligible Total Capital}}{\text{RWAs}}$$

RWAs = Credit Risk RWAs + Market Risk RWAs + Operational Risk RWAs

A.2 Elements of regulatory capital

10. Total regulatory capital shall consist of the sum of the following categories:

    (i) Tier 1 Capital (going-concern capital):

        (a) Common Equity Tier 1 (CET1) Capital;

        (b) Additional Tier 1 (AT1) Capital;

    (ii) Tier 2 Capital (gone-concern capital).

A.3 Limits and minima

11. The limits and minimum capital requirements are as under:

(1) A bank shall maintain a Minimum Total Capital (MTC) of 9 per cent of the RWAs on an ongoing basis i.e., Capital to Risk-Weighted Assets Ratio (CRAR) shall be at least 9 per cent on an ongoing basis. This has been further divided into different components as described under following paragraphs;

(2) CET1 capital shall be at least 5.5 per cent of the RWAs on an ongoing basis;

(3) Tier 1 capital shall be at least 7 per cent of the RWAs on an ongoing basis. Thus, within the minimum Tier 1 capital, AT1 capital can be admitted maximum at 1.5 per cent of the RWAs;

(4) Total capital (Tier 1 capital + Tier 2 capital) shall be at least 9 per cent of the RWAs on an ongoing basis. Thus, within the minimum CRAR of 9 per cent, Tier 2 capital can be admitted maximum up to 2 per cent of the RWAs.

Explanation - If a bank has complied with the minimum CET1 capital ratio, prescribed in these Directions, excess CET1 capital can be admitted for compliance with the minimum Tier 1 capital ratio of 7 per cent of the RWAs. Further, if a bank has complied with the minimum CET1 and Tier 1 capital ratios, prescribed in these Directions, the excess CET1 and / or AT1 capital can be admitted for compliance with the minimum CRAR of 9 per cent of the RWAs;

(5) In addition to the minimum CET1 capital of 5.5 per cent of the RWAs, a bank shall also maintain a Capital Conservation Buffer (CCB) of 2.5 per cent of the RWAs in the form of CET1 capital. Details of operational aspects of CCB have been furnished in paragraphs 250 to 252;

(6) The capital requirements are summarised in Table 1 below:

Table 1: Minimum capital requirement applicable to a bank

Sr. No.	Regulatory Capital	As % to RWAs
(i)	Minimum CET1 Ratio	5.5
(ii)	Minimum Tier 1 Capital Ratio	7.0
(iii)	Maximum AT1 capital (within minimum Tier 1 capital ratio of 7 per cent) [(ii) – (i)]	1.5
(iv)	Minimum Total Capital Ratio (MTC)	9.0
(v)	Maximum Tier 2 Capital (within minimum Total Capital Ratio of 9 per cent) [(iv) – (ii)]	2.0
(vi)	Capital Conservation Buffer (comprised of CET1 capital)	2.5
(vii)	Minimum CET1 Ratio plus CCB [(i) + (vi)]	8.0
(viii)	Minimum Total Capital Ratio plus CCB [(iv) + (vi)]	11.5

B Common Equity Tier 1 (CET1) capital

B.1 CET1 capital - Indian banks

12. CET1 capital shall comprise the following:

(i) Common shares (paid-up equity capital) issued by a bank that meet the criteria for classification as common shares for regulatory purposes as given in paragraph 13;

(ii) Stock surplus (share premium) resulting from the issue of common shares;

(iii) Statutory reserves;

(iv) Capital reserves representing surplus arising out of sale proceeds of assets;

(v) AFS - Reserve

Note –

(1) AFS – Reserve shall be as per the Reserve Bank of India (Commercial Banks – Classification, Valuation and Operation of Investment Portfolio) Directions, 2025; and

(2) Any negative balance in the AFS - Reserve shall be deducted from CET1 capital;

(vi) Revaluation Reserves arising out of change in the carrying amount of a bank's property consequent upon its revaluation may be reckoned as CET1

capital at a discount of 55 per cent, subject to meeting the following conditions:

(a) the bank is able to sell the property readily at its own will and there is no legal impediment in selling the property; and

(b) the revaluation reserves are shown under 'Schedule 2: Reserves and Surplus' in the Balance Sheet of the bank;

(c) revaluations are realistic, in accordance with applicable Accounting Standards;

(d) valuations are obtained, from two independent valuers, at least once in every three years; where the value of the property has been substantially impaired by any event, these are to be immediately revalued and appropriately factored into capital adequacy computations;

(e) the external auditors of the bank have not expressed a qualified opinion on the revaluation of the property; and

(f) the instructions on valuation of properties and other specific requirements as mentioned in the Reserve Bank of India (Commercial Banks – Credit Risk Management) Directions, 2025 are strictly adhered to.

Revaluation reserves which do not qualify as CET1 capital shall also not qualify as Tier 2 capital. A bank may choose to reckon revaluation reserves in CET1 capital or Tier 2 capital at its discretion, subject to fulfilment of all the conditions specified above;

(vii) A bank may, at its discretion, reckon Foreign Currency Translation Reserve (FCTR) arising due to translation of financial statements of its foreign operations in terms of applicable Accounting Standards as CET1 capital at a discount of 25 per cent subject to meeting the following conditions:

(a) The FCTR is shown under 'Schedule 2: Reserves and Surplus' in the Balance Sheet of the bank;

(b) The external auditors of the bank have not expressed a qualified opinion on the FCTR;

(viii) Other disclosed free reserves, if any;

(ix) Balance in Profit and Loss Account at the end of the previous financial year;

(x) A bank may reckon the profits in current financial year for CRAR calculation on a quarterly basis provided the incremental provisions made for Non-Performing Assets (NPAs) at the end of any of the four quarters of the previous financial year have not deviated more than 25 per cent from the average of the four quarters. The amount which can be reckoned shall be arrived at by using the following formula:

$EP_t = \{NP_t – 0.25*D*t\}$

where:

EP_t = Eligible profit up to the quarter 't' of the current financial year; t varies from 1 to 4;

NP_t = Net profit up to the quarter 't';

D = average annual dividend paid during last three financial years.

The cumulative net loss up to the quarter end shall be deducted while calculating CET1 capital for the relevant quarter;

(xi) While calculating capital adequacy at the consolidated level, common shares issued by consolidated subsidiaries of a bank and held by third parties (i.e., minority interest) which meet the criteria for inclusion in CET1 capital [refer to paragraph 27(2)]; and

(xii) Less: Regulatory adjustments / deductions applied in the calculation of CET1 capital [i.e., to be deducted from the sum of items (i) to (xi)].

B.2 Criteria for classification as common shares (paid-up equity capital) for regulatory capital purposes – Indian bank

13. Common shares, which are included in CET1 capital, shall meet all the following criteria:

(i) All common shares shall ideally be the voting shares. However, in rare cases, where a bank needs to issue non-voting common shares as part of CET1 capital, it shall be identical to voting common shares of the issuing bank in all respects except the absence of voting rights. Limit on voting

rights shall be applicable based on the provisions of respective statutes governing individual bank {i.e., Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970 / 1980, in case of nationalized banks; State Bank of India Act, 1955, in case of State Bank of India; Banking Regulation Act, 1949, in case of private sector banks, etc;

(ii) Represents the most subordinated claim in liquidation of the bank;

(iii) Entitled to a claim on the residual assets which is proportional to its share of paid-up capital, after all senior claims have been repaid in liquidation (i.e., has an unlimited and variable claim, not a fixed or capped claim);

(iv) Principal is perpetual and never repaid outside of liquidation (except discretionary repurchases / buy backs or other means of effectively reducing capital in a discretionary manner that is allowable under relevant law as well as guidelines, if any, issued by the Reserve Bank in the matter);

(v) The bank does nothing to create an expectation at issuance that the instrument shall be bought back, redeemed, or cancelled nor do the statutory or contractual terms provide any feature which might give rise to such an expectation;

(vi) Distributions are paid out of distributable items. The level of distributions is not in any way tied or linked to the amount paid-up at issuance and is not subject to a contractual cap (except to the extent that a bank is unable to pay distributions that exceed the level of distributable items). As regards ‘distributable items’, dividend on common shares shall be paid out of current year’s profit only;

(vii) There are no circumstances under which the distributions are obligatory. Non-payment therefore shall not be an event of default;

(viii) Distributions are paid only after all legal and contractual obligations have been met and payments on more senior capital instruments have been made. This means that there are no preferential distributions, including in respect of other elements classified as the highest quality issued capital;

(ix) It is the paid-up capital that takes the first and proportionately greatest share of any losses as they occur. Within the highest quality capital, each

instrument absorbs losses on a going concern basis proportionately and *pari passu* with all the others. In cases where capital instruments have a permanent write-down feature, this criterion is still deemed to be met by common shares;

(x) The paid-up amount is classified as equity capital (i.e., not recognised as a liability) for determining balance sheet insolvency;

(xi) The paid-up amount is classified as equity under the relevant Accounting Standards;

(xii) It is directly issued and paid-up and the bank cannot directly or indirectly have funded the purchase of the instrument. A bank shall not grant advances against its own shares as this would be construed as indirect funding of its own capital. A bank shall also not extend loans against its own shares;

(xiii) The paid-up amount is neither secured nor covered by a guarantee of the issuer or related entity nor subject to any other arrangement that legally or economically enhances the seniority of the claim.

Explanation - A related entity can include a parent company, a sister company, a subsidiary, or any other affiliate. A holding company is a related entity irrespective of whether it forms part of the consolidated banking group;

(xiv) Paid-up capital is only issued with the approval of the owners of the issuing bank, either given directly by the owners or, if permitted by applicable law, given by the Board of Directors or by other persons duly authorised by the owners;

(xv) Paid-up capital is clearly and separately disclosed in the bank's Balance Sheet.

B.3 CET1 capital - Foreign bank's branches

14. CET1 capital of a foreign bank operating in India in branch mode shall comprise the following:

(i) Interest-free funds from Head Office kept in a separate account in Indian books specifically for the purpose of meeting the capital adequacy norms;

(ii) Remittable surplus retained in Indian books which is not repatriable so long as the bank functions in India.

Provided that, a bank shall not include cash / unencumbered approved securities, the source of which is interest-free funds from Head Office and remittable surplus retained in Indian books (reserves), held with the Reserve Bank under 11(2)(b)(i) of the BR Act,1949, reckoned as Credit Risk Mitigation (CRM) for offsetting the gross exposure of the foreign bank branches in India to the Head Office (including overseas branches) for the calculation of Large Exposures Framework limits, in CET1 capital. Accordingly, while assessing the CET1 capital of a bank, this amount shall form part of regulatory adjustments made to CET1 capital so that there is no double counting of the funds as both capital and CRM;

(iii) Statutory reserves kept in Indian books;

(iv) Interest-free funds remitted from abroad for the purpose of acquisition of property and held in a separate account in Indian books provided they are non-repatriable and have the ability to absorb losses regardless of their source;

(v) Capital reserve representing surplus arising out of sale of assets in India held in a separate account and which is not eligible for repatriation so long as the bank functions in India;

(vi) AFS - Reserve

Note –

(1) AFS – Reserve shall be as per the Reserve Bank of India (Commercial Banks – Classification, Valuation and Operation of Investment Portfolio) Directions, 2025; and

(2) Any negative balance in the AFS - Reserve shall be deducted from CET1 capital;

(vii) Revaluation reserves arising out of change in the carrying amount of a bank's property consequent upon its revaluation may be reckoned as CET1 capital at a discount of 55 per cent, subject to meeting the same set of conditions mentioned for Indian bank in paragraph 12(vi) above;

(viii) A bank may, at its discretion, reckon FCTR arising due to translation of financial statements of its foreign operations in terms of applicable Accounting Standards as CET1 capital at a discount of 25 per cent subject to meeting the same set of conditions mentioned for an Indian bank in paragraph 12(vii) above; and

(ix) Less: Regulatory adjustments / deductions applied in the calculation of CET1 capital [i.e., to be deducted from the sum of items (i) to (viii)].

Note-

(a) The instruments to be included in CET1 capital of foreign bank operating in branch mode shall meet the criteria outlined in paragraph 15;

(b) A foreign bank shall furnish to the Reserve Bank, an undertaking to the effect that the bank shall not remit abroad the ‘Capital Reserve’ and ‘remittable surplus retained in India’ as long as it functions in India to be eligible for including this item under CET1 capital;

(c) These funds shall be retained in a separate account titled as 'Amount Retained in India for Meeting CRAR Requirements' under 'Capital Funds';

(d) An auditor's certificate to the effect that these funds represent surplus remittable to Head Office once tax assessments are completed or tax appeals are decided and do not include funds in the nature of provisions towards tax or for any other contingency shall also be furnished to the Reserve Bank;

(e) The net credit balance, if any, in the inter-office account with Head Office / overseas branches shall not be reckoned as capital funds. However, the debit balance in the Head Office account shall have to be set-off against capital subject to the following provisions:

(i) If net overseas placements with Head Office / other overseas branches / other group entities (placement minus borrowings, excluding Head Office borrowings for Tier 1 and 2 capital purposes) exceed 10 per cent of the bank's minimum CRAR

requirement, the amount in excess of this limit shall be deducted from Tier 1 capital;

(ii) For the purpose of the above prudential cap, the net overseas placement shall be the higher of the overseas placements as on date and the average daily outstanding over year to date;

(iii) The overall cap on such placements / investments shall continue to be guided by the present regulatory and statutory restrictions i.e., net open position limit and the gap limits approved by the Reserve Bank, and Section 25 of the BR Act, 1949. All such transactions shall also be in conformity with other Foreign Exchange Management Act, 1999 (FEMA) guidelines.

B.4 Criteria for classification as Common Equity Tier 1 (CET1) capital for regulatory purposes for a foreign bank operating in India in branch mode

15. Instruments, to be included as CET1 for regulatory purposes, shall meet following criteria:

(i) Represents the most subordinated claim in liquidation of the Indian operations of the bank;

(ii) Entitled to a claim on the residual assets which is proportional to its share of paid-up capital, after all senior claims have been repaid in liquidation (i.e., has an unlimited and variable claim, not a fixed or capped claim);

(iii) Principal is perpetual and never repaid outside of liquidation (except with the approval of the Reserve Bank);

(iv) Distributions to the Head Office of the bank are paid out of distributable items. The level of distributions is not in any way tied or linked to the amount paid-up at issuance and is not subject to a contractual cap (except to the extent that a bank is unable to pay distributions that exceed the level of distributable items). As regards ‘Distributable Items’, it is clarified that the dividend on common shares / equity shall be paid out of current year’s profit only;

(v) Distributions to the Head Office of the bank are paid only after all legal and contractual obligations have been met and payments on more senior capital

instruments have been made. This means that there are no preferential distributions, including in respect of other elements classified as the highest quality issued capital;

(vi) This capital takes the first and proportionately greatest share of any losses as they occur. In cases where capital instruments have a permanent write-down feature, this criterion is still deemed to be met by common shares; and

(vii) It is clearly and separately disclosed in the bank's Balance Sheet.

C Additional Tier 1 (AT1) capital

C.1 AT1 capital - Indian banks

16. AT1 capital shall comprise the following:

(i) Perpetual Non-Cumulative Preference Shares (PNCPS), which comply with the regulatory requirements as specified in paragraph 19 and paragraph 26;

(ii) Stock surplus (share premium) resulting from the issue of instruments included in AT1 capital;

(iii) Debt capital instruments eligible for inclusion in AT1 capital, which comply with the regulatory requirements as specified in paragraph 20 and paragraph 26;

(iv) Any other type of instrument generally notified by the Reserve Bank from time to time for inclusion in AT1 capital;

(v) While calculating capital adequacy at the consolidated level, AT1 instruments issued by consolidated subsidiaries of the bank and held by third parties which meet the criteria for inclusion in AT1 capital [refer to paragraph 27(3)]; and

(vi) Less: Regulatory adjustments / deductions applied in the calculation of AT1 capital [i.e., to be deducted from the sum of items (i) to (v)].

C.2 Criteria for classification as AT1 capital for regulatory purposes

17. Criteria for inclusion of PNCPS and PDIs in AT1 capital are furnished in paragraph 19 and paragraph 20 respectively. Paragraph 26 contains criteria for

loss absorption through conversion / write-down / write-off of AT1 instrument on breach of the pre-specified trigger and of all non-common equity regulatory capital instruments at the Point of Non-Viability. A bank's AT1 capital instruments shall meet all these criteria for them to be considered as regulatory capital.

C.3 AT1 capital - Foreign bank's branches

18. AT1 capital of a foreign bank operating in India in branch mode shall comprise the following:

    (i) Head Office borrowings in foreign currency by a foreign bank operating in India for inclusion in AT1 capital which comply with the regulatory requirements as specified in paragraphs 20 and 26;

    (ii) Any other item specifically allowed by the Reserve Bank from time to time for inclusion in AT1 capital; and

    (iii) Less: Regulatory adjustments / deductions applied in the calculation of AT1 capital [i.e., to be deducted from the sum of items (i) and (ii)].

C.4 Criteria for inclusion of Perpetual Non-Cumulative Preference Shares (PNCPS) in AT1 capital – Indian banks

19. The PNCPS shall be issued by an Indian bank, subject to extant legal provisions, only in Indian rupees and shall meet the following terms and conditions to qualify for inclusion in AT1 capital for capital adequacy purposes:

(1) Paid-up status

The instruments shall be issued by the bank (i.e., not by any 'Special Purpose Vehicle (SPV)' etc. set up by the bank for this purpose) and fully paid-up;

(2) Amount

The amount of PNCPS to be raised shall be decided by the Board of Directors of a bank;

(3) Limits

While complying with minimum Tier 1 of 7 per cent of the RWAs, a bank shall not admit, PNCPS together with Perpetual Debt Instrument (PDI) in AT1 capital, more than 1.5 per cent of the RWAs. However, once this minimum total Tier 1 capital has been complied with, any additional PNCPS and PDI issued by the

bank can be included in total Tier 1 capital reported. Excess PNCPS and PDI can be reckoned to comply with Tier 2 capital if the latter is less than 2 per cent of RWAs i.e., while complying with minimum total capital (CRAR) of 9 per cent of the RWAs;

(4) Maturity period

The PNCPS shall be perpetual i.e., there is no maturity date and there are no step-ups or other incentives to redeem;

(5) Rate of dividend

The rate of dividend payable to the investors shall be either a fixed rate or a floating rate referenced to a market determined rupee interest benchmark rate;

(6) Optionality

PNCPS shall not be issued with a 'put option'. However, a bank may issue the instruments with a call option at a particular date subject to following conditions:

(i) The call option on the instrument is permissible after the instrument has run for at least five years;

(ii) To exercise a call option a bank shall receive prior approval of the Reserve Bank [Department of Regulation (DoR)];

(iii) A bank shall not do anything which creates an expectation that the call will be exercised. For example, to preclude such expectation of the instrument being called, the dividend / coupon reset date need not be co-terminus with the call date. A bank may, at its discretion, consider having an appropriate gap between dividend / coupon reset date and call date.

Explanation - If a bank were to call a capital instrument and replace it with an instrument that is more costly (e.g., has a higher credit spread) this might create an expectation that the bank will exercise calls on its other capital instruments. Therefore, a bank may not be permitted to call an instrument if the bank intends to replace it with an instrument issued at a higher credit spread. This is applicable in cases of all AT1 and Tier 2 instruments;

(iv) A bank shall not exercise a call unless:

(a) It replaces the called instrument with capital of the same or better quality and the replacement of this capital is done at conditions which are sustainable for the income capacity of the bank. Replacement issues can be concurrent with but not after the instrument is called; or

(b) The bank demonstrates that its capital position is well above the minimum capital requirements after the call option is exercised.

Explanation - Here, minimum capital requirements refer to CET1 ratio of 8 per cent of RWAs (including CCB of 2.5 per cent of RWAs) and total capital of 11.5 per cent of RWAs plus any additional capital requirement identified under Pillar 2;

(v) The use of tax event and regulatory event calls may be permitted. However, exercise of the calls on account of these events is subject to the requirements set out in points (ii) to (iv) above. The Reserve Bank may permit the bank to exercise the call only if it is convinced that the bank was not in a position to anticipate these events at the time of issuance of PNCPS.

Explanation - To illustrate, if there is a change in tax treatment which makes the capital instrument with tax deductible coupons into an instrument with non-tax-deductible coupons, then the bank will have the option (not obligation) to repurchase the instrument. In such a situation, a bank may be allowed to replace the capital instrument with another capital instrument that perhaps does have tax deductible coupons. Similarly, if there is a downgrade of the instrument in regulatory classification (e.g., if it is decided by the Reserve Bank to exclude an instrument from regulatory capital) the bank may have the option to call the instrument and replace it with an instrument with a better regulatory classification, or a lower coupon with the same regulatory classification with prior approval of the Reserve Bank. However, a bank shall not create an expectation / signal an early redemption / maturity of the regulatory capital instrument;

(7) Repurchase / buy-back / redemption

(i) Principal of the instruments may be repaid (e.g., through repurchase or redemption) only with prior approval of the Reserve Bank and a bank shall

not assume or create market expectations that supervisory approval shall be given (this repurchase / buy-back / redemption of the principal is in a situation other than in the event of exercise of call option by the bank. One of the major differences is that in the case of the former, the option to offer the instrument for repayment on announcement of the decision to repurchase / buy-back / redeem the instrument, will lie with the investors whereas, in case of the latter, it lies with the bank);

(ii) A bank may repurchase / buy-back / redeem the instruments only if:

(a) It replaces such instrument with capital of the same or better quality and the replacement of this capital is done at conditions which are sustainable for the income capacity of the bank; or

(b) The bank demonstrates that its capital position is well above the minimum capital requirements after the repurchase / buy-back / redemption;

(8) Dividend discretion

(i) A bank shall have full discretion at all times to cancel distributions / payments.

Note – Due to full discretion at all times to cancel distributions / payments, 'dividend pushers' are prohibited. An instrument with a dividend pusher obliges the issuing bank to make a dividend / coupon payment on the instrument if it has made a payment on another (typically more junior) capital instrument or share. This obligation is inconsistent with the requirement for full discretion at all times. Furthermore, the term 'cancel distributions / payments' means extinguish these payments. It does not permit features that require the bank to make distributions / payments in kind;

(ii) Cancellation of discretionary payments shall not be an event of default;

(iii) A bank shall have full access to cancelled payments to meet obligations as they fall due;

(iv) Cancellation of distributions / payments shall not impose restrictions on the bank except in relation to distributions to common stakeholders; and

(v) Dividends shall be paid out of distributable items only. As regards 'distributable items', it is clarified that the dividend on PNCPS shall be paid out of current year's profit only.

Note - As provided in Reserve Bank of India (Commercial Banks – Classification, Valuation and Operation of Investment Portfolio) Directions, 2025, the unrealised gains transferred to AFS-Reserve shall not be available for any distribution such as dividend on AT1 capital instruments. Further, the Directions *ibid* provide that a bank shall not pay dividends out of net unrealised gains recognised in the Profit and Loss Account arising on fair valuation of Level 3 financial instruments on its Balance Sheet;

(vi) The dividend shall not be cumulative, i.e., dividend missed in a year shall not be paid in future years, even if adequate profit is available and the level of CRAR conforms to the regulatory minimum. When dividend is paid at a rate lesser than the prescribed rate, the unpaid amount shall not be paid in future years, even if adequate profit is available and the level of CRAR conforms to the regulatory minimum;

(vii) The instrument shall not have a credit sensitive coupon feature, i.e., a dividend that is reset periodically based in whole or in part on the bank's credit standing. For this purpose, any reference rate including a broad index which is sensitive to changes to the bank's own creditworthiness and / or to changes in the credit worthiness of the wider banking sector shall be treated as a credit sensitive reference rate. A bank desirous of offering floating reference rate shall take prior approval of the Reserve Bank (DoR) as regard permissibility of such reference rates;

(viii) A bank may have dividend stopper arrangement that stops dividend payments on common shares in the event the holders of AT1 instruments are not paid dividend / coupon. However, dividend stoppers shall not impede the full discretion that a bank shall have at all times to cancel distributions / payments on the AT1 instrument, nor shall they act in a way that could hinder the re-capitalisation of the bank. For example, it shall not be permitted for a stopper on an AT1 instrument to:

(a) attempt to stop payment on another instrument where the payments on this other instrument were not also fully discretionary;

(b) prevent distributions to shareholders for a period that extends beyond the point in time that dividends / coupons on the AT1 instrument are resumed; and

(c) impede the normal operation of the bank or any restructuring activity (including acquisitions / disposals).

A stopper may act to prohibit actions that are equivalent to the payment of a dividend, such as the bank undertaking discretionary share buybacks, if otherwise permitted;

(9) Treatment in insolvency

The instrument shall not contribute to liabilities exceeding assets if such a balance sheet test forms part of a requirement to prove insolvency under any law or otherwise;

(10) Loss absorption features

PNCPS shall have principal loss absorption through either (i) conversion to common shares at an objective pre-specified trigger point, or (ii) a write-down mechanism which allocates losses to the instrument at a pre-specified trigger point. The write-down will have the following effects:

(i) Reduce the claim of the instrument in liquidation;

(ii) Reduce the amount re-paid when a call is exercised; and

(iii) Partially or fully reduce dividend payments on the instrument.

Various criteria for loss absorption through conversion / write-down / write-off on breach of pre-specified trigger and at the Point of Non-Viability are furnished in paragraph 26;

(11) Prohibition on purchase / funding of PNCPS

Neither the bank nor a related party over which the bank exercises control or significant influence (as defined under relevant Accounting Standards) shall purchase PNCPS, nor shall the bank directly or indirectly fund the purchase of

the instrument. A bank shall also not grant advances against the security of PNCPS issued by it;

(12) Re-capitalisation

The instrument shall not have any features that hinder re-capitalisation, such as provisions which require the issuer to compensate investors if a new instrument is issued at a lower price during a specified time frame;

(13) Reporting of non-payment of dividends and non-exercise of call option

All instances of non-payment of dividends and non-exercise of call option shall be notified by the issuing bank to the Chief General Manager-in-Charges of DoR, Central Office, and Department of Supervision (DoS), Central Office of the Reserve Bank;

(14) Seniority of claim

The claims of the investors in instruments shall be:

(i) Superior to the claims of investors in equity shares;

(ii) Subordinated to the claims of PDIs, all Tier 2 regulatory capital instruments, depositors, and general creditors of the bank; and

(iii) neither secured nor covered by a guarantee of the issuer or related entity or other arrangement that legally or economically enhances the seniority of the claim vis-à-vis bank creditors;

(15) Investment in instruments raised in Indian rupees by foreign entities / Non-Resident Indians (NRIs)

(i) Investment by Foreign Institutional Investor (FIIs) and NRIs shall be within an overall limit of 49 per cent and 24 per cent of the issue respectively, subject to the investment by each FII not exceeding 10 per cent of the issue, and investment by each NRI not exceeding 5 per cent of the issue. Investment by FIIs in these instruments shall be outside the External Commercial Borrowing (ECB) limit for rupee-denominated corporate debt, as fixed by Government of India from time to time. The overall non-resident holding of preference shares and equity shares in public sector banks shall be subject to the applicable statutory / regulatory limits;

(ii) A bank shall comply with the terms and conditions, if any, stipulated by the SEBI / other regulatory authorities in regard to issue of the instruments;

(16) Compliance with reserve requirements

(i) The funds collected by various branches of the bank or other banks for the issue and held pending finalisation of allotment of the AT1 preference shares shall have to be taken into account for the purpose of calculating reserve requirements;

(ii) However, the total amount raised by the bank by issue of PNCPS shall not be reckoned as liability for calculation of net demand and time liabilities for the purpose of reserve requirements and, as such, shall not attract Cash Reserve Ratio (CRR) / Statutory Liquidity Ratio (SLR) requirements;

(17) Reporting of issuances

(i) A bank issuing PNCPS shall submit a report to the Chief General Manager-in-Charge, DoR, Central Office, Reserve Bank of India giving details of the instrument as per the format prescribed in Annex II duly certified by the compliance officer of the bank, soon after the issue is completed;

(ii) The issue-wise details of amount raised as PNCPS qualifying for AT1 capital by the bank from FIIs / NRIs are required to be reported within 30 days of the issue to the Chief General Manager, Reserve Bank of India, Foreign Exchange Department, Central Office, Mumbai - 400 001 in the proforma given at Annex I. The details of the secondary market sales / purchases by FIIs and the NRIs in these instruments on the stock exchange shall be reported by the custodians and designated banks, respectively, to the Reserve Bank as per the applicable FEMA guidelines, as amended from time to time;

(18) Investment in AT1 capital instruments (PNCPS) issued by other banks / financial institutions

(i) A bank's investment in PNCPS issued by other banks and financial institutions shall be reckoned along with the investment in other instruments eligible for capital status while computing compliance with the overall ceiling

of 10 per cent of investing bank's total regulatory capital as prescribed under paragraph 28(8)(i)(a) and also subject to cross holding limits;

(ii) A bank's investments in PNCPS issued by other banks / financial institutions shall attract risk weight as provided in paragraphs 42 to 45 and 188, whichever applicable for capital adequacy purposes;

(iii) A bank's investments in the PNCPS of other banks shall be treated as exposure to capital market and be reckoned for the purpose of compliance with the prudential ceiling for capital market exposure as fixed by the Reserve Bank;

(19) Classification in the Balance Sheet

PNCPS shall be classified as capital and shown under 'Schedule I - Capital' of the Balance Sheet;

(20) PNCPS to retail investors

A bank issuing PNCPS to retail investors, subject to approval of its Board, shall adhere to the following conditions:

(i) The requirement for specific sign-off, as quoted below, from the investors for having understood the features and risks of the instrument shall be incorporated in the common application form of the proposed issue:

"By making this application, I / We acknowledge that I / We have understood the terms and conditions of the Issue of [insert the name of the instruments being issued] of [Name of The Bank] as disclosed in the Draft Shelf Prospectus, Shelf Prospectus and Tranche Document";

(ii) All the publicity material, application form, and other communication with the investor shall clearly state in bold letters (with font size 14) how PNCPS is different from common shares. In addition, the loss absorbency features of the instrument shall be clearly explained and the investor’s sign-off for having understood these features and other terms and conditions of the instrument shall be obtained.

C.5 Criteria for inclusion of Perpetual Debt Instrument (PDI) in AT1 capital

20. The PDI that may be issued as bonds or debentures by an Indian bank shall meet the following terms and conditions to qualify for inclusion in AT1 capital for capital adequacy purposes:

Terms of issue of instruments denominated in Indian rupees

(1) Paid-in status

The instruments shall be issued by the bank (i.e., not by any 'Special Purpose Vehicle' (SPV) etc., set up by the bank for this purpose) and fully paid in;

(2) Amount

The amount of PDI to be raised shall be decided by the Board of Directors of a bank;

(3) Limits

While complying with minimum Tier 1 of 7 per cent of RWAs, a bank cannot admit, PDI together with PNCPS in AT1 capital, more than 1.5 per cent of RWAs. However, once this minimum total Tier 1 capital has been complied with, any additional PNCPS and PDI issued by the bank can be included in total Tier 1 capital reported. Excess PNCPS and PDI can be reckoned to comply with Tier 2 capital if the latter is less than 2 per cent of RWAs, i.e., while complying with minimum total capital of 9 per cent of RWAs;

(4) Maturity period

The PDIs shall be perpetual i.e., there shall be no maturity date and there shall be no step-ups or other incentives to redeem;

(5) Rate of interest

The interest payable to the investors shall be either at a fixed rate or at a floating rate referenced to a market determined rupee interest benchmark rate;

(6) Optionality

PDIs shall not have any 'put option'. However, a bank may issue the instruments with a 'call option' at a particular date subject to following conditions:

(i) The call option on the instrument is permissible after the instrument has run for at least five years;

(ii) To exercise a call option, a bank shall receive prior approval of the Reserve Bank (DoR);

(iii) A bank shall not do anything which creates an expectation that the call will be exercised. For example, to preclude such expectation of the instrument being called, the dividend / coupon reset date need not be co-terminus with the call date. A bank may, at its discretion, consider having an appropriate gap between dividend / coupon reset date and call date; and

(iv) A bank shall not exercise a call unless:

(a) It replaces the called instrument with capital of the same or better quality and the replacement of this capital is done at conditions which are sustainable for the income capacity of the bank. Replacement issues can be concurrent with but not after the instrument is called; or

(b) The bank demonstrates that its capital position is well above the minimum capital requirements after the call option is exercised.

Explanation - minimum capital requirements refer to CET1 ratio of 8 per cent of RWAs (including CCB of 2.5 per cent of RWAs) and total capital of 11.5 per cent of RWAs plus additional capital requirements identified under Pillar 2;

(v) The use of tax event and regulatory event calls may be permitted. However, exercise of the calls on account of these events is subject to the requirements set out in points (ii) to (iv) above. The Reserve Bank may permit the bank to exercise the call only if it is convinced that the bank was not in a position to anticipate these events at the time of issuance of PDIs.

Explanation - To illustrate, if there is a change in tax treatment which makes the capital instrument with tax deductible coupons into an instrument with non-tax-deductible coupons, the bank will have the option (not obligation) to repurchase the instrument. In such a situation, a bank may be allowed to replace the capital instrument with another capital instrument that perhaps does have tax deductible coupons. Similarly, if there is a downgrade of the

instrument in regulatory classification (e.g., if it is decided by the Reserve Bank to exclude an instrument from regulatory capital), the bank will have the option to call the instrument and replace it with an instrument with a better regulatory classification, or a lower coupon with the same regulatory classification with prior approval of the Reserve Bank. However, a bank shall not create an expectation / signal an early redemption / maturity of the regulatory capital instrument;

(7) Repurchase / buy-back / redemption

(i) Principal of the instruments may be repaid (e.g., through repurchase or redemption) only with the prior approval of the Reserve Bank and a bank shall not assume or create market expectations that supervisory approval shall be given (this repurchase / buy-back / redemption of the principal is in a situation other than in the event of exercise of call option by the bank. One of the major differences is that in the case of the former, the option to offer the instrument for repayment on announcement of the decision to repurchase / buy-back / redeem the instrument, would lie with the investors whereas, in case of the latter, it lies with the bank);

(ii) A bank may repurchase / buy-back / redeem only if:

(a) It replaces such instrument with capital of the same or better quality and the replacement of this capital is done at conditions which are sustainable for the income capacity of the bank; or

(b) The bank demonstrates that its capital position is well above the minimum capital requirements after the repurchase / buy-back / redemption;

(8) Coupon discretion

(i) The bank shall have full discretion at all times to cancel distributions / payments.

Explanation - Due to full discretion at all times to cancel distributions / payments, 'dividend pushers' are prohibited. An instrument with a dividend pusher obliges the issuing bank to make a dividend / coupon payment on the instrument if it has made a payment on another (typically more junior)

capital instrument or share. This obligation is inconsistent with the requirement for full discretion at all times. Furthermore, the term 'cancel distributions / payments' means extinguish these payments. It does not permit features that require the bank to make distributions / payments in kind;

(ii) Cancellation of discretionary payments shall not be an event of default;

(iii) A bank shall have full access to cancelled payments to meet obligations as they fall due;

(iv) Cancellation of distributions / payments shall not impose restrictions on the bank except in relation to distributions to common stakeholders;

(v) Coupons shall be paid out of 'distributable items'. In this context, coupon shall be paid out of current year profits. However, if current year profits are not sufficient, coupon may be paid subject to availability of:

(a) Profits brought forward from previous years; and / or

(b) Reserves representing appropriation of net profits, including statutory reserves, and excluding share premium, revaluation reserve, FCTR, investment reserve, unrealised gains transferred to AFS – Reserve, and reserves created on amalgamation.

Note - As provided in Reserve Bank of India (Commercial Banks – Classification, Valuation and Operation of Investment Portfolio) Directions, 2025, the unrealised gains transferred to AFS - Reserve shall not be available for any distribution such as coupon on AT1 capital instruments;

(c) The accumulated losses and deferred revenue expenditure, if any, shall be netted off from (a) and (b) to arrive at the available balances for payment of coupon;

(d) If the aggregate of (i) profits in the current year; (ii) profits brought forward from the previous years; and (iii) permissible reserves as at (b) above, excluding statutory reserves, net of accumulated losses and deferred revenue expenditure are less than the amount of coupon, only then will the bank make appropriation from the statutory

reserves. In such cases, a bank is required to report to the Reserve Bank within twenty-one days from the date of such appropriation in compliance with Section 17(2) of the BR Act 1949;

(e) Prior approval of the Reserve Bank for appropriation of reserves as above, in terms of Reserve Bank of India (Commercial Banks – Financial Statements: Presentation and Disclosures) Directions, 2025, is not required in this regard;

(f) However, payment of coupons on PDIs from the reserves shall be subject to the issuing bank meeting minimum regulatory requirements for CET1, Tier 1, and total capital ratios including the additional capital requirements for Domestic Systemically Important Banks at all times and subject to the restrictions under the capital buffer frameworks (i.e., CCB and Countercyclical Capital Buffer (CCCB) in terms of paragraphs 250 to 252 and 258 to 261);

(vi) To meet the eligibility criteria for PDI, a bank shall ensure and indicate in its offer documents that it has full discretion at all times to cancel distributions / payments;

(vii) the interest shall not be cumulative;

(viii) The instrument shall not have a credit sensitive coupon feature, i.e., a dividend that is reset periodically based in whole or in part on the bank's credit standing. For this purpose, any reference rate including a broad index which is sensitive to changes to the bank's own creditworthiness and / or to changes in the credit worthiness of the wider banking sector shall be treated as a credit sensitive reference rate. A bank desirous of offering floating reference rate shall take prior approval of the Reserve Bank (DoR) as regard permissibility of such reference rates;

(ix) A bank may have dividend stopper arrangement that stops dividend payments on common shares in the event the holders of AT1 instruments are not paid dividend / coupon. However, dividend stoppers shall not impede the full discretion that bank shall have at all times to cancel distributions / payments on the AT1 instrument, nor shall they act in a way

that could hinder the re-capitalisation of the bank. For example, it shall not be permitted for a stopper on an AT1 instrument to:

(a) attempt to stop payment on another instrument where the payments on this other instrument were also not fully discretionary;

(b) prevent distributions to shareholders for a period that extends beyond the point in time that dividends / coupons on the AT1 instrument are resumed; and

(c) impede the normal operation of the bank or any restructuring activity (including acquisitions / disposals).

A stopper may act to prohibit actions that are equivalent to the payment of a dividend, such as the bank undertaking discretionary share buybacks, if otherwise permitted;

(9) Treatment in insolvency

The instrument shall not contribute to liabilities exceeding assets if such a balance sheet test forms part of a requirement to prove insolvency under any law or otherwise;

(10) Loss absorption features

PDIs shall be classified as liabilities for accounting purposes (not for the purpose of insolvency as indicated in paragraph 20(9) above). In such cases, these instruments shall have principal loss absorption through either (i) conversion to common shares at an objective pre-specified trigger point or (ii) a write-down mechanism which allocates losses to the instrument at a pre-specified trigger point. The write-down will have the following effects:

(i) Reduce the claim of the instrument in liquidation;

(ii) Reduce the amount re-paid when a call is exercised; and

(iii) Partially or fully reduce coupon payments on the instrument.

Various criteria for loss absorption through conversion / write-down / write-off on breach of pre-specified trigger and at the point of non-viability are furnished in paragraph 26;

(11) Prohibition on purchase / funding of instruments

Neither the bank nor a related party over which the bank exercises control or significant influence (as defined under relevant Accounting Standards) shall purchase the instrument, nor shall the bank directly or indirectly fund the purchase of the instrument. A bank shall also not grant advances against the security of the debt instruments issued by it;

(12) Recapitalisation

The instrument shall not have any features that hinder re-capitalisation such as provisions which require the issuer to compensate investors, if a new instrument is issued at a lower price during a specified time frame;

(13) Reporting of non-payment of coupons and non-exercise of call option

All instances of non-payment of coupon and non-exercise of call option shall be notified by the issuing bank to the Chief General Managers-in-Charges of DoR and DoS of the Reserve Bank, Mumbai;

(14) Seniority of claim

The claims of the investors in instruments shall be:

(i) superior to the claims of investors in equity shares and PNCPS;

(ii) subordinated to the claims of depositors, general creditors, and subordinated debt of the bank; and

(iii) neither secured nor covered by a guarantee of the issuer or related entity or other arrangement that legally or economically enhances the seniority of the claim vis-à-vis bank creditors;

(15) Investment in instruments raised in Indian rupees by foreign entities / NRIs

(i) Investment by FIIs in instruments raised in Indian rupees shall be outside the ECB limit for rupee denominated corporate debt, as fixed by the Government of India from time to time, for investment by FIIs in corporate debt instruments. Investment in these instruments by FIIs and NRIs shall be within an overall limit of 49 per cent and 24 per cent of the issue, respectively, subject to the investment by each FII and each NRI not exceeding 10 per cent and 5 per cent of the issue respectively;

(ii) A bank shall comply with the terms and conditions, if any, stipulated by the SEBI / other regulatory authorities in regard to issue of the instruments;

(16) Terms of issue of instruments denominated in foreign currency / rupee denominated bonds overseas

A bank may augment its capital funds through the issue of PDIs in foreign currency / rupee denominated bonds overseas without seeking the prior approval of the Reserve Bank, subject to compliance with the FEMA guidelines as applicable and the requirements mentioned below:

(i) These instruments shall comply with all terms and conditions as applicable to the instruments issued in Indian rupees;

(ii) PDIs issued in foreign currency / rupee denominated bonds overseas shall be eligible for inclusion in AT1 capital up to a maximum amount of 1.5 per cent of RWAs as per the latest available financial statements (audited or subjected to limited review);

(iii) The above prescribed limit shall not be applicable to a foreign bank's branches. The limit for PDIs eligible for inclusion in AT1 capital, denominated in foreign currency / rupee denominated bonds, as prescribed above, shall also be applicable to a foreign bank operating under the WOS model;

(iv) Instruments issued in foreign currency shall be outside the existing limit for foreign currency borrowings by Authorised Dealers, stipulated in terms of Master Direction - Risk Management and Inter-Bank Dealings dated July 5, 2016;

(v) A bank, other than a foreign bank branch, raising PDIs overseas shall obtain and keep on record a legal opinion from an advocate / attorney practicing in the relevant legal jurisdiction, that the terms and conditions of issue of the instrument are in conformity with these Directions, can be enforced in the concerned legal jurisdiction and the applicable laws there do not stand in the way of enforcement of those conditions;

(17) Compliance with reserve requirements

The total amount raised by a bank through debt instruments shall not be reckoned as liability for calculation of net demand and time liabilities for the purpose of reserve requirements and, as such, will not attract CRR / SLR requirements;

(18) Reporting of issuances

A bank issuing PDIs shall submit a report to the Chief General Manager-in-Charge, DoR, Reserve Bank of India, Mumbai giving details of the instrument as per the format prescribed in Annex II duly certified by the compliance officer of the bank, soon after the issue is completed;

(19) Investment in AT1 debt capital instruments (PDIs) issued by other banks / financial institutions

(i) A bank's investment in debt instruments issued by other banks and financial institutions shall be reckoned along with the investment in other instruments eligible for capital status while computing compliance with the overall ceiling of 10 per cent of investing bank's total regulatory capital as prescribed under paragraph 28(8)(i)(a) of these Directions and also subject to cross holding limits;

(ii) A bank’s investments in debt instruments issued by other banks shall attract risk weight for capital adequacy purposes, as prescribed in paragraphs 42 to 45 and 188 of these Directions, whichever applicable;

(20) Classification in the balance sheet

The amount raised by way of issue of debt capital instrument shall be classified under ‘Schedule 4 – Borrowings’ in the Balance Sheet;

(21) Raising of instruments for inclusion as AT1 capital by foreign banks in India

A foreign bank in India may raise Head Office (HO) borrowings in foreign currency for inclusion as AT1 capital subject to the same terms and conditions as mentioned in items (1) to (18) above for Indian banks. In addition, the following terms and conditions would also be applicable:

(i) Maturity period: The amount of AT1 capital raised as HO borrowings shall be retained in India on a perpetual basis;

(ii) Rate of interest: Rate of interest on AT1 capital raised as HO borrowings shall not exceed the on-going market rate. Interest shall be paid at half yearly rests;

(iii) Withholding tax: Interest payments to the HO shall be subject to applicable withholding tax;

(iv) Documentation: The foreign bank raising AT1 capital as HO borrowings shall obtain a letter from its HO agreeing to give the loan for supplementing the capital base for the Indian operations of the foreign bank. The loan documentation shall confirm that the loan given by HO shall be eligible for the same level of seniority of claim as the investors in debt capital instruments issued by Indian banks. The loan agreement shall be governed by and construed in accordance with the Indian law;

(v) Disclosure: The total eligible amount of HO borrowings shall be disclosed in the Balance Sheet under the head 'AT1 capital raised in the form of Head Office borrowings in foreign currency';

(vi) Hedging: The total eligible amount of HO borrowing shall remain fully swapped in Indian rupees with the bank at all times;

(vii) Reporting and certification: Details regarding the total amount of AT1 capital raised as HO borrowings, along with a certification to the effect that the borrowing is in accordance with these guidelines, shall be advised to the Chief General Managers-in-Charge of the DoR, Department of External Investments and Operations and Financial Markets Regulation Department, Reserve Bank of India, Mumbai;

(22) PDI to retail investors

A bank issuing PDIs to retail investors, subject to approval of its Board, shall adhere to the following conditions:

(i) For floating rate instruments, a bank shall not use its fixed deposit rate as benchmark;

(ii) The requirement for specific sign-off, as quoted below, from the investors for having understood the features and risks of the instrument shall be incorporated in the common application form of the proposed debt issue:

"By making this application, I / we acknowledge that I / we have understood the terms and conditions of the Issue of [insert the name of the instruments being issued] of [Name of The Bank] as disclosed in the Draft Shelf Prospectus, Shelf Prospectus and Tranche Document ";

(iii) All the publicity material, application form and other communication with the investor shall clearly state in bold letters (with font size 14) how a PDI is different from fixed deposit particularly that it is not covered by deposit insurance. In addition, the loss absorbency features of the instrument shall be clearly explained and the investor's sign-off for having understood these features and other terms and conditions of the instrument shall be obtained.

D Tier 2 capital

D.1 Tier 2 capital - Indian banks

21. Tier 2 capital shall comprise the following:

(i) General provisions and loss reserves

(a) Provisions or loan-loss reserves held against future, presently unidentified losses, which are freely available to meet losses which subsequently materialise, shall qualify for inclusion within Tier 2 capital. Accordingly, general provisions on standard assets, floating provisions, incremental provisions in respect of unhedged foreign currency exposures, provisions held for country exposures, excess provisions which arise on account of sale of NPAs and 'countercyclical provisioning buffer' shall qualify for inclusion in Tier 2 capital. However, these items together shall be admitted as Tier 2 capital up to a maximum of 1.25 per cent of the total credit RWAs under the standardised approach.

Note - A bank may either net off floating provisions from Gross NPAs to arrive at Net NPA or reckon it as part of its Tier 2 capital. For provision on unhedged foreign currency exposures, a bank may refer Reserve Bank of India (Commercial Banks – Credit Risk Management) Directions, 2025;

(b) Investment Fluctuation Reserve (IFR);

(c) Provisions ascribed to identified deterioration of particular assets or loan liabilities, whether individual or grouped shall be excluded. Accordingly, for instance, specific provisions on NPAs, both at individual account or at portfolio level, provisions in lieu of diminution in the fair value of assets in the case of restructured advances, provisions against depreciation in the value of investments shall be excluded;

(ii) Debt capital instruments issued by the bank which comply with the regulatory requirements as specified in paragraph 24 and paragraph 26;

(iii) Preference Share capital instruments [Perpetual Cumulative Preference Shares (PCPS) / Redeemable Non-Cumulative Preference Shares (RNCPS) / Redeemable Cumulative Preference Shares (RCPS)] issued by the bank, which comply with the regulatory requirements as specified in paragraph 25 and paragraph 26;

(iv) Stock surplus (share premium) resulting from the issue of instruments included in Tier 2 capital;

(v) While calculating capital adequacy at the consolidated level, Tier 2 capital instruments issued by consolidated subsidiaries of the bank and held by third parties which meet the criteria for inclusion in Tier 2 capital [refer to paragraph 27(4)];

(vi) Any other type of instrument generally notified by the Reserve Bank from time to time for inclusion in Tier 2 capital; and

(vii) Less: Regulatory adjustments / deductions applied in the calculation of Tier 2 capital [i.e., to be deducted from the sum of items (i) to (vi)].

D.2 Criteria for classification as Tier 2 capital for regulatory purposes

22. Criteria for inclusion of Debt Capital Instruments and PCPS / RNCPS / RCPS in Tier 2 capital are furnished in paragraph 24 and paragraph 25 respectively. Paragraph 26 contains criteria for loss absorption through conversion / write-off of all non-common equity regulatory capital instruments at the Point of Non-

Viability. A bank's Tier 2 capital instruments shall meet all these criteria for them to be considered as regulatory capital.

D.3 Tier 2 capital - Foreign bank's branches

23. Tier 2 capital of a foreign bank operating in India in branch mode shall comprise the following:

    (i) General provisions and loss reserves (as detailed in paragraph 21(i) above);

    (ii) HO borrowings in foreign currency received as part of Tier 2 debt capital provided it meets the criteria given in the paragraph 24 and 26; and

    (iii) Less: Regulatory adjustments / deductions applied in the calculation of Tier 2 capital [i.e., to be deducted from the sum of items (i) and (ii)].

D.4 Criteria for inclusion of debt capital instruments as Tier 2 capital

24. The Tier 2 debt capital instruments that may be issued as bonds / debentures by an Indian bank shall meet the following terms and conditions to qualify for inclusion as Tier 2 capital for capital adequacy purposes:

    Note - The criteria relating to loss absorbency through conversion / write-down / write-off at the Point of Non-Viability are furnished in paragraph 26.

    Terms of issue of instruments denominated in Indian rupees

(1) Paid-in status

The instruments shall be issued by the bank (i.e., not by any 'SPV' etc. set up by the bank for this purpose) and fully paid in;

(2) Amount

The amount of these debt instruments to be raised shall be decided by the Board of Directors of a bank;

(3) Maturity period

The debt instruments shall have a minimum maturity of five years and there are no step-ups or other incentives to redeem;

(4) Discount

The debt instruments shall be subjected to a progressive discount for capital adequacy purposes. As they approach maturity, these instruments shall be subjected to progressive discount as indicated in the Table 2 below for being eligible for inclusion in Tier 2 capital:

Table 2: Progressive discount on debt instrument to be included in Tier 2

Remaining maturity of instruments	Rate of discount (%)
Less than one year	100
One year and more but less than two years	80
Two years and more but less than three years	60
Three years and more but less than four years	40
Four years and more but less than five years	20

(5) Rate of interest

(i) The interest payable to the investors shall be either at a fixed rate or at a floating rate referenced to a market determined rupee interest benchmark rate;

(ii) The instrument shall not have a credit sensitive coupon feature, i.e., a coupon that is reset periodically based in whole or in part on the bank's credit standing. A bank desirous of offering floating reference rate shall take prior approval of the Reserve Bank (DoR) as regard permissibility of such reference rates;

(6) Optionality

The debt instruments shall not have any 'put option'. However, it may be callable at the initiative of the issuer only after a minimum of five years subject to following conditions:

(i) To exercise a call option a bank shall receive prior approval of the Reserve Bank (DoR); and

(ii) A bank shall not do anything which creates an expectation that the call will be exercised. For example, to preclude such expectation of the instrument being called, the dividend / coupon reset date need not be co-terminus with the call date. A bank may, at its discretion, consider having an appropriate gap between dividend / coupon reset date and call date; and

(iii) A bank shall not exercise a call unless:

(a) It replaces the called instrument with capital of the same or better quality and the replacement of this capital is done at conditions which are sustainable for the income capacity of the bank. Replacement issues can be concurrent with but not after the instrument is called; or

(b) The bank demonstrates that its capital position is well above the minimum capital requirements after the call option is exercised.

Explanation - Minimum refers to CET1 ratio of 8 per cent of RWAs (including CCB of 2.5 per cent of RWAs) and total capital ratio of 11.5 per cent of RWAs including any additional capital requirement identified under Pillar 2;

(iv) The use of tax event and regulatory event calls may be permitted. However, exercise of calls on account of these events is subject to the requirements set out in points (i) to (iii) of criterion (6) above. The Reserve Bank may permit the bank to exercise the call only if it is convinced that the bank was not in a position to anticipate these events at the time of issuance of these instruments as explained in case of AT1 instruments;

(7) Treatment in bankruptcy / liquidation

The investor shall have no rights to accelerate the repayment of future scheduled payments (coupon or principal) except in bankruptcy and liquidation;

(8) Prohibition on purchase / funding of instruments

Neither the bank nor a related party over which the bank exercises control or significant influence (as defined under relevant Accounting Standards) shall purchase the instrument, nor shall the bank directly or indirectly fund the purchase of the instrument. A bank shall also not grant advances against the security of the debt instruments issued by it;

(9) Reporting of non-payment of coupons and non-exercise of call option

All instances of non-payment of coupon and non-exercise of call option shall be notified by an issuing bank to the Chief General Managers-in-Charge of DoR and DoS of the Reserve Bank of India, Mumbai;

(10) Seniority of claim

The claims of the investors in instruments shall be:

(i) senior to the claims of investors in instruments eligible for inclusion in Tier 1 capital;

(ii) subordinate to the claims of all depositors and general creditors of the bank; and

(iii) neither secured nor covered by a guarantee of the issuer or related entity or other arrangement that legally or economically enhances the seniority of the claim vis-à-vis bank creditors;

(11) Investment in instruments raised in Indian rupees by foreign entities / NRIs

(i) Investment by FIIs in Tier 2 instruments raised in Indian rupees shall be outside the limit for investment in corporate debt instruments, as fixed by the Government of India from time to time. However, investment by FIIs in these instruments shall be subjected to a separate ceiling of USD 500 million. In addition, NRIs shall also be eligible to invest in these instruments as per existing policy;

(ii) A bank shall comply with the terms and conditions, if any, stipulated by the SEBI / other regulatory authorities in regard to issue of the instruments;

(12) Issuance of rupee denominated bonds overseas by an Indian bank

A bank is permitted to raise funds through issuance of rupee denominated bonds overseas for qualification as debt capital instruments eligible for inclusion as Tier 2 capital, subject to compliance with all the terms and conditions applicable to instruments issued in Indian rupees and FEMA guidelines, as applicable;

(13) Terms of issue of Tier 2 debt capital instruments in foreign currency

A bank may issue Tier 2 debt Instruments in foreign currency without seeking the prior approval of the Reserve Bank, subject to compliance with the requirements mentioned below:

(i) Tier 2 Instruments issued in foreign currency shall comply with all terms and conditions applicable to instruments issued in Indian rupees;

(ii) The total outstanding amount of Tier 2 Instruments in foreign currency shall not exceed 25 per cent of the unimpaired Tier 1 capital. This eligible amount shall be computed with reference to the amount of Tier 1 capital as on March 31 of the previous financial year, after deduction of goodwill and other intangible assets but before the deduction of investments, as per paragraph 28(8) of these Directions.

Note - This limit shall not be applicable to a foreign bank operating in India in branch mode;

(iii) This shall be in addition to the existing limit for foreign currency borrowings by Authorised Dealers stipulated in terms of Master Direction - Risk Management and Inter-Bank Dealings dated July 5, 2016;

(iv) A bank, other than foreign bank branch, raising Tier 2 bonds overseas (including both foreign currency and rupee denominated bonds raised overseas) shall obtain and keep on record a legal opinion from an advocate / attorney practicing in the relevant legal jurisdiction, that the terms and conditions of issue of the instrument are in conformity with these Directions can be enforced in the concerned legal jurisdiction and the applicable laws there do not stand in the way of enforcement of those conditions;

(14) Compliance with reserve requirements

(i) The funds collected by various branches of the bank or other banks for the issue and held pending finalisation of allotment of the Tier 2 capital instruments shall have to be taken into account for the purpose of calculating reserve requirements;

(ii) The total amount raised by a bank through Tier 2 instruments shall be reckoned as liability for the calculation of net demand and time liabilities for the purpose of reserve requirements and, as such, will attract CRR / SLR requirements;

(15) Reporting of issuances

A bank issuing debt instruments shall submit a report to the Chief General Manager-in-Charge, DoR, Reserve Bank of India, Mumbai giving details of the

instrument as per the format prescribed in Annex II duly certified by the compliance officer of the bank, soon after the issue is completed;

(16) Investment in Tier 2 debt capital instruments issued by other banks / financial institutions

(i) A bank's investment in Tier 2 debt instruments issued by other banks and financial institutions shall be reckoned along with the investment in other instruments eligible for capital status while computing compliance with the overall ceiling of 10 per cent of investing bank's total regulatory capital as prescribed under paragraph 28(8)(i)(a) and also subject to cross holding limits;

(ii) Bank's investments in Tier 2 instruments issued by other banks / financial institutions shall attract risk weight as per paragraphs 42 to 45 and 188, whichever applicable for capital adequacy purposes;

(17) Classification in the Balance Sheet

The amount raised by way of issue of Tier 2 debt capital instrument shall be classified under 'Schedule 4 – Borrowings' in the Balance Sheet;

(18) Debt capital instruments to retail investors

A bank issuing subordinated debt to retail investors, subject to approval of its Board shall adhere to the following conditions:

(i) For floating rate instruments, the bank shall not use its fixed deposit rate as benchmark;

(ii) The requirement for specific sign-off, as quoted below, from the investors for having understood the features and risks of the instrument shall be incorporated in the common application form of the proposed debt issue:

"By making this application, I / We acknowledge that I / We have understood the terms and conditions of the Issue of [insert the name of the instruments being issued] of [Name of The Bank] as disclosed in the Draft Shelf Prospectus, Shelf Prospectus and Tranche Document ";

(iii) All the publicity material, application form and other communication with the investor should clearly state in bold letters (with font size 14) how a subordinated bond is different from fixed deposit particularly that it is not covered by deposit insurance. In addition, the loss absorbency features of the instrument shall be clearly explained and the investor's sign-off for having understood these features and other terms and conditions of the instrument should be obtained;

(19) Raising of instruments for inclusion as Tier 2 capital by a foreign bank in India

A foreign bank in India may raise HO borrowings in foreign currency for inclusion as Tier 2 capital subject to the same terms and conditions as mentioned in paragraph 24(1) to 24(18) above for an Indian bank. In addition, the following terms and conditions shall also be applicable:

(i) Maturity period: If the amount of Tier 2 debt capital raised as HO borrowings is in tranches, each tranche shall be retained in India for a minimum period of five years;

(ii) Rate of interest: Rate of interest on Tier 2 capital raised as HO borrowings shall not exceed the on-going market rate. Interest shall be paid at half yearly rests;

(iii) Withholding tax: Interest payments to the HO will be subject to applicable withholding tax;

(iv) Documentation: The foreign bank raising Tier 2 debt capital as HO borrowings shall obtain a letter from its HO agreeing to give the loan for supplementing the capital base for the Indian operations of the foreign bank. The loan documentation shall confirm that the loan given by HO shall be eligible for the same level of seniority of claim as the investors in debt capital instruments issued by an Indian bank. The loan agreement will be governed by and construed in accordance with the Indian law;

(v) Disclosure: The total eligible amount of HO borrowings shall be disclosed in the Balance Sheet under the head 'Tier 2 debt capital raised in the form of Head Office borrowings in foreign currency';

(vi) Hedging: The total eligible amount of HO borrowing shall remain fully swapped in Indian rupees with the bank at all times;

(vii) Reporting and certification: Details regarding the total amount of Tier 2 debt capital raised as HO borrowings, along with a certification to the effect that the borrowing is in accordance with these guidelines, shall be advised to the Chief General Managers-in-Charge of the DoR, Department of External Investments, and Operations and Financial Markets Regulation Department, Reserve Bank of India, Mumbai;

(viii) Features: The HO borrowings shall be fully paid-up, i.e., the entire borrowing or each tranche of the borrowing shall be available in full to the branch in India. It shall be unsecured, subordinated to the claims of other creditors of the foreign bank in India, free of restrictive clauses and shall not be redeemable at the instance of the HO;

(ix) Rate of discount: The HO borrowings shall be subjected to progressive discount as they approach maturity at the rates indicated in Table 3 below:

Table 3: Rate of discount on HO borrowings under Tier 2 by a foreign bank in India

Remaining maturity of borrowing	Rate of discount (%)
More than 5 years	Not Applicable (the entire amount can be included as subordinated debt in Tier 2 capital)
More than 4 years and less than 5 years	20
More than 3 years and less than 4 years	40
More than 2 years and less than 3 years	60
More than 1 year and less than 2 years	80
Less than 1 year	100 (No amount can be treated as subordinate debt for Tier 2 capital)

(20) Requirements

The total amount of HO borrowings shall be reckoned as liability for the calculation of net demand and time liabilities for the purpose of reserve requirements and, as such, will attract CRR / SLR requirements;

(21) Hedging

The entire amount of HO borrowing shall remain fully swapped with a bank at all times. The swap should be in Indian rupees;

(22) Reporting and certification

Such borrowings done in compliance with the guidelines set out above shall not require prior approval of the Reserve Bank. However, information regarding the total amount of borrowing raised from HO under this paragraph, along with a certification to the effect that the borrowing is as per the guidelines, shall be advised to the Chief General Managers-in-Charge of the DoR, Department of External Investments and Operations and Financial Markets Regulation Department, Reserve Bank of India, Mumbai.

D.5 Criteria for Inclusion of Perpetual Cumulative Preference Shares (PCPS) / Redeemable Non-Cumulative Preference Shares (RNCPS) / Redeemable Cumulative Preference Shares (RCPS) as part of Tier 2 capital

25. Terms of issue of PCPS / RNCPS / RCPS to be included as part of Tier 2 capital shall be as under:

Note - The criteria relating to loss absorbency through conversion / write-down / write-off at the Point of Non-Viability are furnished in paragraph 26.

(1) Paid-in status

The instruments shall be issued by the bank (i.e., not by any 'SPV' etc. set up by the bank for this purpose) and fully paid in;

(2) Amount

The amount to be raised shall be decided by the Board of Directors of a bank;

(3) Maturity period

These instruments could be either perpetual (PCPS) or dated (RNCPS and RCPS) instruments with a fixed maturity of minimum five years and there shall be no step-ups or other incentives to redeem. The perpetual instruments shall be cumulative. The dated instruments shall be cumulative or non-cumulative;

(4) Amortisation

The redeemable preference shares (both cumulative and non-cumulative) shall be subjected to a progressive discount for capital adequacy purposes over the last five years of their tenor, as they approach maturity as indicated in the Table 4 below for being eligible for inclusion in Tier 2 capital;

Table 4: Rate of discount on redeemable preference shares eligible for inclusion in Tier 2 capital

Remaining Maturity of Instruments	Rate of Discount (%)
Less than one year	100
One year and more but less than two years	80
Two years and more but less than three years	60
Three years and more but less than four years	40
Four years and more but less than five years	20

(5) Coupon

The coupon payable to the investors shall either be at a fixed rate or at a floating rate referenced to a market determined rupee interest benchmark rate. A bank desirous of offering floating reference rate shall take prior approval of the Reserve Bank (DoR) as regard permissibility of such reference rates;

(6) Optionality

These instruments shall not be issued with a 'put option'. However, a bank may issue the instruments with a call option at a particular date subject to following conditions:

(i) The call option on the instrument is permissible after the instrument has run for at least five years;

(ii) To exercise a call option a bank shall receive prior approval of the Reserve Bank (DoR);

(iii) A bank shall not do anything which creates an expectation that the call will be exercised. For example, to preclude such expectation of the instrument being called, the dividend / coupon reset date need not be co-terminus with the call date. A bank may, at its discretion, consider having an appropriate gap between dividend / coupon reset date and call date;

(iv) A bank shall not exercise a call unless:

(a) It replaces the called instrument with capital of the same or better quality and the replacement of this capital is done at conditions which are sustainable for the income capacity of the bank. Replacement issues can be concurrent with but not after the instrument is called; or

(b) The bank demonstrates that its capital position is well above the minimum capital requirements after the call option is exercised.

Explanation - Minimum refers to CET1 ratio of 8 per cent of RWAs (including CCB of 2.5 per cent of RWAs) and total capital ratio of 11.5 per cent of RWAs plus any additional capital requirement identified under Pillar 2;

(v) The use of tax event and regulatory event calls may be permitted. However, exercise of the calls on account of these events shall be subject to the requirements set out in points (ii) to (iv) of above. The Reserve Bank may permit the bank to exercise the call only if it is convinced that the bank was not in a position to anticipate these events at the time of issuance of these instruments as explained in case of AT1 instruments;

(7) Treatment in bankruptcy / liquidation

The investor shall have no rights to accelerate the repayment of future scheduled payments (coupon or principal) except in bankruptcy and liquidation;

(8) Prohibition on purchase / funding

Neither the bank nor a related party over which the bank exercises control or significant influence (as defined under relevant Accounting Standards) shall purchase these instruments, nor shall the bank directly or indirectly fund the purchase of the instrument. A bank shall also not grant advances against the security of these instruments issued by them;

(9) Reporting of non-payment of coupon and non-exercise of call option

All instances of non-payment of coupon and non-exercise of call option shall be notified by the issuing bank to the Chief General Managers-in-Charge of DoR and DoS of the Reserve Bank of India, Mumbai;

(10) Seniority of claim

The claims of the investors in instruments shall be:

(i) senior to the claims of investors in instruments eligible for inclusion in Tier 1 capital;

(ii) subordinate to the claims of all depositors and general creditors of the bank; and

(iii) neither secured nor covered by a guarantee of the issuer or related entity or other arrangement that legally or economically enhances the seniority of the claim vis-à-vis bank creditors;

(11) Investment in instruments raised in Indian rupees by foreign entities / NRIs

(i) Investment by FIIs and NRIs shall be within an overall limit of 49 per cent and 24 per cent of the issue respectively, subject to the investment by each FII and each NRI not exceeding 10 per cent and 5 per cent of the issue respectively. Investment by FIIs in these instruments shall be outside the ECB limit for rupee denominated corporate debt as fixed by Government of India from time to time. However, investment by FIIs in these instruments shall be subject to separate ceiling of USD 500 million. The overall non-resident holding of preference shares and equity shares in public sector banks shall be subject to the statutory / regulatory limit;

(ii) A bank shall comply with the terms and conditions, if any, stipulated by the SEBI / other regulatory authorities in regard to issue of the instruments;

(12) Compliance with reserve requirements

(i) The funds collected by various branches of the bank or other banks for the issue and held pending finalization of allotment of these instruments shall be taken into account for the purpose of calculating reserve requirements;

(ii) The total amount raised by a bank through the issue of these instruments shall be reckoned as liability for the calculation of net demand and time liabilities for the purpose of reserve requirements and, as such, will attract CRR / SLR requirements;

(13) Reporting of issuances

A bank issuing these instruments shall submit a report to the Chief General Manager-in-charge, DoR, Reserve Bank of India, Mumbai giving details of the instrument as per the format prescribed in Annex II duly certified by the compliance officer of the bank, soon after the issue is completed;

(14) Investment in these Instruments Issued by other banks / financial institutions

(i) A bank's investment in these instruments issued by other banks and financial institutions shall be reckoned along with the investment in other instruments eligible for capital status while computing compliance with the overall ceiling of 10 per cent of an investing bank's total regulatory capital as prescribed under paragraph 28(8)(i)(a) of these Directions and also subject to cross holding limits;

(ii) Bank's investments in these instruments issued by other banks / financial institutions shall attract risk weight for capital adequacy purposes as provided vide paragraphs 42 to 45 and 188, whichever applicable;

(15) Classification in the Balance Sheet

These instruments shall be classified as 'Borrowings' under Schedule 4 of the Balance Sheet under item No. I (i.e., Borrowings);

(16) PCPS / RNCPS / RCPS to retail investors

A bank issuing PCPS / RNCPS / RCPS to retail investors, subject to approval of its Board, shall adhere to the following conditions:

(i) The requirement for specific sign-off, as quoted below, from the investors for having understood the features and risks of the instrument shall be incorporated in the common application form of the proposed issue:

"By making this application, I / We acknowledge that I / We have understood the terms and conditions of the Issue of [insert the name of the instruments being issued] of [Name of The Bank] as disclosed in the Draft Shelf Prospectus, Shelf Prospectus and Tranche Document ";

(ii) All the publicity material, application form and other communication with the investor should clearly state in bold letters (with font size 14) how a PCPS / RNCPS / RCPS is different from common shares / fixed deposit particularly that it is not covered by deposit insurance. In addition, the loss absorbency features of the instrument shall be clearly explained and the investor's sign-off for having understood these features and other terms and conditions of the instrument shall be obtained.

E Minimum requirements to ensure loss absorbency of Additional Tier 1 (AT1) instruments at pre-specified trigger and of all non-equity regulatory capital instruments at the Point of Non-Viability

26. For an instrument issued by a bank to be included in AT1 or in Tier 2 capital, in addition to criteria for individual types of non-equity regulatory capital instruments mentioned in paragraphs 19, 20, 24 and 25, it shall also meet or exceed minimum requirements set out in the following paragraphs:

Loss absorption of AT1 instruments at the pre-specified trigger

(1) Loss absorption features

(i) AT1 capital instruments shall have principal loss absorption at an objective pre-specified trigger point through either:

(a) conversion to common shares; or

(b) a write-down mechanism which allocates losses to the instrument. The write-down shall have the following effects:

(i) reduce the claim of the instrument in liquidation;

(ii) reduce the amount re-paid when a call is exercised; and

(iii) partially or fully reduce coupon / dividend payments on the instrument.

(ii) Accordingly, a bank shall issue AT1 instrument with either conversion (i.e., conversion to common shares) or write-down (temporary or permanent) mechanism.

Explanation - When a paid-up instrument is fully and permanently written down, it ceases to exist resulting in extinguishment of a liability of a bank (a non-common equity instrument) and creates CET1 capital. A temporary write-down is different from a conversion and a permanent write-down i.e., the original instrument may not be fully extinguished. Generally, the par value of the instrument is written-down (decrease) on the occurrence of the trigger event and which may be written-up (increase) back to its original value in future depending upon the conditions prescribed in the terms and conditions of the instrument. The amount shown on the Balance Sheet subsequent to temporary write-down may

depend on the precise features of the instrument and the prevailing Accounting Standards.

(2) Level of pre-specified trigger and amount of equity to be created by conversion / write-down

(i) The pre-specified trigger for loss absorption through conversion / write-down of AT1 instruments (PNCPS and PDI) shall be at least CET1 capital of 6.125 per cent of RWAs. The write-down of any CET1 capital shall not be required before a write-down of any AT1 capital instrument.

(ii) The conversion / write-down mechanism (temporary or permanent) which allocates losses to the AT1 instruments shall generate CET1 capital under applicable Accounting Standards. The instrument shall receive recognition in AT1 capital only up to the extent of minimum level of CET1 capital generated (i.e., net of contingent liability recognised under the applicable Accounting Standards, potential tax liabilities, etc., if any) by a full write-down / conversion of the instrument.

(iii) A bank shall obtain and keep on its records a certificate from the statutory auditors clearly stating that the conversion / write-down mechanism chosen by the bank for a particular AT1 issuance is able to generate CET1 capital under the prevailing Accounting Standards. Further, a bank shall also obtain and keep on its records an external legal opinion confirming that the conversion or write-down of AT1 capital instrument at the pre -specified trigger by the issuing bank is legally enforceable.

Note - Auditor's certificate shall be required not only at the time of issuance of the instruments, but also whenever there is a change in accounting norms / standards which may affect the ability of the loss absorbency mechanism of the instrument to create CET1 capital.

(iv) The aggregate amount to be written down / converted for all AT1 instruments on breaching the trigger level shall be at least the amount needed to immediately return the bank’s CET1 ratio to the trigger level or, if this is not possible, the full principal value of the instruments. Further, the issuer shall have full discretion to determine the amount of AT1 instruments to be converted / written-down subject to the amount of conversion / write-

down not exceeding the amount which would be required to bring the CET1 ratio to 8 per cent of RWAs (minimum CET1 of 5.5 per cent + CCB of 2.5 per cent).

(v) When a bank breaches the pre-specified trigger of loss absorbency of AT1 and the equity is replenished either through conversion or write-down, such replenished amount of equity will be excluded from the total equity of the bank for the purpose of determining the proportion of earnings to be paid out as dividend in terms of rules laid down for maintaining the CCB. However, once the bank has attained total CET1 ratio of 8 per cent without counting the replenished equity capital, that point onwards, the bank may include the replenished equity capital for all purposes. If the total CET1 ratio of the bank falls again below the 8 per cent, it shall include the replenished capital for the purpose of applying the CCB framework.

(vi) The conversion / write-down shall be allowed more than once in case a bank hits the pre-specified trigger level subsequent to the first conversion / write-down which was partial.

(vii) The conversion / write-down of AT1 instruments is primarily intended to replenish the equity in the event it is depleted by losses. Therefore, a bank shall not use conversion / write-down of AT1 instruments to support expansion of balance sheet by incurring further obligations / booking assets. Accordingly, a bank whose CET1 ratio slips below 8 per cent due to losses and is still above 6.125 per cent i.e., trigger point, shall seek to expand its balance sheet further only by raising fresh equity from its existing shareholders or market and the internal accruals. However, fresh exposures can be taken to the extent of amortisation of the existing ones. If any expansion in exposures, such as due to draw down of sanctioned borrowing limits, is inevitable, this shall be compensated within the shortest possible time by reducing other exposures. The bank shall maintain proper records to facilitate verification of these transactions by its internal auditors, statutory auditors, and inspecting officers of the Reserve Bank.

Note - For the purpose of determination of breach of trigger, the fresh equity, if any, raised after slippage of CET1 below 8 per cent shall not be

subtracted. In other words, if CET1 of the bank now is above the trigger level though it would have been below the trigger had it not raised the fresh equity which it did, the trigger shall not be treated as breached.

(3) Treatment of AT1 instruments in the event of winding-up, amalgamation, acquisition, re-constitution etc., of a bank

(i) If a bank goes into liquidation before the AT1 instruments have been written down / converted, these instruments shall absorb losses in accordance with the order of seniority indicated in the offer document and as per usual legal provisions governing priority of charges.

(ii) If a bank goes into liquidation after the AT1 instruments have been written down, the holders of these instruments shall have no claim on the proceeds of liquidation.

Amalgamation of a banking company: (Section 44 A of BR Act, 1949)

(iii) If a bank is amalgamated with any other bank before the AT1 instruments have been written down / converted, these instruments shall become part of the corresponding categories of regulatory capital of the new bank emerging after the merger.

(iv) If a bank is amalgamated with any other bank after the AT1 instruments have been written down temporarily, the amalgamated entity can write-up these instruments as per its discretion.

(v) If a bank is amalgamated with any other bank after the non-equity regulatory capital instruments have been written-down permanently, these cannot be written-up by the amalgamated entity.

Scheme of reconstitution or amalgamation of a banking company: (Section 45 of BR Act, 1949)

(vi) If the relevant authorities decide to reconstitute a bank or amalgamate a bank with any other bank under the Section 45 of the BR Act, 1949, such a bank shall be deemed as non-viable or approaching non-viability and both the pre-specified trigger and the trigger at the point of non-viability (as described in subsequent paragraph 26(6) to 26(10) below) for conversion / write-down of AT1 instruments shall be activated. Accordingly, the AT1

instruments shall be fully converted / written down permanently before amalgamation / reconstitution in accordance with these rules.

(4) Fixation of conversion price, capping of number of shares / voting rights

(i) A bank may issue AT1 instrument with conversion features either based on price fixed at the time of issuance or based on the market price prevailing at the time of conversion.

Explanation - Market price here does not mean the price prevailing on the date of conversion; a bank can use any pricing formula such as weighted average price of shares during a particular period before conversion.

(ii) There will be a possibility of the debt holders receiving a large number of shares in the event the share price is very low at the time of conversion. Thus, debt holders will end up holding the number of shares and attached voting rights exceeding the legally permissible limits. A bank shall, therefore, always keep sufficient headroom to accommodate the additional equity due to conversion without breaching any of the statutory / regulatory ceilings especially that for maximum private shareholdings and maximum voting rights per investors / group of related investors. To achieve this, a bank shall cap the number of shares and / or voting rights in accordance with relevant laws and regulations on ownership and governance of banks. A bank shall adequately incorporate these features in the terms and conditions of the instruments in the offer document. In exceptional circumstances, if the breach is inevitable, the bank shall immediately inform the Reserve Bank (DoR) about it. The investors shall be required to bring the shareholdings below the statutory / regulatory ceilings within the specific time frame as determined by the Reserve Bank.

(iii) In the case of an unlisted bank, the conversion price shall be determined based on the fair value of the bank's common shares to be estimated according to a mutually acceptable methodology, which shall be in conformity with the standard market practice for valuation of shares of unlisted companies.

(iv) To ensure the criteria that the issuing bank shall maintain at all times all prior authorisation necessary to immediately issue the relevant number of

shares specified in the instrument's terms and conditions should the trigger event occur, the capital clause of each bank shall have to be suitably modified to take care of conversion aspects.

(5) Order of conversion / write-down of various types of AT1 instruments

A bank shall clearly indicate in the offer document, the order of conversion / write-down of the instrument in question vis-à-vis other capital instruments which the bank has already issued or may issue in future, based on the advice of its legal counsels.

Minimum requirements to ensure loss absorbency of non-equity regulatory capital instruments at the Point of Non-Viability (PONV)

(6) Mode of loss absorption and trigger event

(i) The terms and conditions of all non-common equity Tier 1 and Tier 2 capital instruments issued by a bank in India shall have a provision that requires such instruments, at the option of the Reserve Bank, to either be written off or converted into common equity upon the occurrence of the trigger event, called the 'PONV Trigger'.

(ii) The PONV Trigger event is the earlier of:

(a) a decision that a conversion (i.e., full conversion to common shares) or write-off (fully and permanently), without which the firm would become non-viable, is necessary, as determined by the Reserve Bank; and

(b) the decision to make a public sector injection of capital, or equivalent support, without which the firm would have become non-viable, as determined by the relevant authority.

The write-off of any CET1 capital shall not be required before the write-off of any non-equity (AT1 and Tier 2) regulatory capital instrument.

(iii) Such a decision shall invariably imply that the write-off or issuance of any new shares as a result of conversion consequent upon the trigger event shall occur prior to any public sector injection of capital so that the capital provided by the public sector is not diluted. As such, the contractual terms and conditions of an instrument shall not provide for any residual claims on

the issuer which are senior to ordinary shares of the bank (or banking group entity where applicable), following a trigger event and when conversion or write-off is undertaken.

(iv) Any compensation paid to the instrument holders as a result of the write-off shall be paid immediately in the form of common shares.

Note - Compensation in the form of common shares shall be viewed as the simultaneous occurrence of (a) permanent write-off of the original instrument; and (b) creation of new common shares issued in lieu of non-equity capital instrument which is written-off, as compensation for its extinguishment. The precise mechanism may vary under the Accounting Standards. No compensation (i.e., zero common shares) is paid in case of full and permanent write-off.

(v) The issuing bank shall maintain at all times all prior authorisation necessary to immediately issue the relevant number of shares specified in the instrument's terms and conditions should the trigger event occur.

(vi) To ensure that these requirements are met, a bank shall obtain and keep on its records an external legal opinion confirming that the conversion or write-off feature of non-equity capital instruments (AT1 or Tier 2) by the Reserve Bank at the PONV is legally enforceable. Further, the legal opinion shall also confirm that there are no legal impediments to the conversion of the instrument into ordinary shares of the bank (or a banking group entity, where applicable) or write-off upon a trigger event. The Reserve Bank may also require the bank to submit additional information in order to ensure that such instruments are eligible for inclusion into regulatory capital.

(7) A non-viable bank

For these guidelines, a non-viable bank shall be a bank which, owing to its financial and other difficulties, may no longer remain a going concern on its own in the opinion of the Reserve Bank unless appropriate measures are taken to revive its operations and thus, enable it to continue as a going concern. The difficulties faced by a bank shall be such that these are likely to result in financial losses and raising the CET1 capital of the bank shall be considered as the most appropriate way to prevent the bank from turning non-viable. Such measures

shall include write-off / conversion of non-equity regulatory capital into common shares in combination with or without other measures as considered appropriate by the Reserve Bank.

Note - In rare situations, a bank may also become non-viable due to non-financial problems, such as conduct of affairs of the bank in a manner which is detrimental to the interest of depositors, serious corporate governance issues, etc. In such situations, raising capital is not considered a part of the solution and therefore, may not attract provisions of this framework.

(8) Restoring viability

A bank facing financial difficulties and approaching a PONV shall be deemed to achieve viability, if within a reasonable time, in the opinion of Reserve Bank, it will be able to come out of the present difficulties if appropriate measures are taken to revive it. The measures including augmentation of equity capital through write-off / conversion / public sector injection of funds are likely to:

(i) Restore depositors' / investors' confidence;

(ii) Improve rating / creditworthiness of the bank and thereby improve its borrowing capacity and liquidity and reduce cost of funds; and

(iii) Augment the resource base to fund balance sheet growth in the case of fresh injection of funds.

(9) Other requirements to be met by the non-common equity capital instruments to absorb losses at the PONV

(i) Instruments may be issued with either of the following feature:

(a) conversion; or

(b) permanent write-off.

(ii) The amount of non-equity capital to be converted / written-off shall be determined by the Reserve Bank.

(iii) When a bank breaches the PONV trigger and the equity is replenished either through conversion or write-off, such replenished amount of equity shall be excluded from the total equity of the bank for the purpose of determining the proportion of earnings to be paid out as dividend in terms

of rules laid down for maintaining CCB. However, once the bank has attained total CET1 ratio of 8 per cent without counting the replenished equity capital, that point onwards, the bank may include the replenished equity capital for all purposes.

Note - If the total CET1 ratio of the bank falls again below 8 per cent, it shall include the replenished capital for the purpose of applying the CCB framework.

(iv) The provisions regarding treatment of AT1 instruments in the event of winding-up, amalgamation, acquisition, re-constitution etc., of the bank as given in paragraph 26(3) shall also be applicable to all non-common equity capital instruments (AT1 and Tier 2 capital instruments) when these events take place after conversion / write-off at the PONV.

(v) The provisions regarding fixation of conversion price, capping of number of shares / voting rights applicable to AT1 instruments in terms of paragraph 26(4) shall also be applicable for conversion of all non-common equity capital instruments (AT1 and Tier 2 capital instruments) at the PONV.

(vi) The provisions regarding order of conversion / write-down of AT1 instruments as given in paragraph 26(5) shall also be applicable for conversion / write-off of all non-common equity capital instruments (AT1 and Tier 2 capital instruments) at the PONV.

(10) Criteria to Determine the PONV

(i) The above framework shall be invoked when a bank is adjudged by the Reserve Bank to be approaching the PONV, or has already reached the PONV, but in the views of the Reserve Bank:

(a) there is a possibility that a timely intervention in form of capital support, with or without other supporting interventions, is likely to rescue the bank; and

(b) if left unattended, the weaknesses would inflict financial losses on the bank and, thus, cause decline in its common equity level.

(ii) The purpose of write-off and / or conversion of non-equity regulatory capital elements will be to shore up the capital level of the bank. The Reserve Bank

shall follow a two-stage approach to determine the non-viability of a bank. The Stage 1 assessment shall consist of purely objective and quantifiable criteria to indicate that there is a prima facie case of a bank approaching non-viability and, therefore, a closer examination of the bank's financial situation is warranted. The Stage 2 assessment shall consist of supplementary subjective criteria which, in conjunction with the Stage 1 information, shall help in determining whether the bank is about to become non-viable. These criteria would be evaluated together and not in isolation.

(iii) Once the PONV is confirmed, the next step shall be to decide whether rescue of the bank would be through write-off / conversion alone or write-off / conversion in conjunction with a public sector injection of funds.

(iv) The trigger at PONV shall be evaluated both at consolidated and solo level and breach at either level will trigger conversion / write-off.

(v) As the capital adequacy is applicable both at solo and consolidated levels, the minority interests in respect of capital instruments issued by subsidiaries of a bank including overseas subsidiaries can be included in the consolidated capital of the banking group only if these instruments have pre-specified triggers (in case of AT1 capital instruments) / loss absorbency at the PONV (for all non-common equity capital instruments). In addition, where a bank wishes the instrument issued by its subsidiary to be included in the consolidated group's capital in addition to its solo capital, the terms and conditions of that instrument shall specify an additional trigger event. This additional trigger event is the earlier of:

(a) a decision that a conversion or write-off, without which the bank or the subsidiary would become non-viable, is necessary, as determined by the Reserve Bank; and

(b) the decision to make a public sector injection of capital, or equivalent support, without which the bank or the subsidiary would have become non-viable, as determined by the Reserve Bank. Such a decision shall invariably imply that the write-off or issuance of any new shares as a result of conversion consequent upon the trigger event shall occur

prior to any public sector injection of capital so that the capital provided by the public sector is not diluted.

Note - The cost to the parent of its investment in each subsidiary and the parent's portion of equity of each subsidiary, at the date on which investment in each subsidiary is made, is eliminated as per AS-21. So, in case of wholly owned subsidiaries, it would not matter whether or not it has same characteristics as the bank's capital. However, in the case of less than wholly owned subsidiaries (or in the case of non-equity regulatory capital of the wholly owned subsidiaries, if issued to the third parties), minority interests constitute additional capital for the banking group over and above what is counted at solo level; therefore, it should be admitted only when it (and consequently the entire capital in that category) has the same characteristics as the bank's capital.

(vi) In such cases, the subsidiary shall obtain its regulator's approval / no-objection for allowing the capital instrument to be converted / written-off at the additional trigger point referred to in paragraph 26(10)(v).

(vii) Any common shares paid as compensation to the holders of the instrument shall be common shares of either the issuing subsidiary or the parent bank (including any successor in resolution).

F Recognition of minority interest (i.e., non-controlling interest) and other capital issued out of consolidated subsidiaries that is held by third parties

27. Recognition of minority interest and other capital issued out of consolidated subsidiaries that is held by third parties shall be as under:

(1) The minority interest shall be recognised only in cases where there is considerable explicit or implicit assurance that the minority interest which is supporting the risks of the subsidiary shall be available to absorb the losses at the consolidated level. Accordingly, the portion of minority interest which supports risks in a subsidiary, which is a bank, shall be included in group's CET1 capital. Consequently, minority interest in the subsidiaries which are not banks shall not be included in the regulatory capital of the group. In other words, the proportion of surplus capital which is attributable to the minority shareholders shall be excluded from the group's CET1

capital. Further, the minority interest in relation to other components of regulatory capital shall also be recognised.

(2) Treatment of minority interest corresponding to common shares issued by consolidated subsidiaries

Minority interest arising from the issue of common shares by a fully consolidated subsidiary of the bank shall receive recognition in CET1 capital only if: (a) the instrument giving rise to the minority interest, if issued by the bank, meets all of the criteria for classification as common shares for regulatory capital purposes as stipulated in paragraph 13; and (b) the subsidiary that issued the instrument is itself a bank. The amount of minority interest meeting the criteria above that shall be recognised in consolidated CET1 capital shall be calculated as under:

(i) Total minority interest meeting the two criteria above minus the amount of the surplus CET1 capital of the subsidiary attributable to the minority shareholders;

(ii) Surplus CET1 capital of the subsidiary shall be calculated as the CET1 of the subsidiary minus the lower of: (a) the minimum CET1 capital requirement of the subsidiary plus the CCB (i.e., 8 per cent of RWAs) and (b) the portion of the consolidated minimum CET1 capital requirement plus the CCB (i.e., 8 per cent of consolidated RWAs) that relates to the subsidiary; and

(iii) The amount of the surplus CET1 capital that is attributable to the minority shareholders shall be calculated by multiplying the surplus CET1 with the percentage of CET1 that is held by minority shareholders.

Note - For the purposes of this paragraph (2), AIFIs, NBFCs regulated by the Reserve Bank and Primary Dealers shall be considered to be a bank.

(3) Treatment of minority interest corresponding to Tier 1 qualifying capital issued by consolidated subsidiaries

Tier 1 capital instruments issued by a fully consolidated subsidiary of the bank to third party investors [including amounts under paragraph 27(2)] may receive recognition in Tier 1 capital only if the instruments would, if issued by the bank,

meet all the criteria for classification as Tier 1 capital. The amount of this capital that shall be recognised in Tier 1 capital will be calculated as below:

(i) Total Tier 1 capital of the subsidiary issued to third parties minus the amount of the surplus Tier 1 capital of the subsidiary attributable to the third-party investors;

(ii) Surplus Tier 1 capital of the subsidiary shall be calculated as the Tier 1 capital of the subsidiary minus the lower of: (a) the minimum Tier 1 capital requirement of the subsidiary plus the CCB (i.e., 9.5 per cent of the RWAs) and (b) the portion of the consolidated minimum Tier 1 capital requirement plus the CCB (i.e., 9.5 per cent of the consolidated RWAs) that relates to the subsidiary;

(iii) The amount of the surplus Tier 1 capital that shall be attributable to the third-party investors shall be calculated by multiplying the surplus Tier 1 capital with the percentage of Tier 1 capital that is held by third party investors; and

(iv) The amount of this Tier 1 capital that will be recognised in AT1 capital shall exclude amounts recognised in CET1 capital under paragraph 27(2).

(4) Treatment of minority interest corresponding to Tier 1 capital and Tier 2 qualifying capital issued by consolidated subsidiaries

Total capital instruments (i.e., Tier 1 and Tier 2 capital instruments) issued by a fully consolidated subsidiary of a bank to third party investors [including amounts under paragraphs 27(2) and 27(3)] may receive recognition in the total capital only if the instruments, if issued by the bank, meet all of the criteria for classification as Tier 1 or Tier 2 capital. The amount of this capital that shall be recognised in consolidated total capital shall be calculated as follows:

(i) Total capital instruments of the subsidiary issued to third parties minus the amount of the surplus total capital of the subsidiary attributable to the third-party investors;

(ii) Surplus total capital of the subsidiary shall be calculated as the total capital of the subsidiary minus the lower of: (a) the minimum total capital requirement of the subsidiary plus the CCB (i.e., 11.5 per cent of the RWAs)

and (b) the portion of the consolidated minimum total capital requirement plus the CCB (i.e., 11.5 per cent of consolidated RWAs) that relates to the subsidiary;

(iii) The amount of the surplus total capital that shall be attributable to the third-party investors shall be calculated by multiplying the surplus total capital with the percentage of total capital that is held by third party investors;

(iv) The amount of this total capital recognised in Tier 2 capital shall exclude amounts recognised in CET1 capital and AT1 capital under paragraph 27(2) and paragraph 27(3) respectively.

(5) An illustration of calculation of minority interest and other capital issued out of consolidated subsidiaries that is held by third parties is as under:

(i) A banking group for this purpose consists of two legal entities that are both banks. Bank P is the parent and Bank S is the subsidiary and their unconsolidated balance sheets are set out below:

Bank P Balance Sheet		Bank S Balance Sheet	
Assets		Assets	
Loans to customers	100	Loans to customers	150
Investment in CET1 of Bank S	7		
Investment in the AT1 of Bank S	4		
Investment in the Tier 2 of Bank S	2		
Total	113	Total	150
Liabilities and equity		Liabilities and equity	
Depositors	70	Depositors	127
Tier 2	10	Tier 2	8
AT1	7	AT1	5
CET1	26	CET1	10
Total	113	Total	150

(ii) The balance sheet of Bank P shows that in addition to its loans to customers, it owns 70 per cent of the common shares of Bank S, 80 per cent of the AT1 of Bank S and 25 per cent of the Tier 2 capital of Bank S. The ownership of the capital of Bank S is therefore as follows:

Capital issued by Bank S			
	Amount issued to parent (Bank P)	Amount issued to third parties	Total

CET1	7	3	10
AT1	4	1	5
Tier 1 (T1)	11	4	15
Tier 2 (T2)	2	6	8
Total capital	13	10	23

Consolidated balance sheet		
Assets		Remarks
Loans to customers	250	Investments of P in S aggregating ₹13 will be cancelled during accounting consolidation
Liabilities and equity		
Depositors	197	
Tier 2 issued by subsidiary to third parties	6	(8-2)
Tier 2 issued by parent	10	
AT1 issued by subsidiary to third parties	1	(5-4)
AT1 issued by parent	7	
Common equity issued by subsidiary to third parties (i.e., minority interest)	3	(10-7)
Common equity issued by parent	26	
Total	250	

(iii) For illustrative purposes, Bank S is assumed to have RWAs of 100 against the actual value of assets of 150. In this example, the minimum capital requirements of Bank S and the subsidiary's contribution to the consolidated requirements are the same. This means that it is subject to the following minimum capital requirement plus CCB requirements and has the following surplus capital:

Minimum and surplus capital of bank S			
	Minimum plus capital conservation buffer required	Actual capital available	Surplus (3-2)
1	2	3	4
CET1 capital	7.0 (= 7.0% of 100)	10	3.0
Tier 1 capital	8.5 (= 8.5% of 100)	15 (10 + 5)	6.5
Total capital	10.5 (= 10.5% of 100)	23 (10 + 5 + 8)	12.5

(iv) The following table illustrates how to calculate the amount of capital issued by Bank S to include in consolidated capital, following the calculation procedure set out in paragraph 27(4) of these Directions:

Bank S: Amount of capital issued to third parties included in consolidated capital					
	Total amount issued (a)	Amount issued to third parties (b)	Surplus (c)	Surplus attributable to third parties (i.e., amount excluded from consolidated capital) (d) = (c) * (b) / (a)	Amount included in consolidated capital (e) = (b) – (d)
CET1 capital	10	3	3.0	0.90	2.10
Tier 1 capital	15	4	6.5	1.73	2.27
Total capital	23	10	12.5	5.43	4.57

(v) The following table summarises the components of capital for the consolidated group based on the amounts calculated in the table above. AT1 is calculated as the difference between CET1 and Tier 1, and Tier 2 is the difference between total Capital and Tier 1.

	Total amount issued by parent (all of which is to be included in consolidated capital)	Amount issued by subsidiaries to third parties to be included in consolidated capital	Total amount issued by parent and subsidiary to be included in consolidated capital
CET1 capital	26	2.10	28.10
AT1 capital	7	0.17	7.17
Tier 1 capital	33	2.27	35.27
Tier 2 capital	10	2.30	12.30
Total capital	43	4.57	47.57

G Regulatory adjustments / deductions

28. The following paragraphs deal with the regulatory adjustments / deductions which shall be applied to regulatory capital both at solo and consolidated level:

(1) Goodwill and all other intangible assets

(i) Goodwill and all other intangible assets shall be deducted from CET1 capital including any goodwill included in the valuation of significant investments in the capital of banking, financial, and insurance entities which

are outside the scope of regulatory consolidation. In terms of AS 23 - Accounting for investments in associates - goodwill / capital reserve arising on the acquisition of an associate by an investor shall be included in the carrying amount of investment in the associate but shall be disclosed separately. Therefore, if the acquisition of equity interest in any associate involves payment which can be attributable to goodwill, this shall be deducted from the CET1 capital of a bank.

(ii) The full amount of the intangible assets shall be deducted net of any associated DTL which would be extinguished if the intangible assets become impaired or derecognised under the relevant Accounting Standards. For this purpose, the definition of intangible assets shall be in accordance with the applicable Accounting Standards. Losses in the current period and those brought forward from previous periods shall also be deducted from CET1 capital, if not already deducted.

(iii) Application of these rules at consolidated level shall mean deduction of any goodwill and other intangible assets from the consolidated CET1 capital which is attributed to the balance sheets of subsidiaries, in addition to deduction of goodwill and other intangible assets which pertain to a solo bank.

(2) Deferred Tax Assets (DTAs)

(i) DTAs associated with accumulated losses and other such assets shall be deducted in full, from CET1 capital.

(ii) DTAs which relate to timing differences (other than those related to accumulated losses) may, instead of full deduction from CET1 capital, be recognised in the CET1 capital up to 10 per cent of a bank's CET1 capital, at its discretion [after the application of all regulatory adjustments mentioned from paragraphs 28(1) to 28(8)(ii)(c)(ii)].

(iii) Further, the limited recognition of DTAs as at paragraph (ii) above along with limited recognition of significant investments in the common shares of unconsolidated financial (i.e., banking, financial, and insurance) entities in terms of paragraph 28(8)(ii)(c)(ii) taken together shall not exceed 15 per cent of the CET1 capital, calculated after all regulatory adjustments set out

from paragraphs 28(1) to 28(8). Paragraph (vi) below provides an illustration of this applicable limited recognition. However, a bank shall ensure that the CET1 capital arrived at after application of 15 per cent limit, specified above, shall in no case result in recognising any item more than the 10 per cent limit applicable individually.

(iv) The amount of DTAs to be deducted from CET1 capital may be netted with associated DTLs provided that:

(a) both the DTAs and DTLs relate to taxes levied by the same taxation authority and offsetting is permitted by the relevant taxation authority;

(b) the DTLs permitted to be netted against DTAs shall exclude amounts that have been netted against the deduction of goodwill, intangibles, and defined benefit pension assets; and

(c) the DTLs shall be allocated on a pro rata basis between DTAs subject to deduction from CET1 capital as at (i) and (ii) above.

(v) The amount of DTAs which is not deducted from CET1 capital (in terms of paragraph (ii) above) shall be risk weighted at 250 per cent as in the case of significant investments in common shares not deducted from bank's CET1 capital as indicated in paragraph 28(8)(ii)(c)(iii).

(vi) Illustration on calculation of 15 per cent of common equity limit on items subject to limited recognition (i.e., DTAs associated with timing differences and significant investments in common shares of unconsolidated financial entities)

(a) A bank shall follow the 15 per cent limit on significant investments in the common shares of unconsolidated financial institutions (banks, insurance, and other financial entities) and DTA arising from timing differences (collectively referred to as specified items) as stipulated in paragraph 28.

(b) The recognition of these specified items will be limited to 15 per cent of CET1 capital, after the application of all deductions. To determine the maximum amount of the specified items that can be recognised*, a bank shall multiply the amount of CET1** (after all deductions,

including after the deduction of the specified items in full, i.e., specified items should be fully deducted from CET1 along with other deductions first for arriving at CET1**) by 17.65 per cent. This number, i.e., 17.65 per cent is derived from the proportion of 15 per cent to 85 per cent (15% / 85% = 17.65%).

Explanation -

(i) * The actual amount that will be recognised may be lower than this maximum, either because the sum of the three specified items is below the 15 per cent limit set out in this illustration, or due to the application of the 10 per cent limit applied to each item.

(ii) ** At this point, this is a 'hypothetical' amount of CET1 in that it is used only for the purposes of determining the deduction of the specified items.

(c) As an example, take a bank with ₹85 of common equity (calculated net of all deductions, including after the deduction of the specified items in full).

(d) The maximum amount of specified items that can be recognised by this bank in its calculation of CET1 capital is ₹85 x 17.65 per cent = ₹15. Any excess above ₹15 shall be deducted from CET1. If the bank has specified items (excluding amounts deducted after applying the individual 10 per cent limits) that in aggregate sum up to the 15 per cent limit, CET1 after inclusion of the specified items, shall amount to ₹85 + ₹15 = ₹100. The percentage of specified items to total CET1 shall equal 15 per cent.

(3) Cash flow hedge reserve

(i) The amount of the cash flow hedge reserve that relates to the hedging of items that are not fair valued on the balance sheet (including projected cash flows) shall be derecognised in the calculation of CET1 capital. This means that positive amounts shall be deducted, and negative amounts shall be added back.

(ii) Application of the above rule at consolidated level shall mean derecognition of cash flow hedge reserve from the consolidated CET1 capital that is attributed to the subsidiaries, in addition to derecognition of cash flow hedge reserve pertaining to the solo bank.

(4) Gain on sale related to securitisation transactions, unrealised profits arising because of transfer of loan exposures, and Security Receipts (SRs) guaranteed by the government of India

(i) A bank shall be guided by the paragraph 88 in this regard. Application of these rules at consolidated level shall mean deduction of gain on sale from the consolidated CET1 capital which is recognised by the subsidiaries in their profit and loss and / or equity, in addition to deduction of any gain on sale recognised by the bank at the solo level.

(ii) A bank shall be guided by the Reserve Bank of India (Commercial Banks – Transfer and Distribution of Credit Risk) Directions, 2025 for the prudential treatment of unrealised profits arising because of transfer of loan exposures and SRs guaranteed by the Government of India.

(5) Cumulative gains and losses due to changes in own credit risk on fair valued financial liabilities

(i) A bank shall derecognise all unrealised gains and losses resulting from changes in the fair value of liabilities due to changes in the bank's own credit risk from CET1 capital. Additionally, with regard to derivative liabilities, all accounting valuation adjustments arising from the bank's own credit risk shall also be derecognised from CET1 capital. The offsetting between valuation adjustments arising from the bank's own credit risk and those arising from its counterparties' credit risk shall not be allowed.

(ii) If a bank values its derivatives and Securities Financing Transactions (SFTs) liabilities taking into account its own creditworthiness in the form of Debit Valuation Adjustments (DVAs), the bank shall deduct all DVAs from its CET1 capital, irrespective of whether the DVAs arises due to changes in its own credit risk or other market factors. Thus, such deduction shall also include the deduction of initial DVA at inception of a new trade. In other words, though a bank shall recognise a loss reflecting the credit risk of the

counterparty [i.e., Credit Valuation Adjustments (CVA)], the bank shall not recognise the corresponding gain due to its own credit risk in CET1 capital.

(iii) Application of the above rules at consolidated level shall mean derecognition of unrealised gains and losses, resulting from changes in the fair value of liabilities due to changes in the subsidiaries' credit risk, from the calculation of consolidated CET1 capital, in addition to derecognition of any such unrealised gains and losses attributed to the bank at the solo level.

(6) Defined benefit pension fund (including other defined employees' funds) assets and liabilities

(i) Defined benefit pension fund liabilities, as included on the balance sheet, shall be fully recognised in the calculation of CET1 capital (i.e., CET1 capital shall not be increased by derecognising these liabilities). For each defined benefit pension fund that is an asset on the balance sheet, the asset shall be deducted in the calculation of CET1 capital net of any associated DTL which would be extinguished if the asset becomes impaired or derecognised under the relevant Accounting Standards.

(ii) Application of the above rule at consolidated level shall mean deduction of defined benefit pension fund assets and recognition of defined benefit pension fund liabilities pertaining to subsidiaries in the consolidated CET1 capital, in addition to those pertaining to the solo bank.

(7) Investments in own shares (Treasury stock)

(i) Investment in a bank's own shares shall be tantamount to repayment of capital and therefore, it is necessary to knock-off such investment from the bank's capital with a view to improving the bank's quality of capital. This deduction shall remove the double counting of equity capital arising from direct holdings, indirect holdings via index funds and potential future holdings as a result of contractual obligations to purchase own shares.

(ii) A bank shall not repay its equity capital without specific approval of the Reserve Bank. Repayment of equity capital can take place by way of share buy-back, investments in own shares (treasury stock) or payment of dividends out of reserves, none of which is permissible. However, a bank

may end up having indirect investments in its own stock if it invests in / takes exposures to mutual funds or index funds / securities which have long position in the bank's share. In such cases, the bank shall look through holdings of index securities to deduct exposures to own shares from its CET1 capital. Following the same approach outlined above, a bank shall deduct investments in its own AT1 capital from the calculation of its AT1 capital and investments in its own Tier 2 capital from the calculation of its Tier 2 capital. In this regard, the following rules may be observed:

(a) If the amount of investments made by the mutual funds / index funds / venture capital funds / private equity funds / investment companies in the capital instruments of the investing bank is known, the indirect investment shall be equal to the bank's investments in such entities multiplied by the per cent of investments of these entities in the investing bank's respective capital instruments;

(b) If the amount of investments made by the mutual funds / index funds / venture capital funds / private equity funds / investment companies in the capital instruments of the investing bank is not known but, as per the investment policies / mandate of these entities such investments are permissible, the indirect investment would be equal to the bank's investments in these entities multiplied by 10 per cent of investments of such entities in the investing bank's capital instruments. A bank shall not follow corresponding deduction approach, i.e., all deductions shall be made from the CET1 capital even if the investments of such entities are in the AT1 / Tier 2 capital of an investing bank.

Note - In terms of Securities and Exchange Board of India (SEBI) (Mutual Funds) Regulations 1996, no mutual fund under all its schemes should own more than ten per cent of any company's paid-up capital carrying voting rights.

(iii) Application of these rules at consolidated level shall mean deduction of subsidiaries' investments in its own shares (direct or indirect) in addition to

the bank's direct or indirect investments in its own shares while computing consolidated CET1 capital.

(8) Investments in the capital of banking, financial, and insurance entities

The rules under this paragraph shall be applicable to a bank's equity investments in other banks and financial entities, even if such investments are exempted from 'capital market exposure' limit.

(i) Limits on a bank's investments in the capital of banking, financial, and insurance entities

(a) A bank's investments in capital instruments issued by banking, financial and insurance entities shall not exceed 10 per cent of its total regulatory capital (Tier 1 plus Tier 2), but after all deductions mentioned in paragraph 28 (1) to paragraph 28(7).

(b) The indicative list of institutions which shall be deemed to be financial institutions other than banks and insurance companies for the purpose of this paragraph is as under:

(i) Asset Management Companies of Mutual Funds / Venture Capital Funds / Private Equity Funds etc.;

(ii) Non-Banking Finance Companies;

(iii) Housing Finance Companies;

(iv) Primary Dealers;

(v) Merchant Banking Companies;

(vi) Entities engaged in activities which are ancillary to the business of banking under the BR Act, 1949; and

(vii) Central Counterparties (CCPs).

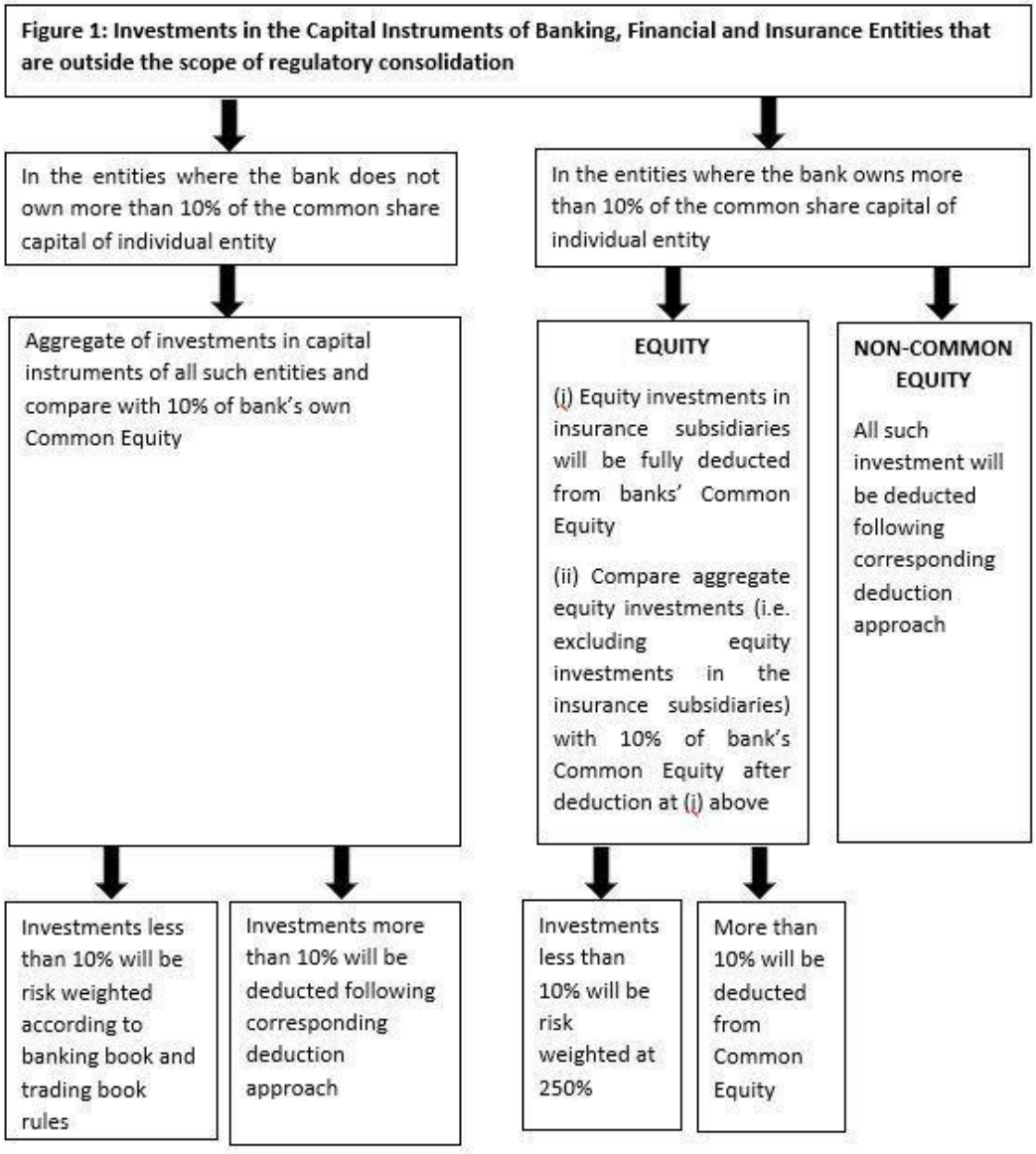
(c) Investments made by a banking subsidiary / associate in the equity or non-equity regulatory capital instruments issued by its parent bank shall be deducted from such subsidiary's regulatory capital following corresponding deduction approach, in its capital adequacy assessment on a solo basis.

(d) The regulatory treatment of investment by the non-banking financial subsidiaries / associates in the parent bank's regulatory capital shall be governed by the applicable regulatory capital norms of the respective regulators of such subsidiaries / associates.

(ii) Treatment of a bank's investments in capital instruments issued by banking, financial and insurance entities within limits

A schematic representation of treatment of a bank's investments in capital instruments of financial entities is shown below. All investments in the capital instruments issued by banking, financial, and insurance entities within the limits mentioned in paragraph 28(8)(i) shall be subject to the following rules:

Note - For this purpose, investments may be reckoned at values according to their classification in terms of Reserve Bank of India (Commercial Banks – Classification, Valuation and Operation of Investment Portfolio) Directions, 2025.



(a) Reciprocal cross holdings in the capital of banking, financial, and insurance entities

Reciprocal cross holdings of capital shall be fully deducted. A bank shall apply a corresponding deduction approach to such investments in the capital of the other banks, financial institutions, and insurance entities. This means the deduction shall be applied to the same component of capital (CET1, AT1, and Tier 2 capital) for which the

capital would qualify if it was issued by the bank itself. For this purpose, a holding shall be treated as reciprocal cross holding if the investee entity has also invested in any class of a bank's capital instruments which need not necessarily be the same as the bank's holdings.

(b) Investments in the capital of banking, financial, and insurance entities which are outside the scope of regulatory consolidation and where the bank does not own more than 10 per cent of the issued common share capital of the entity

Note – Investments in entities that are outside the scope of regulatory consolidation refers to investments in entities that have not been consolidated at all or have not been consolidated in such a way as to result in their assets being included in the calculation of consolidated RWAs of the group.

(i) The regulatory adjustment described in this paragraph applies to investments in the capital of banking, financial, and insurance entities that are outside the scope of regulatory consolidation and where a bank does not own more than 10 per cent of the issued common share capital of individual entity. In addition:

(a) Investments include direct, indirect, and synthetic holdings of capital instruments. For example, a bank shall look through holdings of index securities to determine its underlying holdings of capital.

Explanation - Indirect holdings are exposures or part of exposures that, if a direct holding loses its value, will result in a loss to the bank substantially equivalent to the loss in the value of direct holding.

(b) Holdings in both the Banking Book and Trading Book shall be included. Capital includes common stock (paid-up equity capital) and all other types of cash and synthetic capital instruments (e.g., subordinated debt).

(c) Underwriting positions held for five working days or less can be excluded. Underwriting positions held for longer than five working days shall be included.

(d) If the capital instrument of the entity in which a bank has invested does not meet the criteria for CET1, AT1, or Tier 2 capital of the bank, the capital is to be considered common shares for the purposes of this regulatory adjustment. If the investment is issued out of a regulated financial entity and not included in regulatory capital in the relevant sector of the financial entity, it is not required to be deducted.

(e) With the prior approval of the Reserve Bank, a bank can temporarily exclude certain investments where these have been made in the context of resolving or providing financial assistance to reorganise a distressed institution.

(ii) If the total of all holdings listed in paragraph (i) above, in aggregate exceed 10 per cent of the bank's CET1 capital (after applying all other regulatory adjustments in full), the amount above 10 per cent shall be deducted, applying a corresponding deduction approach. This means the deduction shall be applied to the same component of capital for which the capital would qualify if it was issued by the bank itself. Accordingly, the amount to be deducted from the CET1 capital shall be calculated as the total of all holdings which in aggregate exceed 10 per cent of the bank's CET1 capital (as per above) multiplied by the common equity holdings as a percentage of the total capital holdings. This shall result in a deduction from CET1 capital which corresponds to the proportion of total capital holdings held in common equity. Similarly, the amount to be deducted from AT1 capital shall be calculated as the total of all holdings which in aggregate exceed 10 per cent of the bank's CET1 capital (as per above) multiplied by the AT1 capital holdings as a percentage of the total capital holdings. The amount to be deducted from Tier 2 capital shall be

calculated as the total of all holdings which in aggregate exceed 10 per cent of the bank's CET1 capital (as per above) multiplied by the Tier 2 capital holdings as a percentage of the total capital holdings. (Please refer to illustration given under paragraph 28(8)(ii)(b)(vi)).

(iii) If, under the corresponding deduction approach, a bank is required to make a deduction from a particular Tier of capital and it does not have enough capital under that Tier to meet that deduction, the shortfall shall be deducted from the next higher Tier of capital (e.g., if a bank does not have enough AT1 capital to satisfy the deduction, the shortfall shall be deducted from CET1 capital).

(iv) Investments below the threshold of 10 per cent of a bank's CET1 capital, which are not deducted, shall be risk weighted. Thus, instruments in the Trading Book shall be treated as per the market risk rules and instruments in the Banking Book shall be treated as per the standardised approach for credit risk mentioned in these Directions. For the application of risk weighting, the amount of the holdings which are required to be risk weighted shall be allocated on a pro rata basis between the banking and trading book. However, in certain cases, such investments in both scheduled and non-scheduled commercial banks shall be fully deducted from CET1 capital of the investing bank as indicated in paragraphs 42 to 45, 188, and 198.

(v) For risk weighting as indicated in paragraph (iv) above, investments in securities having comparatively higher risk weights shall be considered for risk weighting to the extent required to be risk weighted, both in banking and trading books. In other words, investments with comparatively poor ratings (i.e., with higher risk weights) shall be considered for application of risk weighting first and the residual investments shall be considered for deduction.

(vi) Illustration on regulatory adjustment due to investments in the capital of banking, financial, and insurance entities which are outside the scope of regulatory consolidation is as under:

(a) Details of regulatory capital structure of a bank

	(Amount in ₹ crore)
Paid-up equity capital	300
Eligible Reserve and Surplus	100
Total common equity	**400**
Eligible AT1 capital	15
Total Tier 1 capital	**415**
Eligible Tier 2 capital	135
Total Eligible capital	**550**

(b) Details of capital structure and bank's investments in unconsolidated entities

Entity	**Total Capital of the Investee entities**				**Investments of bank in these entities**			
	CET1	AT1	Tier 2	Total capital	Common Equity	AT1	Tier 2	Total Investment
Investments in the capital of banking, financial, and insurance entities which are outside the scope of regulatory consolidation and where the bank does not own more than 10% of the issued common share capital of the entity								
A	250	0	80	**330**	12	0	15	**27**
B	300	10	0	**310**	14	10	0	**24**
Total	**550**	**10**	**80**	**640**	**26**	**10**	**15**	**51**
Significant investments in the capital of banking, financial, and insurance entities which are outside the scope of regulatory consolidation								
C	150	20	10	**180**	20	10	0	**30**
D	200	10	5	**215**	25	5	5	**35**
Total	**350**	**30**	**15**	**395**	**45**	**15**	**5**	**65**

(c) Regulatory adjustments on account of investments in entities where bank does not own more than 10 per cent of the issued common share capital of the entity

C-1: Bifurcation of Investments of bank into Trading and Banking Book				
	CET1	AT1	Tier 2	Total Investment
Total investments in A & B held in Banking Book	11	6	10	**27**
Total investments in A & B held in Trading Book	15	4	5	**24**
Total of Banking and Trading Book Investments in A & B	**26**	**10**	**15**	**51**

C-2: Regulatory adjustments	
Bank's aggregate investment in Common Equity of A & B	26
Bank's aggregate investment in AT1 capital of A & B	10
Bank's aggregate investment in Tier 2 capital of A & B	15
Total of bank's investment in A and B	**51**
Bank common equity	400
10% of bank's common equity	40
Bank's total holdings in capital instruments of A & B in excess of 10% of banks common equity (51 - 40)	11

Note - Investments in both A and B will qualify for this treatment as individually, both of them are less than 10% of share capital of respective entity. Investments in C & D do not qualify as bank's investment is more than 10% of its common share capital.

C-3: Summary of Regulatory Adjustments		Banking Book	Trading Book
Amount to be deducted from common equity of the bank (26 / 51) * 11	5.60		
Amount to be deducted from AT1 of the bank (10 / 51) * 11	2.16		
Amount to be deducted from Tier 2 of the bank (15 / 51) * 11	3.24		
Total Deduction	**11.00**		
Common equity investments of the bank in A & B to be risk weighted	20.40 (26 - 5.60)	8.63 (11 / 26) * 20.40	11.77
AT1 capital investments of the bank in A & B to be risk weighted	7.84 (10 - 2.16)	4.70	3.14
Tier 2 capital investments of the bank in A & B to be risk weighted	11.76 (15 - 3.24)	7.84	3.92
Total allocation for risk weighting	**40.00**	21.17	18.83

(d) Regulatory adjustments on account of significant investments in the capital of banking, financial and insurance entities which are outside the scope of regulatory consolidation

Bank aggregate investment in Common Equity of C & D	45
Bank's aggregate investment in AT1 capital of C & D	15
Bank's aggregate investment in Tier 2 capital of C & D	5
Total of bank's investment in C and D	**65**
Bank's common equity	400
10% of bank's common equity	40
Bank's investment in equity of C & D in excess of 10% of its common equity (45 - 40)	5

D-1: Summary of regulatory adjustments	
Amount to be deducted from common equity of the bank (excess over 10%)	5
Amount to be deducted from AT1 of the bank (all AT1 investments to be deducted)	15
Amount to be deducted from Tier 2 of the bank (all Tier 2 investments to be deducted)	5
Total deduction	**25**
Common equity investments of the bank in C & D to be risk weighted (up to 10%)	40

(e) Total regulatory capital of the bank after regulatory adjustments

	Before deduction	Deductions as per Table C-3	Deductions as per Table D-1	After deductions
Common Equity	400.00	5.61	5.00	387.24*
AT1 capital	15.00	2.16	15.00	0.00
Tier 2 capital	135.00	3.24	5.00	126.76
Total Regulatory capital	**550.00**	**11.00**	**25.00**	**514.00**
*Since there is a shortfall of 2.16 in the AT1 capital of the bank after deduction, which has to be deducted from the next higher category of capital i.e., common equity.				

(c) **Investments in the capital of banking, financial, and insurance entities which are outside the scope of regulatory consolidation where the bank owns more than 10 per cent of the issued common share capital of individual entity**

(i) The regulatory adjustment described in this paragraph applies to investments in the capital of banking, financial, and insurance entities that are outside the scope of regulatory consolidation where a bank owns more than 10 per cent of the issued common

share capital of the issuing entity or where the entity is an affiliate of the bank. In addition:

(a) Investments include direct, indirect, and synthetic holdings of capital instruments. For example, a bank shall look through holdings of index securities to determine its underlying holdings of capital.

(b) Holdings in both the Banking Book and Trading Book shall be included. Capital includes common stock and all other types of cash and synthetic capital instruments (e.g., subordinated debt).

(c) Underwriting positions held for five working days or less can be excluded. Underwriting positions held for longer than five working days shall be included.

(d) If the capital instrument of the entity in which a bank has invested does not meet the criteria for CET1, AT1, or Tier 2 capital of the bank, the capital shall be considered common shares for the purposes of this regulatory adjustment. If the investment is issued out of a regulated financial entity and not included in regulatory capital in the relevant sector of the financial entity, it is not required to be deducted.

(e) With the prior approval of the Reserve Bank, a bank can temporarily exclude certain investments where these have been made in the context of resolving or providing financial assistance to reorganise a distressed institution.

Explanation -

(i) An affiliate of a bank is defined as a company that controls, or is controlled by, or is under common control with, the bank. Control of a company is defined as (i) ownership, control, or holding with power to vote 20 per cent or more of a class of voting

securities of the company; or (ii) consolidation of the company for financial reporting purposes.

(ii) Indirect holdings are exposures or part of exposures that, if a direct holding loses its value, will result in a loss to the bank substantially equivalent to the loss in the value of direct holding.

(ii) Investments other than common shares

All investments included in paragraph (i) above which are not common shares shall be fully deducted following a corresponding deduction approach. This means the deduction shall be applied to the same Tier of capital for which the capital would qualify if it was issued by a bank itself. If a bank is required to make a deduction from a particular Tier of capital and it does not have enough capital under that Tier to meet that deduction, the shortfall shall be deducted from the next higher Tier of capital (e.g., if a bank does not have enough AT1 capital to satisfy the deduction, the shortfall shall be deducted from CET1 capital).

(iii) Investments which are common shares

All investments included in paragraph (i) above which are common shares, and which exceed 10 per cent of a bank's CET1 capital (after the application of all regulatory adjustments) shall be deducted while calculating CET1 capital. The amount that is not deducted (up to 10 per cent if bank's common equity invested in the equity capital of such entities) in the calculation of CET1 shall be risk weighted at 250 per cent [refer to illustration given under paragraph 28(8)(ii)(b)(vi)]. However, in certain cases, such investments in both scheduled and non-scheduled commercial banks shall be fully deducted from CET1 capital of an investing bank as required in paragraphs 42 to 45, 188 and 198.

(iii) With regard to computation of indirect holdings through mutual funds or index funds, of capital of banking, financial, and insurance entities which

are outside the scope of regulatory consolidation as mentioned in paragraphs 28(8)(ii)(b) and paragraphs 28(8)(ii)(c) above, the following rules shall be observed:

(a) If the amount of investments made by the mutual funds / index funds / venture capital funds / private equity funds / investment companies in the capital instruments of the financial entities is known, the indirect investment of a bank in such entities shall be equal to bank's investments in these entities multiplied by the percent of investments of such entities in the financial entities' capital instruments;

(b) If the amount of investments made by the mutual funds / index funds / venture capital funds / private equity funds / investment companies in the capital instruments of the investing bank is not known but, as per the investment policies / mandate of these entities such investments are permissible, the indirect investment shall be equal to the bank's investments in these entities multiplied by maximum permissible limit which these entities are authorized to invest in the financial entities' capital instruments; and

(c) If neither the amount of investments made by the mutual funds / index funds / venture capital funds / private equity funds in the capital instruments of financial entities nor the maximum amount which these entities can invest in financial entities are known but, as per the investment policies / mandate of these entities such investments are permissible, the entire investment of the bank in these entities shall be treated as indirect investment in financial entities. A bank shall note that this method does not follow corresponding deduction approach, i.e., all deductions shall be made from the CET1 capital even though, the investments of such entities are in the AT1 / Tier 2 capital of the investing bank.

(iv) Application of these rules at consolidated level shall mean:

(a) Identifying the relevant entities below and above threshold of 10 per cent of common share capital of investee entities, based on aggregate

investments of the consolidated group (parent plus consolidated subsidiaries) in common share capital of individual investee entities.

(b) Applying the rules as stipulated in paragraphs 28(8)(ii)(a), 28(8)(ii)(b) and 28(8)(ii)(c) and segregating investments into those which shall be deducted from the consolidated capital and those which shall be risk weighted. For this purpose:

(i) investments of the entire consolidated entity in capital instruments of investee entities shall be aggregated into different classes of instruments; and

(ii) the consolidated CET1 capital of the group shall be taken into account.

(9) When returns of the investors of the capital issues are counter guaranteed by the bank, such investments shall not be considered as regulatory capital for the purpose of capital adequacy.

Explanation - Certain investors such as Employee Pension Funds subscribe to regulatory capital issues of commercial banks concerned and these funds enjoy the counter guarantee by the bank concerned in respect of returns. Such investments shall not be considered as regulatory capital.

(10) Equity investments in non-financial subsidiaries

As indicated in paragraphs 8(3) and 8(6), equity investments in non-financial subsidiaries shall be fully deducted from the consolidated and solo CET1 capital of a bank, after making all the regulatory adjustments as indicated in above paragraphs.

(11) Intra group transactions and exposures

Intra-group exposures beyond permissible limits, if any, shall be deducted from CET1 capital of a bank.

Note – Permissible limits are mentioned in the Reserve Bank of India (Commercial Banks – Concentration Risk Management) Directions, 2025.

(12) Net unrealised gains arising on fair valuation of Level 3 financial instruments

The net unrealised gains arising on fair valuation of Level 3 financial instruments (including derivatives) shall be deducted from CET1 capital.

(13) Investment in the subordinated units of any AIF scheme

If a bank's contribution is in the form of subordinated units of any AIF scheme, then it shall deduct the entire investment from its capital funds – proportionately from both Tier 1 and Tier 2 capital (wherever applicable).

Note - A bank shall also refer to Reserve Bank of India (Commercial Banks – Undertaking of Financial Services) Directions, 2025 in this regard.

(14) In terms of Reserve Bank of India (Commercial Banks – Credit Facilities) Directions, 2025, if a bank is the Default Loss Guarantee (DLG) provider, it shall deduct the full amount of DLG, which is outstanding, from its capital.

H Guidelines on general permission for infusion of capital in overseas banking centres and retention / repatriation / transfer of profits in these centres by banks incorporated in India

(Not applicable to a foreign bank)

29. A bank shall adhere to the following guidelines on general permission for infusion of capital in overseas banking centres and retention / repatriation / transfer of profits in these centres:

(1) A bank which meets the regulatory capital requirements (including CCB, Domestic – Systemically Important Bank (D-SIB) capital requirements where applicable, and CCCB as may be mandated) may, with the approval of its Boards:

(i) infuse capital in its overseas branches and banking subsidiaries; and

(ii) retain profits in, and transfer or repatriate profits from these overseas centres.

Explanation – Overseas banking centers, in the context of this paragraph, include branches, banking subsidiaries, joint ventures, and associates. A bank shall continue to take the applicable Reserve Bank approvals necessary for opening and for change in the nature of these centres.

(2) A bank shall, while considering such proposals, analyse all relevant aspects including inter alia the business plans, home and host country regulatory requirements and performance parameters of its overseas centres. A bank shall also ensure compliance with all applicable home and host country laws and regulations.

(3) A bank which does not meet the minimum regulatory capital requirements shall seek prior approval of the Reserve Bank.

(4) A bank shall report all such instances of infusion of capital and / or retention / transfer / repatriation of profits in overseas branches and banking subsidiaries within 30 days of such action, to the Chief General Manager-in-Charge, DoR, Central Office, Mumbai with a copy to Chief General Manager-in-Charge, DoS, Central Office, Mumbai. In case of retention of profits in overseas branch / subsidiary, the reporting shall be done within 30 days of the finalisation of the annual financial statements of the overseas branch / subsidiary.

Chapter IV

Risk weighted assets (RWAs)

A Capital charge for credit risk

A.1 General

30. A bank shall follow the standardised approach for computing the capital charge for credit risk. Under this approach, a bank shall rely upon the ratings assigned by the external credit rating agencies specifically accredited by Reserve Bank that meet the eligibility criteria specified under the revised framework or specific risk weights prescribed in these directions, as the case may be.

A.2 Claims on domestic sovereigns

31. Both fund-based and non-fund-based claims on the Central Government shall attract zero risk weight. Central Government guaranteed claims shall also attract zero risk weight.

32. Direct loan / credit / overdraft exposure, if any, of a bank to the State Governments and the investment in State Government securities shall attract zero risk weight. State Government guaranteed claims shall attract 20 per cent risk weight.

33. The risk weight applicable to claims on Central Government exposures shall also apply to the claims on the Reserve Bank, Deposit Insurance and Credit Guarantee Corporation (DICGC), Credit Guarantee Fund Trust for Micro and Small Enterprises (CGTMSE), Credit Risk Guarantee Fund Trust for Low Income Housing (CRGFTLIH), and individual schemes under National Credit Guarantee Trustee Company Ltd. (NCGTC) which are backed by explicit Central Government Guarantee. The claims on Export Credit Guarantee Corporation shall also attract a risk weight of 20 per cent.

34. The risk weight of zero per cent as mentioned in paragraph 33 shall be applicable in respect of exposures guaranteed under any existing or future schemes launched by CGTMSE, CRGFTLIH, and NCGTC satisfying the following conditions:

    (i) Prudential aspects: The guarantees provided under the respective schemes shall comply with the requirements for credit risk mitigation in

terms of paragraphs 167 to 176 of these Directions which inter alia requires such guarantees to be direct, explicit, irrevocable and unconditional.

(ii) Restrictions on permissible claims: Where the terms of the guarantee schemes restrict the maximum permissible claims through features like specified extent of guarantee coverage, clause on first loss absorption by member lending institutions (MLI), payout cap, etc., the zero per cent risk weight shall be restricted to the maximum permissible claim and the residual exposure shall be subjected to risk weight as applicable to the counterparty in terms of extant regulations.

(iii) In case of a portfolio-level guarantee, effective from April 1, 2023, the extent of exposure subjected to first loss absorption by the MLI, if any, shall be subjected to full capital deduction and the residual exposure shall be subjected to risk weight as applicable to the counterparty in terms of extant regulations, on a pro rata basis. The maximum capital charge shall be capped at a notional level arrived at by treating the entire exposure as unguaranteed.

(iv) Subject to the aforementioned prescriptions, any scheme launched after September 7, 2022, under any of the aforementioned Trust Funds, in order to be eligible for zero per cent risk weight, shall provide for settlement of the eligible guaranteed claims within thirty days from the date of lodgment, and the lodgment shall be permitted within sixty days from the date of default. Some illustrative examples of risk weights applicable on claims guaranteed under specific existing schemes are as follows:

Scheme name	Guarantee Cover	Risk Weight
1. Credit Guarantee Fund Scheme for Factoring (CGFSF)	The first loss of 10% of the amount in default to be borne by Factors. The remaining 90% (i.e., second loss) of the amount in default will be borne by NCGTC and Factors in the ratio of 2:1 respectively	First loss of 10% amount in default – Full capital deduction 60% amount in default borne by NCGTC- 0% RW. Balance 30% amount in default Counterparty / Regulatory Retail Portfolio (RRP) RW as applicable.

Scheme name	Guarantee Cover	Risk Weight
		Note - The maximum capital charge shall be capped at a notional level arrived by treating the entire exposure as unguaranteed.
2. Credit Guarantee Fund Scheme for Skill Development (CGFSD)	75% of the amount in default. 100% of the guaranteed claims shall be paid by the Trust after all avenues for recovery have been exhausted and there is no scope for recovering the default amount.	Entire amount in default - Counterparty / Regulatory Retail Portfolio (RRP) RW as applicable.
3. Credit Guarantee Fund for Micro Units (CGFMU)	Micro Loans The first loss to the extent of 3% of amount in default. Out of the balance, guarantee will be to a maximum extent of 75% of the amount in default in the crystallized portfolio	First loss of 3% amount in default – Full capital deduction 72.75% of the amount in default - 0% RW, subject to maximum of $(\{15\% * \mathrm{CP}\} - \mathrm{C}) * \left[\frac{\mathrm{SLA}}{\mathrm{CP}}\right]$ Where- o CP = Crystallized Portfolio (sanctioned amount) o C = Claims received in previous years, if any, in the crystallized portfolio o SLA = Sanctioned limit of each account in the crystallized portfolio o 15 per cent represents the payout cap Balance amount in default - Counterparty / RRP RW as applicable. *Note* - The maximum capital charge shall be capped at a notional level arrived by treating

Scheme name	Guarantee Cover	Risk Weight
		the entire exposure as unguaranteed.
4.CGTMSE guarantee coverage for Micro-Enterprises	Up to ₹5 lakh 85% of the amount in default subject to a maximum of ₹4.25 lakh Above ₹5 lakh & up to ₹50 lakh 75% of the amount in default subject to a maximum of ₹37.50 lakh Above ₹50 lakh & up to ₹200 lakh 75% of the amount in default subject to a maximum of ₹150 lakh	Guaranteed amount in default – 0% RW* Balance amount in default - Counterparty / RRP RW as applicable.
*In terms of the payout cap stipulations of CGTMSE, claims of the member lending institutions will be settled to the extent of 2 times of the fee including recovery remitted during the previous financial year. However, since the balance claims will be settled in subsequent year / s as the position is remedied, the entire extent of guaranteed portion may be assigned zero percent risk weight.		

Note -

(a) The above regulatory stipulation shall be applicable to a bank to the extent it is recognised as eligible MLIs under the respective schemes.

(b) Guarantee coverage, first loss percentage, and payout cap ratio may be factored in as given above and as amended from time to time in the respective schemes.

35. The above risk weights for both direct claims and guarantee claims shall be applicable as long as they are classified as 'standard' / performing assets. Where these sovereign exposures are classified as non-performing, they shall attract risk weights as applicable to NPAs, which are detailed in paragraphs 63 to 68.

36. The above risk weights shall be applied if such exposures are denominated in Indian rupees and also funded in Indian rupees.

A.3 Claims on foreign sovereigns and foreign central banks

37. Subject to paragraph 38 below, claims on foreign sovereigns and their central banks shall attract risk weights as per the rating assigned to those sovereigns

and central banks / sovereign and central bank claims, by international rating agencies as follows:

Table 5: Claims on foreign sovereigns / central banks – risk weights

Standard & Poor's (S&P) / Fitch ratings	AAA to AA	A	BBB	BB to B	Below B	Unrated
Moody's ratings	Aaa to Aa	A	Baa	Ba to B	Below B	Unrated
Risk weight (%)	0	20	50	100	150	100

Explanation - The risk weight assigned to an investment in US Treasury Bills by any overseas branch of an Indian Bank in Paris, irrespective of the currency of funding, shall be determined by the rating assigned to the Treasury Bills, as indicated in Table 5.

38. Claims on the foreign sovereign or foreign central bank in their jurisdiction, denominated in the domestic currency of that jurisdiction, met out of resources of the same currency shall attract a risk weight of zero per cent. However, in case a host country supervisor requires a more conservative treatment to such claims in the books of the foreign branches of the Indian bank, it shall adopt the requirements prescribed by the host country supervisors for computing capital adequacy.

Explanation - The risk weight assigned to an investment in US Treasury Bills by overseas branch of any Indian bank in New York shall attract a zero per cent risk weight, irrespective of the rating of the claim, if the investment is funded from out of the USD denominated resources of that overseas branch of the Indian bank in New York. In case the overseas branch of the Indian bank in New York, did not have any USD denominated resources, the risk weight shall be determined by the rating assigned to the Treasury Bills, as indicated in Table 5 above.

A.4 Claims on public sector entities (PSEs)

39. Claims on domestic PSEs shall be risk weighted as claims on corporates given in paragraphs 47 to 49.

40. Claims on foreign PSEs shall be risk weighted as per the rating assigned by the international rating agencies as under:

Table 6: Claims on foreign PSEs – risk weights

S&P / Fitch ratings	AAA to AA	A	BBB to BB	Below BB	Unrated
Moody's ratings	Aaa to Aa	A	Baa to Ba	Below Ba	Unrated
Risk weight (%)	20	50	100	150	100

A.5 Claims on Multilateral Development Banks (MDBs), Bank for International Settlements (BIS) and International Monetary Fund (IMF)

41. Claims on the BIS, the IMF, and the following eligible MDBs evaluated by the Basel Committee on Banking Supervision (BCBS) shall be treated as claims on scheduled banks meeting the minimum capital adequacy requirements and assigned a uniform twenty per cent risk weight:

(i) World Bank Group: IBRD and IFC;

(ii) Asian Development Bank;

(iii) African Development Bank;

(iv) European Bank for Reconstruction and Development;

(v) Inter-American Development Bank;

(vi) European Investment Bank;

(vii) European Investment Fund;

(viii) Nordic Investment Bank;

(ix) Caribbean Development Bank;

(x) Islamic Development Bank;

(xi) Council of Europe Development Bank;

(xii) International Finance Facility for Immunization (IFFIM); and

(xiii) Asian Infrastructure Investment Bank (AIIB).

A.6 Claims on banks (exposure to capital instruments)

42. Investments of a bank in equity and capital instruments of other banks shall not be treated in terms of paragraph 28(8) above, but shall be risk-weighted as per Table 7 below, when they satisfy the following conditions:

(i) Investments in capital instruments of banks where the investing bank holds not more than 10 per cent of the issued common shares of the investee banks, subject to the following conditions:

(a) Aggregate of these investments, together with investments in the capital instruments in insurance and other financial entities, do not exceed 10 per cent of Common Equity of the investing bank; and

(b) The equity investment in the investee entities is outside the scope of regulatory consolidation.

(ii) Equity investments in other banks where the investing bank holds more than 10 per cent of the issued common shares of the investee banks, subject to the following conditions:

(a) Aggregate of these investments, together with such investments in insurance and other financial entities, do not exceed 10 per cent of Common Equity of the investing bank.

(b) The equity investment in the investee entities is outside the scope of regulatory consolidation.

Table 7: Claims on banks incorporated in India and foreign bank branches in India

	Risk Weights (%)					
	All Scheduled Banks (Commercial Banks, Regional Rural Banks, Local Area Banks and Co-operative Banks)			**All Non-Scheduled Banks (Commercial Banks, Regional Rural Banks, Local Area Banks and Co-operative Banks)**		
Level of CET1 including applicable CCB (%) of the investee bank under Basel III / Total capital of other banks (where applicable)	**Investments referred to in paragraph 42(i)**	**Investments referred to in paragraph 42(ii)**	**All other claims**	**Investments referred to in paragraph 42(i)**	**Investments referred to in paragraph 42(ii)**	**All other claims**
1	2	3	4	5	6	7
For banks which are under Basel III Capital Regulations						
Applicable Minimum CET1 + (Applicable CCB and above)	125 % or the risk weight as per the rating of the instrument or counterparty,	250	20	125% or the risk weight as per the rating of the instrument or counterparty,	300	100

	Risk Weights (%)					
	All Scheduled Banks (Commercial Banks, Regional Rural Banks, Local Area Banks and Co-operative Banks)			All Non-Scheduled Banks (Commercial Banks, Regional Rural Banks, Local Area Banks and Co-operative Banks)		
Level of CET1 including applicable CCB (%) of the investee bank under Basel III / Total capital of other banks (where applicable)	**Investments referred to in paragraph 42(i)**	**Investments referred to in paragraph 42(ii)**	**All other claims**	**Investments referred to in paragraph 42(i)**	**Investments referred to in paragraph 42(ii)**	**All other claims**
1	2	3	4	5	6	7
	whichever is higher			whichever is higher		
Applicable Minimum CET1 + (CCB = 75% and <100% of applicable CCB)	150	300	50	250	350	150
Applicable Minimum CET1 + (CCB = 50% and <75% of applicable CCB)	250	350	100	350	450	250
Applicable Minimum CET1 + (CCB = 0% and <50% of applicable CCB)	350	450	150	625	Full deduction*	350
Minimum CET1 less than applicable minimum	625	Full deduction*	625	Full deduction*	Full deduction*	625
For banks which are not under Basel III Capital Regulations						
9 and above	100 % or the risk weight as per the rating of the instrument or counterparty, or as applicable for Capital Market Exposure whichever is higher	250	20	100 % or the risk weight as per the rating of the instrument or counterparty, or as applicable for Capital Market Exposure whichever is higher	300	100
6 to < 9	150	300	50	250	350	150
3 to < 6	250	350	100	350	450	250

	Risk Weights (%)					
	All Scheduled Banks (Commercial Banks, Regional Rural Banks, Local Area Banks and Co-operative Banks)			All Non-Scheduled Banks (Commercial Banks, Regional Rural Banks, Local Area Banks and Co-operative Banks)		
Level of CET1 including applicable CCB (%) of the investee bank under Basel III / Total capital of other banks (where applicable)	**Investments referred to in paragraph 42(i)**	**Investments referred to in paragraph 42(ii)**	**All other claims**	**Investments referred to in paragraph 42(i)**	**Investments referred to in paragraph 42(ii)**	**All other claims**
1	2	3	4	5	6	7
0 to < 3	350	450	150	625	Full deduction*	350
Negative	625	Full deduction*	625	Full deduction*	Full deduction*	625

*The deduction should be made from CET1 capital

Note - For claims held in trading book, a bank shall refer the paragraphs 188 and 198 under 'capital charge for market risk'.

43. The claims on a foreign bank shall be risk weighted as under as per the ratings assigned by international rating agencies.

Table 8: Claims on foreign banks – risk weights

S&P / Fitch ratings	AAA to AA	A	BBB	BB to B	Below B	Unrated
Moody's ratings	Aaa to Aa	A	Baa	Ba to B	Below B	Unrated
Risk weight (%)	20	50	50	100	150	50

The exposures of the Indian branches of a foreign bank, guaranteed / counter-guaranteed by the overseas Head Offices or the bank's branch in another country shall amount to a claim on the parent foreign bank if exposure is reckoned as per prudential norms on the foreign bank's branch / Head Office and shall also attract the risk weights as per Table 8 above. If the bank reckons the exposure on the original counterparty, it shall attract the risk weight as per Tables 9.1 and 9.2, if the counterparty is a person resident in India, or 150 per cent if the counterparty is a person resident outside India.

44. However, the claims on a bank which are denominated in 'domestic' foreign currency met out of the resources in the same currency raised in that jurisdiction

shall be risk weighted at 20 per cent provided the bank complies with the minimum CRAR prescribed by the concerned bank regulator(s).

Explanation - For example, a Euro denominated claim of an Indian bank's branch in Paris on a European bank in Paris which is funded from out of the Euro denominated deposits of the Indian bank in Paris shall attract a 20 per cent risk weight irrespective of the rating of the claim, provided European bank complies with the minimum CRAR stipulated by its regulator / supervisor in France. If the European bank were breaching the minimum CRAR, the risk weight shall be as indicated in Table 7 above.

45. However, in case a Host Country Supervisor requires a more conservative treatment for such claims in the books of the foreign branches of the Indian banks, it shall adopt the requirements prescribed by the Host supervisor for computing capital adequacy.

A.7 Claims on primary dealers

46. Claims on primary dealers shall be risk weighted in a manner similar to claims on corporates.

A.8 Claims on corporates and non-banking financial companies (NBFCs)

47. Claims on corporates, and exposures to all NBFCs excluding core investment companies (CICs), shall be risk weighted as per the ratings assigned by the rating agencies registered with the SEBI and accredited by the Reserve Bank. Exposures to CICs, rated as well as unrated, shall be risk-weighted at 100 per cent. Tables 9.1 and 9.2 indicate the risk weight applicable to claims on corporates and exposures to all NBFCs, excluding CICs.

Explanation - Claims on corporates shall include all fund based and non-fund-based exposures other than those which qualify for inclusion under 'sovereign', 'bank', 'regulatory retail', 'residential mortgage', 'non-performing assets', specified category addressed separately in these guidelines.

Table 9.1: Long term claims on corporates and NBFCs excluding CICs - risk weights

Domestic rating agencies	AAA	AA	A	BBB	BB & below	Unrated
Risk weight (%)	20	30	50	100	150	100

Table 9.2: Short term claims on Corporates and NBFCs excluding CICs -risk weights

CARE	CRISIL Ratings Ltd.	India Ratings and Research Private Limited (India Ratings)	ICRA	Brickwork	Acuite Ratings & Research Limited (Acuite)	INFOMERICS Valuation and Rating Ltd.	(%)
CARE A1+	CRISIL A1+	IND A1+	ICRA A1+	Brickwork A1+	Acuite A1+	IVR A1+	20
CARE A1	CRISIL A1	IND A1	ICRA A1	Brickwork A1	Acuite A1	IVR A1	30
CARE A2	CRISIL A2	IND A2	ICRA A2	Brickwork A2	Acuite A2	IVR A2	50
CARE A3	CRISIL A3	IND A3	ICRA A3	Brickwork A3	Acuite A3	IVR A3	100
CARE A4 & D	CRISIL A4 & D	IND A4 & D	ICRA A4 & D	Brickwork A4 & D	Acuite A4 & D	IVR A4 and D	150
Unrated	Unrated	Unrated	Unrated	Unrated	Unrated	Unrated	100

Explanation –

(i) No claim on an unrated corporate shall be given a risk weight preferential to that assigned to its sovereign of incorporation.

(ii) Claims on corporates and NBFCs, except CICs, having aggregate exposure from banking system of more than ₹100 crore which were rated earlier and subsequently have become unrated shall attract a risk weight of 150 per cent.

(iii) All unrated claims on corporates and NBFCs, except CICs, having aggregate exposure from banking system of more than ₹200 crore shall attract a risk weight of 150 per cent.

48. The Reserve Bank may increase the standard risk weight for unrated claims where a higher risk weight is warranted by the overall default experience. As part of the supervisory review process, the Reserve Bank may also consider whether the credit quality of unrated corporate claims held by an individual bank should warrant a standard risk weight higher than 100 per cent.

49. The claims on non-resident corporates shall be risk weighted as under as per the ratings assigned by international rating agencies. Further, with regard to claims on non-resident corporates originating at International Financial Services Centre (IFSC) for which ratings are assigned by M/s CareEdge Global IFSC Limited, the mapping shall be as per Table 10.2 below.

Table 10.1: Claims on non-resident corporates - risk weight mapping for the ratings assigned by S&P/Fitch/Moody's Ratings

S&P / Fitch Ratings	AAA to AA	A	BBB to BB	Below BB	Unrated
Moody's ratings	Aaa to Aa	A	Baa to Ba	Below Ba	Unrated
Risk Weight (%)	20	50	100	150	100

Table 10.2: Claims on non-resident corporates - risk weights mapping for the ratings assigned by M/s CareEdge Global IFSC Limited - for claims originating at International Financial Services Centre (IFSC)

CareEdge Global IFSC Limited	**AAA**	**AA**	**A**	**BBB**	**BB & below**
Risk Weight (%)	20	30	50	100	150

Explanation –

(i) Unrated claims having aggregate exposure from banking system of more than ₹200 crore shall attract a risk weight of 150 per cent.

(ii) Claims with aggregate exposure from banking system of more than ₹100 crore which were rated earlier and subsequently have become unrated shall attract a risk weight of 150 per cent.

(iii) No claim on an unrated corporate shall be given a risk weight preferential to that assigned to its sovereign of incorporation.

A.9 Claims included in the regulatory retail portfolios

50. Claims (both fund-based and non-fund based) that meet all the four criteria listed in paragraph 52 shall be considered as retail claims for regulatory capital purposes and included in a regulatory retail portfolio. Claims included in this portfolio shall be assigned a risk-weight of 75 per cent, except as provided in paragraphs 63 to 68 for non-performing assets.

51. The following claims, both fund based, and non-fund based, shall be excluded from the regulatory retail portfolio:

(i) Exposures by way of investments in securities (such as bonds and equities), whether listed or not;

(ii) Mortgage Loans to the extent that they qualify for treatment as claims secured by residential property (refer paragraphs 55 to 59), or claims secured by commercial real estate (refer paragraphs 60 to 62);

(iii) Loans and advances to bank's own staff which are fully covered by superannuation benefits and / or mortgage of flat / house;

(iv) Consumer credit, including personal loans and credit card receivables;

(v) Capital market exposures; and

(vi) Alternate Investment Funds (AIFs).

52. The qualifying criteria for claims to be considered as regulatory retail claim for capital adequacy purpose are as under:

(i) Orientation criterion - The exposure (both fund-based and non-fund-based) is to an individual person or persons or to a small business; person under this clause shall mean any legal person capable of entering into contracts and would include but not be restricted to individual and HUF; small business would include partnership firm, trust, private limited companies, public limited companies, co-operative societies etc. Small business is one where the total average annual turnover is less than ₹50 crore. The turnover criterion shall be linked to the average of the last three years in the case of existing entities; projected turnover in the case of new entities; and both actual and projected turnover for entities which are yet to complete three years.

(ii) Product Criterion - The exposure (both fund-based and non-fund-based) takes the form of any of the following: revolving credits and lines of credit (including overdrafts), term loans and leases (e.g., instalment loans and leases, student and educational loans) and small business facilities and commitments.

(iii) Granularity Criterion - No aggregate exposure to one counterpart should exceed 0.2 per cent of the overall regulatory retail portfolio. 'Aggregate exposure' means gross amount (i.e., not taking any benefit for credit risk mitigation into account) of all forms of debt exposures (e.g., loans or commitments) that individually satisfy the three other criteria. In addition, 'one counterpart' means one or several entities that may be considered as a single beneficiary (e.g., in the case of a small business that is affiliated to another small business, the limit shall apply to the bank's aggregated exposure on both businesses). While a bank may appropriately use the

group exposure concept for computing aggregate exposures, it shall evolve adequate systems to ensure strict adherence with this criterion. NPAs under retail loans shall be excluded from the overall regulatory retail portfolio when assessing the granularity criterion for risk-weighting purposes.

(iv) Low value of individual exposures - The maximum aggregated retail exposure to one counterpart shall not exceed the absolute threshold limit of ₹7.5 crore.

Explanation –

Microfinance loans which are not in the nature of consumer credit and fulfil all the four criteria specified in paragraph 52, may be classified under regulatory retail portfolio, provided that a bank put in place appropriate policies and standard operating procedures to ensure fulfilment of the qualifying criteria.

53. For ascertaining compliance with the absolute threshold, exposure shall mean sanctioned limit or the actual outstanding, whichever is higher, for all fund based and non-fund-based facilities, including all forms of off-balance sheet exposures. In the case of term loans and EMI based facilities, where there is no scope for redrawing any portion of the sanctioned amounts, exposure shall mean the actual outstanding.

54. The Reserve Bank shall evaluate at periodic intervals the risk weight assigned to the retail portfolio with reference to the default experience for these exposures. As part of the supervisory review process, the Reserve Bank would also consider whether the credit quality of regulatory retail claims held by individual banks should warrant a standard risk weight higher than 75 per cent.

A.10 Claims secured by residential property

55. Lending to individuals meant for acquiring residential property which are fully secured by mortgages on the residential property that is or will be occupied by the borrower, or that is rented, shall be risk weighted as indicated at Tables 11, 12 and 13 below, based on Board approved valuation policy. Loan to value (LTV) ratio shall be computed as a percentage with total outstanding in the account (viz. ‘principal + accrued interest + other charges pertaining to the loan’ without

any netting) in the numerator and the realisable value of the residential property mortgaged to the bank in the denominator.

Table 11: Claims secured by residential property – risk weights for loans sanctioned up to June 06, 2017

Category of loan	LTV ratio (%)	Risk weight (%)
(a) Individual Housing Loans		
(i) Up to ₹30 lakh	≤80	35
	>80 and ≤90	50
(ii) Above ₹30 lakh and up to ₹75 lakh	≤75	35
	>75 and ≤80	50
(iii) Above ₹75 lakh	≤75	75
(b) Commercial real estate – residential housing (CRE-RH)	N A	75
(c) Commercial Real Estate (CRE)	N A	100

Table 12: Claims secured by residential property – risk weights for loans sanctioned on or after June 07, 2017

Category of Loan	LTV Ratio (%)	Risk Weight (%)
(a) Individual Housing Loans		
(i) Up to ₹30 lakh	≤80	35
	>80 and ≤90	50
(ii) Above ₹30 lakh and up to ₹75 lakh	≤80	35
(iii) Above ₹75 lakh	≤75	50
(b) CRE-RH	N A	75
(c) Commercial Real Estate (CRE)	N A	100

56. However, the following LTV ratios and risk weights shall apply to individual housing loans sanctioned on or after October 16, 2020 and up to March 31, 2023, irrespective of the loan amount.

Table 13: Claims secured by residential property – risk weights for loans sanctioned on or after October 16, 2020 and up to March 31, 2023

LTV Ratio (%)	Risk Weight (%)
≤ 80	35
> 80 and ≤ 90	50

Note -

(i) The LTV ratio shall not exceed the prescribed ceiling in all fresh cases of sanction. In case the LTV ratio is currently above the ceiling prescribed for any reasons, efforts shall be made to bring it within limits.

(ii) A bank's exposures to third dwelling unit onwards to an individual shall also be treated as CRE exposures for risk weight purpose.

(iii) For computing realisable value of the residential property for individual housing loans, a bank may refer to the guidelines on Housing Finance prescribed in MD on Credit Facilities.

57. All other claims secured by residential property shall attract the higher of the risk weight applicable to the counterparty or to the purpose for which the bank has extended finance.

58. Loans / exposures to intermediaries for on-lending shall not be eligible for inclusion under claims secured by residential property but shall be treated as claims on corporates or claims included in the regulatory retail portfolio as the case may be.

59. Investments in mortgage-backed securities (MBS) backed by exposures as at paragraph 55 above shall be governed by the directions in paragraphs 88 to 126.

A.11 Claims classified as commercial real estate exposure

60. Commercial real estate exposure (CRE) is described in the guidelines issued vide Reserve Bank of India (Commercial Banks – Credit Facilities) Directions, 2025.

61. CRE (RH) will attract a risk weight of 75 per cent as mentioned in Table 8.2 above. CRE other than CRE (RH) shall attract a risk weight of 100 per cent.

62. Investments in MBS backed by exposures as at paragraph 60 shall be governed by the directions in paragraphs 88 to 126.

A.12 Non-Performing Assets (NPAs)

63. The unsecured portion of NPA (other than a qualifying residential mortgage loan which is addressed in paragraph 68), net of specific provisions (including partial write-offs), shall be risk-weighted as follows:

(i) 150 per cent risk weight when specific provisions are less than 20 per cent of the outstanding amount of the NPA;

(ii) 100 per cent risk weight when specific provisions are at least 20 per cent of the outstanding amount of the NPA; and

(iii) 50 per cent risk weight when specific provisions are at least 50 per cent of the outstanding amount of the NPA.

64. For computing the level of specific provisions in NPAs for deciding the risk-weighting, all funded NPA exposures of a single counterparty (without netting the value of the eligible collateral) shall be reckoned in the denominator.

65. For defining the secured portion of the NPA, eligible collateral shall be the same as recognised for credit risk mitigation purposes (paragraph 161). Hence, other forms of collateral like land, buildings, plant, machinery, current assets shall not be reckoned while computing the secured portion of NPAs for capital adequacy purposes.

66. In addition to the above, where a NPA is fully secured by the following forms of collateral that are not recognised for credit risk mitigation purposes, either independently or along with other eligible collateral, a 100 per cent risk weight may apply, net of specific provisions, when provisions reach 15 per cent of the outstanding amount:

(i) Land and building which are valued by an expert valuer and where the valuation is not more than three years old, and

(ii) Plant and machinery in good working condition at a value not higher than the depreciated value as reflected in the audited balance sheet of the borrower, which is not older than eighteen months.

67. The above collaterals (mentioned in paragraph 66) shall be recognised only where the bank is having clear title to realise the sale proceeds thereof and can appropriate the same towards the amounts due to the bank. The bank's title to the collateral shall be well documented. These forms of collaterals are not recognised anywhere else under the standardised approach.

68. Claims secured by residential property, as defined in paragraph 55, which are NPA shall be risk weighted at 100 per cent net of specific provisions. If the specific provisions in such loans are at least 20 per cent but less than 50 per cent of the outstanding amount, the risk weight applicable to the loan net of specific provisions shall be 75 per cent. If the specific provisions are 50 per cent or more the applicable risk weight shall be 50 per cent.

A.13 Specified categories

69. Fund based and non-fund-based claims on Alternate Investment Funds, which are considered as high-risk exposures, shall attract a higher risk weight of 150 per cent.

70. The Reserve Bank may, in due course, decide to apply a 150 per cent or higher risk weight reflecting the higher risks associated with any other claim that may be identified as a high-risk exposure.

71. Consumer credit exposure, including personal loans, but excluding housing loans, education loans, vehicle loans and loans secured by gold and gold jewellery, shall attract a risk weight of 125 per cent. Microfinance loans that are in the nature of consumer credit and are not eligible for classification under regulatory retail under paragraphs 50 to 54 shall be risk weighted at 100 per cent. Credit card receivables shall attract a higher risk weight of 150 per cent or higher, if warranted by the external rating (or the lack of it) of the counterparty. As gold and gold jewellery are eligible financial collateral, the counterparty exposure in respect of personal loans secured by gold and gold jewellery shall be worked out under the comprehensive approach as per paragraph 160. The 'exposure value after risk mitigation' shall attract the risk weight of 125 per cent. All other consumer credit exposures shall attract a risk weight of 100 per cent, unless specified otherwise.

72. Advances classified as 'capital market exposures' shall attract a 125 per cent risk weight or risk weight warranted by external rating (or lack of it) of the counterparty, whichever is higher. These risk weights shall also be applicable to all banking book exposures, which are exempted from capital market exposure ceilings for direct investments / total capital market exposures.

    Explanation - The applicable risk weight for banking book exposure / capital charge for market risk exposure for a bank's equity investments in other banks / financial institutions etc. are covered under paragraphs 42, 188 and 198. These risk weights / capital charge shall also apply to exposures which are exempt from 'capital market exposure' limit.

73. The exposure to capital instruments issued by NBFCs which are not deducted and are required to be risk weighted in terms of paragraph 28(8)(ii)(b) shall be

risk weighted at 125 per cent or as per the external ratings, whichever is higher. The exposure to equity instruments issued by NBFCs which are not deducted and are required to be risk weighted in terms of paragraph 28(8)(ii)(c) shall be risk weighted at 250 per cent. The claims (other than in the form of capital instruments of investee companies) on all NBFCs excluding CIC shall be risk weighted as per the ratings assigned by the rating agencies registered with the SEBI and accredited by the Reserve Bank, in a manner similar to that of corporates. The claims on CICs, rated and unrated, shall be risk-weighted at 100 per cent.

74. All investments in the paid-up equity of non-financial entities (other than subsidiaries) which exceed 10 per cent of the issued common share capital of the issuing entity or where the entity is an unconsolidated affiliate as defined in paragraph 28(8)(ii)(c)(i) shall receive a risk weight of 1250 per cent. Equity investments equal to or below 10 per cent paid-up equity of such investee companies shall be assigned a 125 per cent risk weight or the risk weight as warranted by rating or lack of it, whichever higher.

Note - Equity investments in non-financial subsidiaries shall be deducted from the consolidated / solo bank capital as indicated in paragraphs 3.4.2 / 3.5.1.

75. The exposure to capital instruments issued by financial entities (other than banks and NBFCs) which are not deducted and are required to be risk weighted in terms of paragraph 28(8)(ii)(b) shall be risk weighted at 125 per cent or as per the external ratings whichever is higher. The exposure to equity instruments issued by financial entities (other than banks and NBFCs) which are not deducted and are required to be risk weighted in terms of paragraph 28(8)(ii)(c) shall be risk weighted at 250 per cent.

76. Bank's investments in the non-equity capital elißgible instruments of other banks should be risk weighted as prescribed in paragraph 42.

77. Unhedged foreign currency exposure

Table 14: Capital requirement for a bank's exposures to entities with unhedged foreign currency exposures (over and above the present capital requirements)

Potential Loss / EBID* (%)	Incremental Capital Requirement
Up to 75 per cent	0

More than 75 per cent	25 percentage point increase in the risk weight (for example, for an entity which otherwise attracts a risk weight of 50 per cent, the applicable risk weight would become 75 per cent.)

* EBID = Profit After Tax + Depreciation + Interest on debt + Lease Rentals, if any

Note - Please refer to Reserve Bank of India (Commercial Banks – Credit Risk Management) Directions, 2025.

78. Please refer to Reserve Bank of India (Commercial Banks – Concentration Risk Management) Directions, 2025 regarding enhancing credit supply for large borrowers through market mechanism, which inter alia mentions as under:

Additional Risk weight of 75 percentage points over and above the applicable risk weight for the exposure to the specified borrower shall apply on the incremental exposure of the banking system to a specified borrower beyond Normally permitted lending limit (NPLL). The resultant additional risk weighted exposure, in terms of RWA, shall be distributed in proportion to each bank's funded exposure to the specified borrower.

Explanation -

(i) 'Specified borrower' means a borrower having an Aggregate Sanctioned Credit Limit (ASCL) of more than ₹10,000 crore at any time from April 1, 2019 onwards.

(ii) **'**NPLL' means 50 per cent of the incremental funds raised by the specified borrower over and above its Aggregate Sanctioned Credit Limit as on the reference date, in the financial years (FYs) succeeding the FY in which the reference date falls. For this purpose, any funds raised by way of equity shall be deemed to be part of incremental funds raised by the specified borrower (from outside the banking system) in the given year; Provided that where a specified borrower has already raised funds by way of market instruments and the amount outstanding in respect of such instruments as on the reference date is 15 per cent or more of ASCL on that date, the NPLL shall mean 60 per cent of the incremental funds raised by the specified borrower over and above its ASCL as on the reference date, in the financial years (FYs) succeeding the FY in which the reference date falls.

(iii) 'ASCL' means the aggregate of the fund-based credit limits sanctioned or outstanding, whichever is higher, to a borrower by the banking system. ASCL would also include unlisted privately placed debt with the banking system.

A.14 Other Assets

79. Loans and advances to a bank's own staff which are fully covered by superannuation benefits and / or mortgage of flat / house shall attract a 20 per cent risk weight. Since flat / house is not an eligible collateral and since a bank normally recover the dues by adjusting the superannuation benefits only at the time of cessation from service, the concessional risk weight shall be applied without any adjustment of the outstanding amount. In case a bank is holding eligible collateral in respect of amounts due from a staff member, the outstanding amount in respect of that staff member shall be adjusted to the extent permissible, as indicated in paragraphs 157 to 165.

80. Other loans and advances to bank's own staff shall be eligible for inclusion under regulatory retail portfolio and shall therefore attract a 75 per cent risk weight.

81. All other assets shall attract a uniform risk weight of 100 per cent.

A.15 Off-balance sheet items

82. The total risk weighted off-balance sheet credit exposure shall be calculated as the sum of the risk-weighted amount of the market related and non-market related off-balance sheet items. The risk-weighted amount of an off-balance sheet item that gives rise to credit exposure shall be calculated by the following process:

(1) the notional amount of the transaction shall be converted into a credit equivalent amount, by multiplying the amount by the specified credit conversion factor (CCF) or by applying the current exposure method; and

(2) the resulting credit equivalent amount shall be multiplied by the risk weight applicable to the counterparty or to the purpose for which the bank has extended finance or the type of asset, whichever is higher.

83. Where the off-balance sheet item is secured by eligible collateral or guarantee, the credit risk mitigation directions detailed in paragraphs 154 to 181 shall be applied.

84. Non-market-related off-balance sheet items

(1) The credit equivalent amount in relation to a non-market related off-balance sheet item like direct credit substitutes, trade and performance related contingent items and commitments with certain drawdown, other commitments, etc. shall be determined by multiplying the contracted amount of that particular transaction by the relevant CCF as elaborated in Table 15.

(2) Where the non-market related off-balance sheet item is an undrawn or partially undrawn fund-based facility, the amount of undrawn commitment to be included in calculating the off-balance sheet non-market related credit exposures is the maximum unused portion of the commitment that could be drawn during the remaining period to maturity. Any drawn portion of a commitment forms a part of bank's on-balance sheet credit exposure.

Explanation –

(i) For example, in the case of a cash credit facility for ₹100 lakh (which is not unconditionally cancellable) where the drawn portion is ₹60 lakh, the undrawn portion of ₹40 lakh shall attract a CCF of 20 per cent (since the CC facility is subject to review / renewal normally once a year). The credit equivalent amount of ₹8 lakh (20 per cent of ₹40 lakh) shall be assigned the appropriate risk weight as applicable to the counterparty / rating to arrive at the risk weighted asset for the undrawn portion. The drawn portion (₹60 lakh) shall attract a risk weight as applicable to the counterparty / rating.

(ii) For example, a TL of ₹700 crore is sanctioned for a large project which can be drawn down in stages over a three-year period. The terms of sanction allow draw down in three stages - ₹150 crore in Stage I, ₹200 crore in Stage II and ₹350 cr in Stage III, where the borrower needs the bank’s explicit approval for draw down under Stages II and III after completion of certain formalities. If the borrower has drawn already ₹50 crore under Stage I, then the undrawn portion would be computed with reference to Stage I alone i.e., it will be ₹100 cr. If Stage I is scheduled to be completed within one year,

the CCF will be 20 per cent and if it is more than one year then the applicable CCF will be 50 per cent.

(3) In the case of irrevocable commitments to provide off-balance sheet facilities, the original maturity shall be measured from the commencement of the commitment until the time the associated facility expires. Such commitments should be assigned the lower of the two applicable CCFs.

Explanation –

(i) For example, an irrevocable commitment with an original maturity of 12 months, to issue a 6-month documentary letter of credit, is deemed to have an original maturity of 18 months.

(ii) For example, an irrevocable commitment with an original maturity of 15 months (50 per cent - CCF) to issue a six-month documentary letter of credit (20 per cent - CCF) shall attract the lower of the CCF i.e., the CCF applicable to the documentary letter of credit viz. 20 per cent.

(4) The CCFs for non-market related off-balance sheet transactions are as under:

Table 15: CCF - non-market related off-balance sheet items

Sr. No.	Instruments	CCF (%)
1.	Direct credit substitutes e.g., general guarantees of indebtedness (including standby L / Cs serving as financial guarantees for loans and securities, credit enhancements, liquidity facilities for securitisation transactions), and acceptances (including endorsements with the character of acceptance). (i.e., the risk of loss depends on the credit worthiness of the counterparty or the party against whom a potential claim is acquired)	100
2.	Certain transaction-related contingent items (e.g., performance bonds, bid bonds, warranties, indemnities and standby letters of credit related to particular transaction).	50
3.	Short-term self-liquidating trade letters of credit arising from the movement of goods (e.g., documentary credits collateralised by the underlying shipment) for both issuing bank and confirming bank.	20
4.	Sale and repurchase agreement and asset sales with recourse, where the credit risk remains with the bank.	100

Sr. No.	Instruments	CCF (%)
	(These items are to be risk weighted according to the type of asset and not according to the type of counterparty with whom the transaction has been entered into.)	
5.	Forward asset purchases, forward deposits and partly paid shares and securities, which represent commitments with certain drawdown. (These items are to be risk weighted according to the type of asset and not according to the type of counterparty with whom the transaction has been entered into.)	100
6	Lending of banks' securities or posting of securities as collateral by banks, including instances where these arise out of repo style transactions (i.e., repurchase / reverse repurchase and securities lending / securities borrowing transactions)	100
7.	Note issuance facilities and revolving / non-revolving underwriting facilities.	50
8	Commitments with certain drawdown	100
9.	Other commitments (e.g., formal standby facilities and credit lines) with an original maturity of a) up to one year b) over one year Similar commitments that are unconditionally cancellable at any time by the bank without prior notice or that effectively provide for automatic cancellation due to deterioration in a borrower's credit worthiness.*	 20 50 0
10.	Take-out Finance in the books of taking-over institution	
	(i) Unconditional take-out finance	100
	(ii) Conditional take-out finance	50

*However, this shall be subject to a bank demonstrating that it is actually able to cancel any undrawn commitments in case of deterioration in a borrower's credit worthiness failing which the credit conversion factor applicable to such facilities which are not cancellable shall apply. The bank's compliance to these guidelines shall be assessed under Supervisory Review and Evaluation Process under Pillar 2 of the Reserve Bank. Borrowers having aggregate fund based working capital limit of ₹150 crore and above from the banking system, the undrawn portion of cash credit / overdraft limits sanctioned, irrespective of whether unconditionally cancellable or not, shall attract a CCF of 20 per cent.

(5) Regarding non-market related off-balance sheet items, the following transactions with non-bank counterparties shall be treated as claims on banks:

(i) Guarantees issued by the bank against the counter guarantees of other banks.

(ii) Rediscounting of documentary bills discounted by other banks and bills discounted by the bank which have been accepted by another bank shall be treated as a funded claim on a bank.

In all the above cases a bank should be fully satisfied that the risk exposure is in fact on the other bank. If it is satisfied that the exposure is on the other bank, it shall assign these exposures the risk weight applicable to banks as detailed in paragraphs 42 to 45.

(6) Issue of irrevocable payment commitment by a bank to various stock exchanges on behalf of Mutual Funds and foreign institutional investors (FIIs) is a financial guarantee with a CCF of 100 per cent. However, capital shall be maintained only on exposure, which is reckoned as CME, i.e., 30 per cent of the settlement amount under T+1 settlement cycle, because the rest of the exposure is deemed to have been covered by cash / securities which are admissible risk mitigants as per capital adequacy framework. Thus, capital is to be maintained on the amount taken for CME and the risk weight shall be 125 per cent thereon. Under T+2 settlement cycle, the CME shall be reckoned at 50 per cent of the settlement amount.

(7) For classification of bank guarantees viz. direct credit substitutes and transaction-related contingent items etc. (Sr. No. 1 and 2 of Table 15 above), the following principles shall be followed for the application of CCFs:

(i) Financial guarantees are direct credit substitutes wherein a bank irrevocably undertakes to guarantee the repayment of a contractual financial obligation. Financial guarantees essentially carry the same credit risk as a direct extension of credit i.e., the risk of loss is directly linked to the creditworthiness of the counterparty against whom a potential claim is acquired. An indicative list of financial guarantees, attracting a CCF of 100 per cent is as under:

(a) Guarantees for credit facilities;

(b) Guarantees in lieu of repayment of financial securities;

(c) Guarantees in lieu of margin requirements of exchanges;

(d) Guarantees for mobilisation advance, advance money before the commencement of a project and for money to be received in various stages of project implementation;

(e) Guarantees towards revenue dues, taxes, duties, levies etc. in favour of Tax / Customs / Port / Excise Authorities and for disputed liabilities for litigation pending at courts;

(f) Credit enhancements;

(g) Liquidity facilities for securitisation transactions;

(h) Acceptances (including endorsements with the character of acceptance); and

(i) Deferred payment guarantees.

(ii) Performance guarantees are essentially transaction-related contingencies that involve an irrevocable undertaking to pay a third party in the event the counterparty fails to fulfil or perform a contractual non-financial obligation. In such transactions, the risk of loss depends on the event which need not necessarily be related to the creditworthiness of the counterparty involved. An indicative list of performance guarantees, attracting a CCF of 50 per cent is as under:

(a) Bid bonds;

(b) Performance bonds and export performance guarantees;

(c) Guarantees in lieu of security deposits / earnest money deposits (EMD) for participating in tenders;

(d) Retention money guarantees; and

(e) Warranties, indemnities and standby letters of credit related to particular transaction.

(8) Partial Credit Enhancement (PCE) facilities to the extent drawn should be treated as an advance in the balance sheet. Undrawn facilities would be an off-balance sheet item and reported under ‘Contingent Liability – Others’. The capital required to be maintained by the RE providing PCE for a given bond issue shall

be based on the PCE amount and the applicable risk weight for the RE corresponding to the pre- enhanced rating of the bond.

(i) To illustrate, in the case of a SCB, assume that the total bond size is ₹100 and pre-enhanced rating of the bond is BBB. In this scenario, the applicable risk weight at the pre-enhanced rating of BBB is 100%.

(ii) The capital requirement (assuming CRAR of 9%) for varying amount of PCE, would, therefore be:

PCE Amount (₹)	**Capital Requirement for PCE provider (₹)**
20	1.8 (20*100%*9%)
30	2.7 (30*100%*9%)
40	3.6 (40*100%*9%)
50	4.5 (50*100%*9%)

For the purpose of capital computation in the books of PCE provider, lower of the two pre-enhanced credit ratings shall be reckoned.

(iii) It is possible that the credit rating of the bond changes during the lifetime of the bond, necessitating a change in the capital requirement. Therefore, the rating of the bond shall be monitored regularly, and capital requirement adjusted in the following manner:

(a) In case of change in the pre-enhanced rating of the bond, the capital required shall be recalculated based on the risk weight applicable to revised pre-enhanced rating, subject to a floor, i.e., the capital requirement on the PCE at the time of issuance of the PCE enhanced bonds.

(b) As long as the bond outstanding amount exceeds the aggregate PCE (drawn and contingent non-funded) offered, the capital held shall not be less than the amount required to be held at the time of issuance of the PCE enhanced bond. However, once the bond outstanding has amortised below the aggregate PCE amount, the capital can be computed taking into account the outstanding bond amount.

(c) In situations where the pre-enhanced rating of the bond slips below investment grade (BBB minus), full capital to the extent of PCE provided shall be maintained by all banks.

In all circumstances, the capital computed for PCE as mentioned above and required to be maintained by the PCE provider, shall be capped by the total amount of PCE provided.

85. Treatment of total counterparty credit risk

(1) The total capital charge for counterparty credit risk shall cover the default risk as well as credit migration risk of the counterparty reflected in mark-to-market losses on the expected counterparty risk (such losses being known as credit value adjustments or CVA). Counterparty risk may arise in the context of OTC derivatives, exchange traded derivatives, and SFTs.

Explanation –

Instruments that give rise to counterparty risk generally exhibit the following abstract characteristics.

(i) The transactions generate a current exposure or market value.

(ii) The transactions have an associated random future market value based on market variables.

(iii) The transactions generate an exchange of payments or an exchange of a financial instrument against payment.

(iv) Collateral may be used to mitigate risk exposure and is inherent in the nature of some transactions.

(v) Short-term financing may be a primary objective in that the transactions mostly consist of an exchange of one asset for another (cash or securities) for a relatively short period of time, usually for the business purpose of financing. The two sides of the transactions are not the result of separate decisions but form an indivisible whole to accomplish a defined objective.

(vi) Netting may be used to mitigate the risk.

(vii) Positions are frequently valued (most commonly on a daily basis), according to market variables.

(viii) Remargining may be employed.

The ‘capital charge for default risk’ shall be calculated using **Current Exposure Method** as explained in paragraph 85(2). The ‘capital charge for CVA risk’ shall be calculated as explained in paragraph 85(3). The Current Exposure method is applicable only to OTC derivatives. The counterparty risk on account of

Securities Financing Transactions is covered in paragraph 164 of these Directions.

(2) Default risk capital charge for counterparty credit risk (CCR)

The exposure amount for the purpose of computing default risk capital charge for CCR shall be calculated using the Current Exposure Method (CEM) described as under:

(i) The credit equivalent amount of a market related off-balance sheet transaction calculated using the current exposure method is the sum of current credit exposure and potential future credit exposure of these contracts. For this purpose, credit equivalent amount shall be adjusted for legally valid eligible financial collaterals in accordance with the provisions of paragraphs 157 to 165 – Credit Risk Mitigation Techniques – collateralised transactions, and the provisions held by the bank for CVA losses.

(ii) The CVA loss shall be calculated as a prudent valuation adjustment as per prudent valuation guidance contained in paragraph 213, without taking into account any offsetting debit valuation adjustments (DVA) which have been deducted from capital (please see paragraph 28(5)). The CVA loss deducted from exposures to determine outstanding EAD is the CVA loss gross of all DVA which have been separately deducted from capital. To the extent DVA has not been separately deducted from a bank's capital, the CVA loss used to determine outstanding EAD shall be net of such DVA. Risk Weighted Assets for a given OTC derivative counterparty shall be calculated as the applicable risk weight under the Standardised Approach multiplied by the outstanding EAD of the counterparty. This reduction of EAD by CVA losses does not apply to the determination of the CVA risk capital charge as per formula given in paragraph 85(3)(ii).

(iii) While computing the credit exposure, banks may exclude 'sold options' that are outside netting and margin agreements, provided the entire premium / fee or any other form of income is received / realised. For 'sold options' (outside netting and margin agreements) where the premium / fee or any

other form of income is not fully received / realised, the add-on shall be capped to the amount of unpaid premia.

(iv) Current credit exposure is the sum of the positive mark-to-market value of these contracts. The Current Exposure Method requires periodical calculation of the current credit exposure by marking these contracts to market, thus capturing the current credit exposure.

(v) Potential future credit exposure shall be determined by multiplying the notional principal amount of each of these contracts irrespective of whether the contract has a zero, positive, or negative mark-to-market value by the relevant add-on factor indicated below according to the nature and residual maturity of the instrument.

Table 16: Add-on factors for market-related off-balance sheet items (see paragraph 204 for CDS exposures)

	Add-on factor (%)	
	Interest Rate Contracts	**Exchange Rate Contracts and Gold**
One year or less	0.50	2.00
Over one year to five years	1.00	10.00
Over five years	3.00	15.00

Note -

(a) For contracts with multiple exchanges of principal, the add-on factors shall be multiplied by the number of remaining payments in the contract.

(b) For contracts that are structured to settle outstanding exposure following specified payment dates and where the terms are reset such that the market value of the contract is zero on these specified dates, the residual maturity shall be set equal to the time until the next reset date. However, in the case of interest rate contracts which have residual maturities of more than one year and meet the above criteria, the add-on factor shall be subject to a floor of 1.0 per cent.

(c) No potential future credit exposure shall be calculated for single currency floating / floating interest rate swaps. The credit exposure on

these contracts shall be evaluated solely on the basis of their mark-to-market value.

(d) Potential future exposures shall be based on 'effective' rather than 'apparent notional amounts'. In the event that the 'stated notional amount' is leveraged or enhanced by the structure of the transaction, a bank shall use the 'effective notional amount' when determining potential future exposure. For example, a stated notional amount of USD 1 million with payments based on an internal rate of two times the BPLR / Base Rate shall have an effective notional amount of USD 2 million.

(vi) When effective bilateral netting contracts as specified in paragraph 87 are in place, RC shall be the net replacement cost and the add-on shall be A_{Net} as calculated below:

(a) Credit exposure on bilaterally netted forward transactions shall be calculated as the sum of the net mark-to-market replacement cost, if positive, plus an add-on based on the notional underlying principal. The add-on for netted transactions (A_{Net}) shall equal the weighted average of the gross add-on (A_{Gross}) and the gross add-on adjusted by the ratio of net current replacement cost to gross current replacement cost (NGR). This is expressed through the following formula:

$$A_{Net} = 0.4 * A_{Gross} + 0.6 * NGR \cdot A_{Gross}$$

where:

NGR = level of net replacement cost / level of gross replacement cost for transactions subject to legally enforceable netting agreements. A bank shall calculate NGR on a counterparty by counterparty basis for all transactions that are subject to legally enforceable netting agreements.

A_{Gross} = sum of individual add-on amounts (calculated by multiplying the notional principal amount by the appropriate add-on factors set out in Table 15 and the tables in paragraph 204)

of all transactions subject to legally enforceable netting agreements with one counterparty.

(b) For calculating potential future credit exposure to a netting counterparty for forward foreign exchange contracts and other similar contracts in which the notional principal amount is equivalent to cash flows, the notional principal shall be the net receipts falling due on each value date in each currency. The reason for this is that offsetting contracts in the same currency maturing on the same date will have lower potential future exposure as well as lower current exposure.

(c) **Explanations regarding Bilateral Netting under Current Exposure Method-**

(i) To avail the benefit of bilateral netting for computation of regulatory capital requirement for derivative transactions, a bank shall have an effective bilateral netting contract or agreement with each counterparty, as specified in paragraph 87.

(ii) Bilateral Netting as per this paragraph, shall be applicable for all OTC derivative exposures to a counterparty, arising from the netting set covered by a qualifying bilateral netting agreement, subject to meeting the criterion prescribed for effective bilateral netting contracts as specified in paragraph 87.

(iii) For such exposures as at (ii) above, Replacement Cost shall be Net Replacement Cost and Potential Future Exposure shall be A_{Net}. A_{Net} shall be calculated using gross add-on (A_{Gross}) and NGR. Gross add-on (A_{Gross}), in turn, shall be calculated as sum of individual add-on amounts (add-on factor multiplied by notional principal amount).

(iv) However, while calculating add-on amounts in case of forward foreign exchange contracts or other similar contracts where notional principal amount is equivalent to cash flows, the notional principal amount shall be taken as the net receipts falling due on each value date in each currency.

(v) The term 'product categories' in the definition of cross-product netting refers to (a) OTC derivative transactions and (b) repo / reverse repo. Cross-Product Netting is not permitted for capital adequacy as well as leverage ratio measure. Thus, all eligible OTC derivative transactions with a counterparty shall form part of one netting set and all eligible OTC repo / reverse repo transactions with that counterparty shall form part of a separate netting set.

(vi) Within a netting set, trades with a counterparty across maturities shall be netted and the risk-weight corresponding to the worst applicable long-term rating of the counterparty shall be applied. Under the same principle, for calculation of incurred CVA losses, credit spread pertaining to long-term issuer rating shall be used.

Collateral can be netted against both replacement cost and PFE for capital adequacy purposes. While computing for leverage ratio exposure measure, as provided in paragraph 267, collateral cannot be netted against derivative exposure (RC and PFE). However, cash variation margin can be used to reduce replacement cost portion of the leverage ratio exposure measure, but not the PFE subject to conditions provided in paragraph 267. The exposure computation under the Large Exposure Framework shall be as per Reserve Bank of India (Commercial Banks – Concentration Risk Management) Directions, 2025. Regarding presentation in the financial statements, a bank may refer to Guidance Note on Accounting for Derivative Contracts (Revised 2021) issued by the Institute of Chartered Accountants of India (ICAI). The Guidance Note (Para 64) mandates that all amounts presented in the financial statements should be gross amounts.

(vii) The provisioning requirement for standard assets shall be applicable on the credit exposures arising from derivative contracts. For this purpose, credit exposure of derivative contracts shall be computed as per these Directions.

Accordingly, for a netting set, standard asset provisions on derivative exposures shall be computed based on net replacement cost instead of current marked to market value of the contract (i.e., replacement cost), subject to compliance with the conditions prescribed for 'effective bilateral netting contracts' in paragraph 87.

(viii) The Current Exposure Method, as provided in these Directions, shall be applicable for measurement of credit exposure of derivatives products for the purpose of Reserve Bank of India (Commercial Banks – Concentration Risk Management) Directions, 2025.

(3) CVA risk capital charge

(i) The banks are also required to compute an additional capital charge towards CVA to cover the risk of mark-to-market losses on the expected counterparty risk to OTC derivatives. The CVA capital charge shall be calculated in the manner indicated below. A bank is not required to include in this capital charge (a) transactions with a CCP; and (b) securities financing transactions (SFTs).

(ii) A bank shall use the following formula to calculate a portfolio capital charge for CVA risk for its counterparties:

$$K = 2.33 \cdot \sqrt{h} \cdot \sqrt{\left(\sum_i 0.5 \cdot w_i \cdot \left(M_i \cdot EAD_i^{total} - M_i^{hedge} B_i \right) - \sum_{ind} w_{ind} \cdot M_{ind} \cdot B_{ind} \right)^2 + \sum_i 0.75 \cdot w_i^2 \cdot \left(M_i \cdot EAD_i^{total} - M_i^{hedge} B_i \right)^2}$$

Where;

(a) **h** is the one-year risk horizon (in units of a year), h = 1.

(b) $\mathbf{w_i}$ is the weight applicable to counterparty 'i'. Counterparty 'i' shall be mapped to one of the seven weights $\mathbf{w_i}$ based on its external rating, as shown in Tables 17.1 and 17.2 below.

(c) $\mathbf{EAD}_i^{total}$ is the exposure at default of counterparty 'i' (summed across its netting sets) including the effect of collateral as per the existing CEM as applicable to the calculation of counterparty risk capital

charges for such counterparty by the bank. The exposure shall be discounted by applying the factor (1-exp(-0.05*M_i)) / (0.05*M_i).

(d) **B_i** is the notional of purchased single name CDS hedges (summed if more than one position) referencing counterparty 'i' and used to hedge CVA risk. This notional amount shall be discounted by applying the factor (1-exp(-0.05*M_i^{hedge})) / (0.05* M_i^{hedge}).

(e) **B_{ind}** is the full notional of one or more index CDS of purchased protection, used to hedge CVA risk. This notional amount shall be discounted by applying the factor (1-exp(-0.05*M_{ind})) / (0.05* M_{ind}).

(f) **w_{ind}** is the weight applicable to index hedges. The bank shall map indices to one of the seven weights w_i based on the average spread of index 'ind'.

(g) **M_i** is the effective maturity of the transactions with counterparty 'i'. **M_i** is the notional weighted average maturity of all the contracts with counterparty 'i'.

(h) **M_i^{hedge}** is the maturity of the hedge instrument with notional B_i (the quantities Mi^{hedge}. Bi are to be summed if these are several positions).

(i) **M_{ind}** is the maturity of the index hedge 'ind'. In case of more than one index hedge position, it is the notional weighted average maturity.

(j) For any counterparty that is also a constituent of an index on which a CDS is used for hedging counterparty credit risk, the notional amount attributable to that single name (as per its reference entity weight) shall be subtracted from the index CDS notional amount and treated as a single name hedge (B_i) of the individual counterparty with maturity based on the maturity of the index.

(k) The weights, based on the external rating of the counterparty, are given in the Table below:

Table 17.1: Weights (w_i) based on external credit rating

Rating	W_i
AAA	0.7%
AA	0.7%

Rating	W_i
A	0.8%
BBB	1.0%
BB	2.0%
B and unrated	3.0%
CCC	10.0%

(l) In cases where the unrated counterparty is a scheduled commercial bank (SCB), a bank shall use the following Table to arrive at the implied ratings of the counterparty-bank and consequently, the W_i.

Table 17.2: Implied ratings and weights (w_i) based where the unrated counterparty is a SCB

Applicable Risk weight of the Counterparty-bank according to Table 7	Implied ratings	W_i
20	AAA / AA	0.7%
50	A	0.8%
100	BBB	1%
150	BB	2%
625	CCC	10%

(m) A bank shall continuously monitor the capital adequacy position of its counterparty banks so that the effect of any change in the implied ratings is adequately reflected in CVA capital charge calculations.

Illustration of calculation of CVA risk capital charge

(Figures in ₹ crore)

Derivatives	Counter party	Notional principal of trades whose MTM is negative	Notional principal of trades whose MTM is positive	Total Notional Principal (column 3+4)	Weighted average residual maturity	Positive MTM value of trades (column 4)	PFE	Total current credit exposure as per CEM	External rating of counter party
1	**2**	**3**	**4**	**5**	**6**	**7**	**8**	**9**	**10**
Interest rate swaps	A	150	150	300	1.85 years	1.5	1%	4.5	A (risk weight 50%)
Currency swaps	B	300	200	500	5.01 years	2.8	10%	52.8	AAA

									(risk weight 20%)

Formula to be used for calculation of capital charge for CVA risk:

$$K = 2.33 \cdot \sqrt{h} \cdot \sqrt{\left(\sum_i 0.5 \cdot w_i \cdot \left(M_i \cdot EAD_i^{total} - M_i^{hedge} B_i \right) - \sum_{ind} w_{ind} \cdot M_{ind} \cdot B_{ind} \right)^2 + \sum_i 0.75 \cdot w_i^2 \cdot \left(M_i \cdot EAD_i^{total} - M_i^{hedge} B_i \right)^2}$$

Where:

(i) B_i is the notional of purchased single name CDS hedges - nil;

(iii) B_{ind} is the full notional of one or more index CDS of purchased protection, used to hedge CVA risk – nil;

(iv) w_{ind} is the weight applicable to index hedges – nil;

(v) M_i^{hedge} is the maturity of the hedge instrument with notional Bi;

(vi) M_i is the effective maturity of the transactions with counterparty 'i';

(vii) EAD_i total is the exposure at default of counterparty 'i' (summed across its netting sets). For non-IMM banks the exposure shall be discounted by applying the factor: $(1-\exp(-0.05*M_i)) / (0.05*M_i)$; and

(viii) h = 1 year.

Assumptions:

(a) Applicable coupon rate on both legs of swap with exchange of coupon at yearly intervals for swap with counterparty A = 6% p.a.

(b) Applicable coupon rate on both legs of swap with exchange of coupon at yearly intervals for swap with counterparty = 7% p.a.

Calculation:

Discount factor to be applied to counterparty A: $(1-\exp(-0.05*M_A)) / (0.05*M_A)$ = 0.95551

Discounted EAD_A = 4.5*0.95551=4.2981

Discount factor to be applied to counterparty B: $(1-\exp(-0.05*M_B)) / (0.05*M_B)$ =0.8846

Discounted EAD_B = 52.8*0.8846=46.7061

K= 2.33*1*[{(0.5*.008*(1.85*4.2981-0) + (0.5*0.007*(5.01*46.7061-0))-0}2+

(0.75*0.0082*(1.85*4.2981-0)2 + (0.75*0.0072*(5.01*46.7061-0)2]1 / 2

= 2.33*1.66 = 3.86

Therefore, total capital charge for CVA risk on portfolio basis = ₹3.86 crore

(4) Calculation of the aggregate CCR and CVA risk capital charges

The total CCR capital charge for the bank shall be determined as the sum of the following two components:

(i) The sum over all counterparties of the CEM based capital charge determined as per paragraph 85(2); and

(ii) The standardised CVA risk capital charge determined as per paragraph 85(3).

(5) Capital requirement for exposures to CCPs

Scope of application

(i) Exposures to CCPs arising from OTC derivatives transactions, exchange traded derivatives transactions and SFTs shall be subject to the counterparty credit risk treatment as indicated in the paragraphs below.

(ii) Exposures arising from the settlement of cash transactions (equities, fixed income, spot FX, commodity etc.) shall not be subject to this treatment. The settlement of cash transactions shall be as per the treatment described in paragraph 86.

(iii) When the clearing member-to-client leg of an exchange traded derivatives transaction is conducted under a bilateral agreement, both the client bank

and the clearing member shall capitalise that transaction as an OTC derivative.

(iv) For the purpose of capital adequacy framework, CCPs shall be considered a financial institution. Accordingly, a bank's investments in the capital of CCPs shall be treated in terms of paragraph 28.

(v) Capital requirements shall be dependent on the nature of a CCP i.e., whether it is a QCCP or a non-Qualifying CCP.

(a) Regardless of whether a CCP is classified as a QCCP or not, a bank shall maintain adequate capital for its exposures. Under Pillar 2, a bank shall consider whether it might need to hold capital in excess of the minimum capital requirements if, for example, (i) its dealings with a CCP give rise to more risky exposures or (ii) where, given the context of that bank's dealings, it is unclear that the CCP meets the definition of a QCCP.

(b) A bank may be required to hold additional capital against its exposures to QCCPs via Pillar 2, if in the opinion of the Reserve Bank, it is necessary to do so.

(c) Where the bank is acting as a clearing member, the bank shall assess through appropriate scenario analysis and stress testing whether the level of capital held against exposures to a CCP adequately addresses the inherent risks of those transactions. This assessment shall include potential future or contingent exposures resulting from future drawings on default fund commitments, and / or from secondary commitments to take over or replace offsetting transactions from clients of another clearing member in case of this clearing member defaulting or becoming insolvent.

(d) A bank shall monitor and report to senior management and the appropriate committee of the Board (e.g., Risk Management Committee) on a regular basis (quarterly or at more frequent intervals) all of its exposures to CCPs, including exposures arising from trading

through a CCP and exposures arising from CCP membership obligations such as default fund contributions.

(e) Unless the Department of Regulation, Reserve Bank requires otherwise, the trades with a former QCCP may continue to be capitalised as though they are with a QCCP for a period not exceeding three months from the date it ceases to qualify as a QCCP. After that time, the bank's exposures with such a central counterparty shall be capitalised according to rules applicable for non-QCCP.

(6) Exposures to QCCPs

(i) Trade exposures

Clearing member exposures to QCCPs

(a) Where a bank acts as a clearing member of a QCCP for its own purposes, a risk weight of 2 per cent shall be applied to the bank's trade exposure to the QCCP in respect of OTC derivatives transactions, exchange traded derivatives transactions and SFTs.

(b) The exposure amount for such trade exposure shall be calculated in accordance with the Current Exposure Method for derivatives and rules as applicable for capital adequacy for repo / reverse repo-style transactions (please refer to paragraph 164).

(c) Where settlement is legally enforceable on a net basis in an event of default and regardless of whether the counterparty is insolvent or bankrupt, the total replacement cost of all contracts relevant to the trade exposure determination shall be calculated as a net replacement cost if the applicable close-out netting sets meet the requirements set out in paragraph 87 of these guidelines.

Note - The trade exposure (i.e., both replacement cost and potential future exposure) shall be computed on net basis, provided other conditions stated in this paragraph 85(6) are met.

(d) A bank shall demonstrate that the conditions mentioned in Paragraph 87 are fulfilled on a regular basis by obtaining independent and reasoned legal opinion as regards legal certainty of netting of

exposures to QCCPs. A bank shall also obtain from the QCCPs, the legal opinion taken by the respective QCCPs on the legal certainty of their major activities such as settlement finality, netting, collateral arrangements (including margin arrangements), default procedures etc.

Clearing member exposures to clients

(e) The clearing member shall always capitalise its exposure (including potential CVA risk exposure) to clients as bilateral trades, irrespective of whether the clearing member guarantees the trade or acts as an intermediary between the client and the QCCP. However, to recognise the shorter close-out period for cleared transactions, a clearing member may capitalise the exposure to its clients by multiplying the EAD by a scalar which is not less than 0.71.

Client bank exposures to clearing member

(f) Where a bank is a client of the clearing member, and enters into a transaction with the clearing member acting as a financial intermediary (i.e., the clearing member completes an offsetting transaction with a QCCP), the client's exposures to the clearing member shall receive the treatment applicable to a clearing member's exposure to QCCPs (as described in the foregoing provisions, as mentioned in this paragraph 85(6)), if following conditions are met:

(i) The offsetting transactions are identified by the QCCP as client transactions and collateral to support them is held by the QCCP

and / or the clearing member, as applicable, under arrangements that prevent any losses to the client due to:

(a) the default or insolvency of the clearing member;

(b) the default or insolvency of the clearing member's other clients; and

(c) the joint default or insolvency of the clearing member and any of its other clients.

(ii) The client bank shall obtain an independent, written and reasoned legal opinion which concludes that, in the event of legal challenge, the relevant courts and administrative authorities would find that the client would bear no losses on account of the insolvency of an intermediary under the relevant law, including:

(a) the law(s) applicable to client bank, clearing member and QCCP;

(b) the law of the jurisdiction(s) of the foreign countries in which the client bank, clearing member or QCCP are located;

(c) the law that governs the individual transactions and collateral; and

(d) the law that governs any contract or agreement necessary to meet the condition (a).

(iii) Relevant laws, regulations, rules, contractual, or administrative arrangements provide that the offsetting transactions with the defaulted or insolvent clearing member are highly likely to continue to be indirectly transacted through the QCCP, or by the QCCP, should the clearing member default or become insolvent. In such circumstances, the client positions and collateral with the QCCP shall be transferred at the market value unless the client requests to close out the position at the market value. If relevant laws, regulations, rules, contractual or administrative agreements provide that trades are highly likely to be ported, this

condition shall be considered to be met. If there is a clear precedent for transactions being ported at a QCCP and intention of the participants is to continue this practice, then these factors shall be considered while assessing if trades are highly likely to be ported. The fact that QCCP documentation does not prohibit client trades from being ported shall not be sufficient to conclude that they are highly likely to be ported. Other evidence such as the criteria mentioned in this paragraph 85(6) is necessary to make this claim.

(g) Where a client is not protected from losses in the case that the clearing member and another client of the clearing member jointly default or become jointly insolvent, but all other conditions mentioned above are met and the concerned CCP is a QCCP, a risk weight of 4 per cent shall apply to the client's exposure to the clearing member.

(h) Where the client bank does not meet the requirements in the above paragraphs, the bank shall be required to capitalise its exposure (including potential CVA risk exposure) to the clearing member as a bilateral trade.

(i) Under situations in which a client enters into a transaction with the QCCP with a clearing member guaranteeing its performance, the capital requirements shall be based on the provisions, as mentioned in this paragraph 85(6).

Treatment of posted collateral

(j) In all cases, any assets or collateral posted shall, from the perspective of the bank posting such collateral, receive the risk weights that otherwise applies to such assets or collateral under the capital adequacy framework, regardless of the fact that such assets have been posted as collateral. Collateral posted from banking book shall receive banking book treatment and collateral posted from trading book shall receive trading book treatment. Where assets or collateral of a clearing member or client are posted with a QCCP or a clearing member and are not held in a bankruptcy remote manner, the bank

posting such assets or collateral shall also recognise credit risk based upon the assets or collateral being exposed to risk of loss based upon the creditworthiness of the entity holding such assets or collateral.

Provided that, where the entity holding such assets or collateral is the QCCP, a risk-weight of 2 per cent applies to collateral included in the definition of trade exposures. The relevant risk-weight of the QCCP shall apply to assets or collateral posted for other purposes.

(k) Collateral posted by the clearing member (including cash, securities, other pledged assets, and excess initial or variation margin, also called over-collateralisation), that is held by a custodian, and is bankruptcy remote from the QCCP, is not subject to a capital requirement for counterparty credit risk exposure to such bankruptcy remote custodian.

Explanation - The word ‘custodian’ may include a trustee, agent, pledgee, secured creditor or any other person that holds property in a way that does not give such person a beneficial interest in such property and shall not result in such property being subject to legally-enforceable claims by such persons, creditors, or to a court-ordered stay of the return of such property, should such person become insolvent or bankrupt.

(l) Collateral posted by a client, that is held by a custodian, and is bankruptcy remote from the QCCP, the clearing member and other clients, is not subject to a capital requirement for counterparty credit risk. If the collateral is held at the QCCP on a client’s behalf and is not held on a bankruptcy remote basis, a 2 per cent risk weight shall apply to the collateral if the conditions laid down in the preceding provisions on ‘client bank exposures to clearing members’ are met. A risk weight of 4 per cent shall apply if a client is not protected from losses in the case that the clearing member and another client of the clearing member jointly default or become jointly insolvent, but all other conditions laid down in the preceding provisions, as mentioned in this

paragraph 85(6) on ‘client bank exposures to clearing members’ are met.

(m) If a clearing member collects collateral from a client for client cleared trades and passes it on to the QCCP, the clearing member may recognise this collateral for both the QCCP - clearing member leg and the clearing member - client leg of the client cleared trade. Therefore, initial margins (IMs) as posted by clients to clearing members mitigate the exposure the clearing member has against these clients.

(ii) Default fund exposures to QCCPs

(a) Where a default fund is shared between products or types of business with settlement risk only (e.g., equities and bonds) and products or types of business which give rise to counterparty credit risk i.e., OTC derivatives, exchange traded derivatives or SFTs, all of the default fund contributions shall receive the risk weight determined according to the formulae and methodology specified hereinafter, without apportioning to different classes or types of business or products.

(b) However, where the default fund contributions from clearing members are segregated by product types and only accessible for specific product types, the capital requirements for those default fund exposures determined according to the formulae and methodology specified hereinafter shall be calculated for each specific product giving rise to counterparty credit risk. In case the QCCP’s prefunded own resources are shared among product types, the QCCP shall have to allocate those funds to each of the calculations, in proportion to the respective product specific exposure, i.e., EAD.

(c) A clearing member bank shall capitalise its exposures arising from default fund contributions to a qualifying CCP by applying the following methodology:

(i) A clearing member bank shall apply a risk-weight of 1250 per cent to its default fund exposures to the QCCP, subject to an overall cap on the RWA from all its exposures to the QCCP (i.e., including trade exposures) equal to 20 per cent of the trade

exposures to the QCCP. More specifically, the RWA for both bank i's trade and default fund exposures to each QCCP are equal to:

Min {(2% * TE_i + 1250% * DF_i); (20% * TE_i)}

Where;

TE_i is bank i's trade exposure to the QCCP; and

DF_i is bank i's pre-funded contribution to the QCCP's default fund.

Note - The 2 per cent risk weight on trade exposures does not apply additionally, as it is included in the equation.

(7) Exposures to non-qualifying CCPs

(i) A bank shall apply the Standardised Approach for credit risk according to the category of the counterparty, to its trade exposure to a non-qualifying CCP.

Note - In cases where a CCP is to be considered as a non-QCCP and the exposure is to be reckoned on CCP, the applicable risk weight shall be according to the ratings assigned to the CCPs.

(ii) A bank shall apply a risk weight of 1250 per cent to its default fund contributions to a non-qualifying CCP.

(iii) For the purpose of this paragraph, the default fund contributions of such a bank shall include both the funded and the unfunded contributions which are liable to be paid should the CCP so require. Where there is a liability for unfunded contributions (i.e., unlimited binding commitments) the Reserve Bank shall determine in its Pillar 2 assessments the amount of unfunded commitments to which 1250 per cent risk weight shall apply.

86. Failed transactions

(1) With regard to unsettled securities and foreign exchange transactions, a bank is exposed to counterparty credit risk from trade date, irrespective of the booking or the accounting of the transaction. A bank shall develop, implement and improve systems for tracking and monitoring the credit risk exposure arising from

unsettled transactions as appropriate for producing management information that facilitates action on a timely basis.

(2) A bank shall closely monitor securities and foreign exchange transactions that have failed, starting from the day they fail, for producing management information that facilitates action on a timely basis. Failed transactions give rise to risk of delayed settlement or delivery.

(3) Failure of transactions settled through a delivery-versus-payment system (DvP), providing simultaneous exchanges of securities for cash, expose a bank to a risk of loss on the difference between the transaction valued at the agreed settlement price and the transaction valued at current market price (i.e., positive current exposure). Failed transactions where cash is paid without receipt of the corresponding receivable (securities, foreign currencies, or gold,) or, conversely, deliverables were delivered without receipt of the corresponding cash payment (non-DvP, or free delivery) expose a bank to a risk of loss on the full amount of cash paid or deliverables delivered. Therefore, a capital charge is required for failed transactions and shall be calculated as under for all failed transactions, including transactions through recognised clearing houses and central counterparties but excluding repurchase, reverse-repurchase agreements and securities lending and borrowing that have failed to settle:

(4) For DvP Transactions - If the payments have not taken place five business days after the settlement date, a bank shall calculate a capital charge by multiplying the positive current exposure of the transaction by the appropriate factor as under.

Table 18: Capital charge for DvP transactions

Number of working days after the agreed settlement date	Corresponding factor (in per cent)
From 5 to 15	9
From 16 o 30	50
From 31 to 45	75
46 or more	100

(5) For non-DvP transactions (free deliveries) after the first contractual payment / delivery leg, the bank that has made the payment shall treat its exposure as a loan if the second leg has not been received by the end of the business day. If the dates when two payment legs are made are the same according to the time

zones where each payment is made, it is deemed that they are settled on the same day. For example, if a bank in Tokyo transfers Yen on day X (Japan Standard Time) and receives corresponding US Dollar via CHIPS on day X (US Eastern Standard Time), the settlement is deemed to take place on the same value date. A bank shall compute the capital requirement using the counterparty risk weights prescribed in these guidelines. However, if five business days after the second contractual payment / delivery date the second leg has not yet effectively taken place, the bank that has made the first payment leg shall receive a risk weight of 1250 per cent on the full amount of the value transferred plus replacement cost, if any. This treatment shall apply until the second payment / delivery leg is effectively made.

87. Requirements for recognition of net replacement cost in close-out netting sets

(1) For repo-style transactions

(i) The effects of bilateral netting agreements covering repo-style transactions shall be recognised on a counterparty-by-counterparty basis if the agreements are legally enforceable in each relevant jurisdiction upon the occurrence of an event of default and regardless of whether the counterparty is insolvent or bankrupt. In addition, netting agreements shall:

(a) provide the non-defaulting party the right to terminate and close-out in a timely manner all transactions under the agreement upon an event of default, including in the event of insolvency or bankruptcy of the counterparty;

(b) provide for the netting of gains and losses on transactions (including the value of any collateral) terminated and closed out under it so that a single net amount is owed by one party to the other;

(c) allow for the prompt liquidation or setoff of collateral upon the event of default;

(d) be, together with the rights arising from the provisions required in (a) to (c) above, legally enforceable in each relevant jurisdiction upon the occurrence of an event of default and regardless of the counterparty's insolvency or bankruptcy; and

(e) Netting across positions in the banking and trading book shall only be recognised when the netted transactions fulfil the following conditions:

(i) All transactions are marked to market daily; and

(ii) The collateral instruments used in the transactions are recognised as eligible financial collateral in the banking book.

Note - The holding period for the haircuts shall depend as in other repo-style transactions on the frequency of margining.

(2) For derivatives transactions

(i) A bank may net transactions subject to novation under which any obligation between a bank and its counterparty to deliver a given currency on a given value date is automatically amalgamated with all other obligations for the same currency and value date, legally substituting one single amount for the previous gross obligations.

(ii) A bank may also net transactions subject to any legally valid form of bilateral netting not covered in sub-paragraph (2)(i) above, including other forms of novation.

(iii) In both cases (i) and (ii), a bank shall need to satisfy that it has:

(a) A netting contract or agreement with the counterparty which creates a single legal obligation, covering all included transactions, such that the bank shall have either a claim to receive or obligation to pay only the net sum of the positive and negative mark-to-market values of included individual transactions in the event a counterparty fails to perform due to any of the following: default, bankruptcy, liquidation, or similar circumstances.

Note - Membership agreement together with relevant netting provisions contained in QCCP’s bye laws, rules and regulations are a type of netting agreement.

(b) Written and reasoned legal opinions that, in the event of a legal challenge, the relevant courts and administrative authorities shall find the bank's exposure to be such a net amount under:

(i) The law of the jurisdiction in which the counterparty is chartered and, if the foreign branch of a counterparty is involved, then also under the law of the jurisdiction in which the branch is located;

(ii) The law that governs the individual transactions; and

(iii) The law that governs any contract or agreement necessary to effect the netting.

(c) Procedures in place to ensure that the legal characteristics of netting arrangements are kept under review in the light of possible changes in relevant law.

(iv) Contracts containing walkaway clauses shall not be eligible for netting for the purpose of calculating capital requirements under these Directions. A walkaway clause is a provision which permits a non-defaulting counterparty to make only limited payments or no payment at all, to the estate of a defaulter, even if the defaulter is a net creditor.

A.16 Securitisation exposures

Capital requirements on securitisation exposures undertaken on or after September 24, 2021

General conditions

88. A bank shall maintain capital against all securitisation exposure amounts, including those arising from the provision of credit risk mitigants to a securitisation transaction, investments in asset-backed or mortgage-backed securities, retention of a subordinated tranche, and extension of a liquidity facility or credit enhancement. For capital computation, whenever securitisation exposures are a subject of repurchase agreements and repurchased by a bank, the exposure shall be treated as retained exposure and not a fresh exposure. A bank shall deduct from CET1 or NOF (in case of other regulated entities which do not have any specific requirement of CET1) any increase in equity capital resulting from a securitisation transaction, either realised at the time of sale of underlying assets to the SPE, or unrealised gains on sale of underlying assets such as that associated with expected future margin income, where recognised upfront, till the maturity of such assets.

89. For calculating exposure amount, a bank shall measure the exposure amount of its off-balance exposure as follows:

(i) for credit risk mitigants sold or purchased by a bank (including a SFB), the treatment set out in paragraphs 154 to 181 shall apply;

(ii) for facilities that are not eligible credit risk mitigants, the bank shall use a CCF of 100 per cent; and

(iii) for derivatives contracts other than credit risk derivatives contracts, such as interest rate or currency swaps sold or purchased by the bank, to the extent not covered by paragraphs 89(i) and 89(ii) above, the measurement approach set out in paragraph 85(2) shall apply.

90. For the purpose of calculating capital requirements, a bank's exposure A overlaps another exposure B if in all circumstances the bank will preclude any loss for the bank on exposure B by fulfilling its obligations with respect to exposure A. For example, if a bank provides full credit support to some securitisation notes and holds a portion of these securitisation notes, its full credit support obligation precludes any loss from its exposure to the securitisation notes. If a bank can verify that fulfilling its obligations with respect to exposure A shall preclude a loss from its exposure to B under any circumstance, the bank does not need to calculate risk-weighted assets for its exposure B.

91. To arrive at an overlap, a bank shall, for the purposes of calculating capital requirements, split or expand its exposures, i.e., splitting exposures into portions that overlap with another exposure held by the bank and other portions that do not overlap; and expanding exposures by assuming for capital purposes that obligations with respect to one of the overlapping exposures are larger than those established contractually. For example, a liquidity facility shall not be contractually required to cover defaulted assets in certain circumstances. For capital purposes, such a situation shall not be regarded as an overlap to the securitisation notes issued by that securitisation. However, the bank shall calculate RWAs for the liquidity facility as if it were expanded (either to cover defaulted assets or in terms of trigger events) to preclude all losses on the securitisation notes. In such a case, the bank shall only need to calculate capital requirements on the liquidity facility.

92. Overlap may also be recognised between relevant capital charges for exposures in the trading book and capital charges for exposures in the banking book, provided that the bank is able to calculate and compare the capital charges for the relevant exposures.

93. Liquidity facilities provided by a bank that satisfy the requirements of Reserve Bank of India (Commercial Banks – Securitisation Transactions) Directions, 2025 shall attract risk weights as per the SEC-ERBA approach prescribed in paragraphs 115 to 122.

94. Liquidity facilities provided by a bank that do not satisfy the requirements of Reserve Bank of India (Commercial Banks – Securitisation Transactions) Directions, 2025 shall maintain capital charge equal to the actual exposure, after applying a CCF of 100 per cent for the undrawn portion.

95. All securitisation exposures, which are not covered by these directions, or which do not satisfy the conditions prescribed in these directions (including the exposures prohibited and conditions prescribed as per Reserve Bank of India (Commercial Banks – Securitisation Transactions) Directions, 2025 or where originator is not a lender referred to in Reserve Bank of India (Commercial Banks – Securitisation Transactions) Directions, 2025, or for which prudential treatment is not advised explicitly in these directions or Reserve Bank of India (Commercial Banks – Securitisation Transactions) Directions, 2025, a bank shall maintain capital charge equal to the actual exposure and shall be subjected to supervisory scrutiny and suitable action.

Derecognition of transferred assets for the purpose of capital adequacy

96. An originator shall maintain capital against the exposures transferred to a SPE, which then forms the underlying for securitisation notes issued by the SPE, i.e., the exposures transferred to a SPE shall be included in the calculation of risk-weighted assets of the originator and the consideration received from SPE shall be recognised as an advance, unless the following conditions are satisfied.

(1) The originator does not maintain direct or indirect control over the transferred exposures. For this purpose, the originator is deemed to have maintained effective control over the transferred credit risk exposures if it: (i) is able to repurchase from the SPE the previously transferred exposures in order to realise

their benefits; or (ii) is obligated, contractually or otherwise, to retain the risk of the transferred exposures.

Explanation - For this paragraph, retention of servicing rights in respect of the transferred exposures shall not constitute control by the originator over the transferred exposures.

(2) The originator shall not be able to repurchase the transferred exposures unless it is done through invocation of a clean-up call option.

Provided that, the purchase on invocation of clean-up calls is conducted at arm's length, on market terms and conditions (including price / fee) and is subject to the originator's normal credit approval and review processes;

(3) The transferred exposures are legally isolated from the originator in such a way that the exposures are put beyond the reach of the originator or its creditors, even in bankruptcy (specially Insolvency and Bankruptcy Code, 2016) or administration.

(4) The securitisation notes issued by the SPE are not obligations of the originator. Thus, the investors who purchase the securitisation notes have a claim only to the underlying exposures.

(5) The holders of the securitisation notes issued by the SPE against the transferred exposures have the right to pledge or trade them without any restriction unless the restriction is imposed by a statutory or regulatory risk retention requirement.

(6) The exercise of the clean-up calls, if any, shall not be mandatory on the originator, in form or substance and shall be at the discretion of the originator.

(7) The clean-up call options, if any, shall not be structured to avoid allocating losses to credit enhancements or positions held by investors or otherwise structured to provide credit enhancements.

Provided that, if a clean-up call, when exercised, is found to serve as a credit enhancement (for example, to purchase delinquent underlying exposures), the exercise of the clean-up call shall be considered a form of implicit support provided by the originator.

(8) The threshold at which clean-up calls become exercisable shall not be more than 10 per cent of the original value of the underlying exposures or securitisation notes.

(9) The securitisation does not contain clauses that require the originator to replace or replenish the underlying exposures to improve the credit quality of the pool in the event of deterioration in the underlying credit quality, except under conditions specifically permitted in these Directions.

(10) If the originator provides credit enhancement or first loss facility, the securitisation structure shall not allow for increase in the above positions after inception.

(11) The securitisation does not contain clauses that increase the yield payable to parties other than the originator such as investors and third-party providers of credit enhancements, in response to a deterioration in the credit quality of the underlying pool.

Explanation –

(i) This restriction stipulates that deterioration in the credit quality of the underlying pool shall be covered through invocation of first loss or second loss facilities, if available, and the protection available due to the seniority of the securitisation exposures, and not by increase in payments to the investors.

(ii) This restriction shall not apply to increase in yields to investors on account of movements in reference rates to which the underlying loans shall be benchmarked.

(12) There shall be no termination options or triggers to the securitisation exposures except eligible clean-up call options or termination provisions for specific changes in tax and regulation (regulatory or tax call options) or early amortisation provisions.

Provided that, early amortisation provisions do not subordinate the originator's senior or *pari passu* interest in the underlying to the interest of other investors, nor subordinate the originator's subordinated interest to an even greater degree relative to the interest of other parties, nor in other ways increase the exposure

of the originator to the losses associated with the underlying exposures shall be treated as in violation of the provisions of this paragraph.

97. The originator shall obtain legal opinion that the transfer of exposures to a special purpose entity satisfies the above conditions if the exposures are to be excluded from the calculation of RWAs.

Approaches for computation of RWA

98. A bank shall apply Securitisation External Ratings Based approach (SEC-ERBA) for calculation of RWA for credit risk of securitisation exposures. For unrated securitisation exposures, bank shall maintain capital charge equal to the actual exposure.

99. The capital charges computed based on the prescribed risk weights are subject to a cap of the actual exposure in respect of which capital adequacy is being computed such that the capital requirement for any securitisation position does not exceed the securitisation exposure amount.

100. However, the originator shall apply a maximum capital requirement for the securitisation exposures it holds, up to the permissible aggregate threshold, equal to the capital requirement that shall have been assessed against the entire underlying loan exposures had they not been securitised.

101. When a bank provides implicit support to a securitisation, it shall, at a minimum, hold capital against all the underlying exposures associated with the securitisation transaction as if they had not been securitised. Additionally, a bank shall not be permitted to recognise in regulatory capital any gain on sale.

Determination of attachment point (A) and detachment point (D)

102. The attachment point (A) represents the threshold at which losses within the underlying pool shall first be allocated to the relevant securitisation exposure. It shall be expressed as a decimal value between zero and one and shall be equal to the greater of zero and the ratio of the outstanding balance of the pool of underlying exposures in the securitisation minus the outstanding balance of all tranches that rank senior or *pari passu* to the tranche containing the relevant securitisation position including the exposure itself to the outstanding balance of all the underlying exposures in the securitisation.

103. The detachment point (D) represents the threshold at which losses within the underlying pool result in a total loss of principal for the tranche in which a relevant securitisation exposure resides. It shall be expressed as a decimal value between zero and one and shall be equal to the greater of zero and the ratio of the outstanding balance of the pool of underlying exposures in the securitisation minus the outstanding balance of all tranches that rank senior to the tranche containing the relevant securitisation position to the outstanding balance of all the underlying exposures in the securitisation.

104. For the calculation of A and D, over-collateralisation and funded reserve accounts shall be recognised as tranches; and the assets forming these reserve accounts shall be recognised as underlying assets. Only the loss-absorbing part of the funded reserve accounts that provide credit enhancement shall be recognised as tranches and underlying assets.

105. Unfunded reserve accounts, such as those to be funded from future receipts from the underlying exposures (e.g., unrealised excess spread) and assets that do not provide credit enhancement related to these instruments shall not be included in the above calculation of A and D.

106. A bank shall take into consideration the economic substance of the transaction rather than the form and apply these definitions conservatively in the light of the structure.

Determination of tranche maturity

107. For risk-based capital purposes, tranche maturity (M_T) shall be measured at the bank's discretion in either of the following manners.

    (i) As the rupee weighted-average maturity of the contractual cash flows of the tranche, as expressed below, where CF_t denotes the cash flows (principal, interest payments and fees) contractually payable by the borrower in period t. The contractual payments shall be unconditional and shall not be dependent on the actual performance of the securitised assets. If such unconditional contractual payment dates are not available, the final legal maturity shall be used.

$$M_T = \frac{\sum_t tCF_t}{\sum_t CF_t}$$

(ii) On the basis of final legal maturity of the tranche, where M_L is the final legal maturity of the tranche. (M_T and M_L are in years)

$$M_T = 1 + 0.8(M_L - 1)$$

In all cases, M_T shall have a floor of one year and a cap of five years. The cap of five years is only for the capital computation purposes and is not applicable for the actual permissible maturity for tranches.

108. When determining the maturity of a securitisation exposure, a bank shall take into account the maximum period of time they are exposed to potential losses from the securitised assets. In cases where a bank provides a commitment, the bank shall calculate the maturity of the securitisation exposure resulting from this commitment as the sum of the contractual maturity of the commitment and the longest maturity of the asset(s) to which the bank shall be exposed after a draw has occurred.

109. For credit protection instruments that are only exposed to losses that occur up to the maturity of that instrument, a bank shall be allowed to apply the contractual maturity of the instrument and shall not have to look through to the protected position.

Treatment by a bank of credit risk mitigation for securitisation exposures

110. A bank shall recognise credit protection purchased on a securitisation exposure when calculating capital requirements subject to the following:

(i) collateral recognition is limited to that permitted under paragraph 161. Eligible Collateral pledged by SPEs shall be recognised;

(ii) credit protection provided by the entities listed in paragraph 171 shall be recognised. SPEs shall not be recognised as eligible guarantors; and

(iii) where guarantees fulfil the minimum operational conditions as specified in paragraphs 167 to 176 of these Directions, a bank shall take account of such credit protection in calculating capital requirements for securitisation exposures.

111. When a bank provides full (or pro rata) credit protection to a securitisation exposure, it shall calculate its capital requirements as if it directly holds the

portion of the securitisation exposure on which it has provided credit protection (in accordance with the definition of tranche maturity).

112. Provided that the conditions set out in paragraph 110 are met, the bank buying full (or pro rata) credit protection shall recognise the credit risk mitigation on the securitisation exposure in accordance with the CRM framework.

113. Under all approaches, a lower-priority sub-tranche shall be treated as a non-senior securitisation exposure even if the original securitisation exposure prior to protection qualifies as senior tranche as defined in Reserve Bank of India (Commercial Banks – Securitisation Transactions) Directions, 2025.

114. A maturity mismatch exists when the residual maturity of a hedge is less than that of the underlying exposure. When protection is bought on a securitisation exposure(s), for the purpose of setting regulatory capital against a maturity mismatch, the capital requirement shall be determined in accordance with paragraphs 177 to 180 of these Directions. When the exposures being hedged have different maturities, the longest maturity shall be used.

SEC-ERBA

115. For securitisation exposures that are externally rated, RWAs under the SEC-ERBA shall be determined by multiplying securitisation exposure amounts by the appropriate risk weights as determined by paragraphs 116 to 118 as mentioned in these Directions below, provided that the following operational criteria are met:

(i) To be eligible for risk-weighting purposes, the external credit assessment shall take into account and reflect the entire amount of credit risk exposure the bank has with regard to all payments owed to it. For example, if a bank is owed both principal and interest, the assessment shall fully take into account and reflect the credit risk associated with timely repayment of both principal and interest.

(ii) The external credit assessments shall be from an eligible external credit rating agency (CRA) as provided in paragraphs 131 to 153 of these Directions. A rating shall be published in a publicly accessible form and included in the CRA's transition matrix. Also, loss and cash flow analysis as well as sensitivity of ratings to changes in the underlying rating assumptions shall be publicly available. Consequently, ratings that are made available

only to the parties to a transaction do not satisfy this requirement. Further, the external credit assessment provided by the eligible CRAs shall not be more than six months old.

(iii) Eligible CRAs shall have a demonstrated expertise in assessing securitisations, which shall be evidenced by strong market acceptance.

(iv) Furthermore, a bank shall not use the credit assessments issued by one external CRA for one or more tranches and those of another external CRA for other positions (whether retained or purchased) within the same securitisation structure that may or may not be rated by the first external credit rating agency. Where two or more eligible CRAs shall be used and these assess the credit risk of the same securitisation exposure differently, paragraph 151 shall apply.

(v) Where CRM is provided to specific underlying exposures or the entire pool by an eligible guarantor as defined in paragraph 171 and is reflected in the external credit assessment assigned to a securitisation exposure(s), the risk weight associated with that external credit assessment shall be used. To avoid any double counting, no additional capital recognition is permitted. If the CRM provider is not recognised as an eligible guarantor, the covered securitisation exposures shall be treated as unrated.

(vi) In the situation where a CRM solely protects a specific securitisation exposure within a given structure (e.g. asset-backed security tranche) and this protection is reflected in the external credit assessment, the bank shall treat the exposure as if it is unrated and then apply the CRM treatment outlined in paragraphs 154 to 181 of these Directions.

(vii) A bank is not permitted to use any external credit assessment for risk weighting purposes where the assessment is at least partly based on unfunded support provided by the bank. For example, if a bank buys asset-backed security (ABS) where it provides an unfunded securitisation exposure (e.g., liquidity facility or credit enhancement), and that exposure plays a role in determining the credit assessment on the ABS, the bank shall treat the ABS as if it were not rated. The bank shall continue to hold

capital against the other securitisation exposures it provides (e.g., against the liquidity facility and / or credit enhancement).

116. For exposures with short-term ratings, the following risk weights shall apply:

Table 19: ERBA risk weights for short-term ratings				
External credit assessment	A1+ / A1	A2	A3	All other ratings
Risk weight	15%	50%	100%	1250%

117. For exposures with long-term ratings, the risk weights depend on:

(i) the external rating grade;

(ii) the seniority of the position;

(iii) the tranche maturity; and

(iv) in the case of non-senior tranches, the tranche thickness.

118. Specifically, for exposures with long-term ratings, risk weights shall be determined according to the following table and shall be adjusted for tranche maturity and tranche thickness for non-senior tranches as prescribed in paragraph 119 as mentioned below.

Table 20: ERBA risk weights for long-term ratings				
Rating	Senior tranche		Non-senior (thin) tranche	
	Tranche maturity (MT)		Tranche maturity (MT)	
	1 year	5 years	1 year	5 years
AAA	15%	20%	15%	70%
AA+	15%	30%	15%	90%
AA	25%	40%	30%	120%
AA-	30%	45%	40%	140%
A+	40%	50%	60%	160%
A	50%	65%	80%	180%
A-	60%	70%	120%	210%
BBB+	75%	90%	170%	260%
BBB	90%	105%	220%	310%
BBB-	120%	140%	330%	420%
BB+	140%	160%	470%	580%

Table 20: ERBA risk weights for long-term ratings				
Rating	Senior tranche		Non-senior (thin) tranche	
	Tranche maturity (MT)		Tranche maturity (MT)	
	1 year	5 years	1 year	5 years
BB	160%	180%	620%	760%
BB-	200%	225%	750%	860%
B+	250%	280%	900%	950%
B	310%	340%	1050%	1050%
B-	380%	420%	1130%	1130%
CCC+ / CCC / CCC-	460%	505%	1250%	1250%
Below CCC-	1250%	1250%	1250%	1250%

119. The risk weight assigned to a securitisation exposure when applying the SEC-ERBA is calculated as follows:

(i) To account for tranche maturity, a bank shall use linear interpolation between the risk weights for one and five years.

(ii) To account for tranche thickness, a bank shall calculate the risk weight for non-senior tranches as follows:

$$Risk\ weight = (risk\ weight\ from\ table\ after\ adaausting\ for\ maturity) * (1 - \min(T, 50\%))$$

where T is the tranche thickness.

120. In the case of market risk hedges such as currency or interest rate swaps, the risk weight shall be inferred from a securitisation exposure that is *pari passu* to the swaps or, if such an exposure does not exist, from the next subordinated tranche.

121. The resulting risk weight is subject to a floor risk weight of 15 per cent. In addition, the resulting risk weight shall never be lower than the risk weight corresponding to a senior tranche of the same securitisation with the same rating and maturity.

122. An illustrative example for calculation of risk weights is as below:

(i) Underlying loans being securitised: ₹2000 crores;

(ii) Issued Securitised Notes: ₹1800 crores;

(iii) Overcollateralisation: ₹200 crores;

(iv) Maturity 'M' (as envisaged for use in RWA computation): 3 years;

(v) Total underlying pool for purpose of attachment and detachment point computation: ₹2000 crores;

(vi) Calculation below is exhibited for non-STC securitisation;

(vii) Adjustment in Risk Weight for a maturity equal to

M years = RWyear1 + (M-1) * $\frac{\text{RWyear 5} - \text{RWyear 1}}{(5-1)}$ (Column 4 below);

(viii) Risk Weight (%) = Risk weight as given in table in paragraph 118 (depending upon senior / non-senior exposure) adjusted for maturity * (1-Minimum (T,50%)) (Column 5 below).

Illustration: RWA Computation

Securitisation Notes (1)	**Determination of Tranche Thickness (2)**	**Rating (presumptive, not indicative) (3)**	**RW after interpolating linked to maturity year (4)**	**RW after factoring in tranche thickness (5)**	**RWA@ (6)**
Note A (senior): ₹ 1500 crores	Attachment point*: (250+50+200) / 2000 = 0.25	AA+	RW for 1 year = 15% RW for 5 year = 30% (from table 20)	No tranche thickness adjustment	1500 * 22.5% = 337.5 crores
	Detachment Point#: 1 (1500+250+50+200) / 2000		Actual RW adjusting for maturity	requirement for senior tranche	
	Tranche thickness (T): (1-0.25) = 0.75		15% + (30-15)%*2 / 4 = 22.5%		
Note B: 250 crores	Attachment point: (50+200) / 2000 = 0.125	AA-	RW for 1 year = 40% RW for 5 year = 140% (from table 20)	90% * (1-Min(0.5,0.125)) = 78.75%	250 * 78.75% =196.875 crores
	Detachment Point: (250+50+200) / 2000 = 0.25		Actual RW adjusting for maturity		
	Tranche thickness (T): (0.25-0.125) = 0.125		40% + (140-40)%*2 / 4 = 90%		

Securitisation Notes (1)	Determination of Tranche Thickness (2)	Rating (presumptive, not indicative) (3)	RW after interpolating linked to maturity year (4)	RW after factoring in tranche thickness (5)	RWA@ (6)
Note C: 50 crores	Attachment point: 200 / 2000= 0.10	BB+	RW for 1 year = 470% RW for 5 year = 580% (from table 20)	525% * (1-Min (0.5,0.025)) = 511.875%	50 * 511.875%= 255.94 crores
	Detachment Point: (50+200) / 2000 = 0.125		470% + (580-470)%*2 / 4=525%		
	Tranche thickness (T): (0.125-0.10) = 0.025				
Total Risk-Weighted Assets					**790.315 crores**

*Attachment point of a tranche is the fraction of pool losses to which it is not exposed

#Detachment point of a tranche is the fraction of pool losses at which it is entirely wiped-out Attachment point of one tranche is the detachment point of the next-most junior tranche.

Alternative capital treatment for simple, transparent and comparable (STC) securitisation

(This paragraph is applicable to STC securitisations. Securitisation transactions that satisfy all the criteria laid out in Reserve Bank of India (Commercial Banks – Securitisation Transactions) Directions, 2025 fall within the scope of the STC framework)

123. For exposures with short-term ratings, the following risk weights shall apply:

Table 21: ERBA STC risk weights for short-term ratings				
External credit assessment	A1+ / A1	A2	A3	All other ratings
Risk weight	10%	30%	60%	1250%

124. For exposures with long-term ratings, risk weights shall be determined according to the following table and shall be adjusted for tranche maturity, and tranche thickness for non-senior tranches according to paragraph 119 as mentioned above.

Table 22: ERBA STC risk weights for long-term ratings		
Rating	Senior tranche	Non-senior (thin) tranche

	Tranche maturity (MT)		Tranche maturity (MT)	
	1 year	5 years	1 year	5 years
AAA	10%	10%	15%	40%
AA+	10%	15%	15%	55%
AA	15%	20%	15%	70%
AA-	15%	25%	25%	80%
A+	20%	30%	35%	95%
A	30%	40%	60%	135%
A-	35%	40%	95%	170%
BBB+	45%	55%	150%	225%
BBB	55%	65%	180%	255%
BBB-	70%	85%	270%	345%
BB+	120%	135%	405%	500%
BB	135%	155%	535%	655%
BB-	170%	195%	645%	740%
B+	225%	250%	810%	855%
B	280%	305%	945%	945%
B-	340%	380%	1015%	1015%
CCC+ / CCC / CCC-	415%	455%	1250%	1250%
Below CCC-	1250%	1250%	1250%	1250%

125. The resulting risk weight is subject to a floor risk weight of 10 per cent for senior tranches, and 15 per cent for non-senior tranches.

Note - All the criteria mentioned in the Reserve Bank of India (Commercial Banks – Securitisation Transactions) Directions, 2025 shall be satisfied for a securitisation to receive the alternative regulatory capital treatment as determined by paragraphs 123 to 125.

126. Capital requirements on securitisation exposures undertaken prior to September 24, 2021 shall be as under (the circulars mentioned in this paragraph shall otherwise be treated as repealed):

(1) General

(i) A securitisation transaction, which meets the minimum requirements, as stipulated in circular DBOD.No.BP.BC.60 / 21.04.048 / 2005-06 dated February 1, 2006 on 'Guidelines on Securitisation of Standard Assets', circular DBOD.No.BP.BC.103 / 21.04.177 / 2011-12 dated May 07, 2012 on 'Revision to the Guidelines on Securitisation Transactions' and circular DBOD.No.BP.BC- 25 / 21.04.177 / 2013-14 dated July 1, 2013 on 'Revision to the Guidelines on Securitisation Transactions - Reset of Credit Enhancement' shall qualify for the following prudential treatment of securitisation exposures for capital adequacy purposes. A bank's exposures to a securitisation transaction, referred to as securitisation exposures, shall include, but are not restricted to the following: as investor, as credit enhancer, as liquidity provider, as underwriter, as provider of credit risk mitigants. Cash collaterals provided as credit enhancements shall also be treated as securitisation exposures.

(ii) A bank is required to hold regulatory capital against all of its securitisation exposures, including those arising from the provision of credit risk mitigants to a securitisation transaction, investments in asset-backed securities, retention of a subordinated tranche, and extension of a liquidity facility or credit enhancement, as set forth in the following paragraphs. Repurchased securitisation exposures shall be treated as retained securitisation exposures.

(iii) An originator in a securitisation transaction which does not meet the minimum requirements prescribed in the guidelines dated February 01, 2006, May 07, 2012, and July 1, 2013, and therefore does not qualify for de-recognition shall hold capital against all of the exposures associated with the securitisation transaction as if they had not been securitised. Additionally, the originator shall deduct any 'gain on sale' (i.e. the profit realised at the time of sale of the securitised assets to SPV) on such transaction from Tier I capital. This capital shall be in addition to the capital which a bank is required to maintain on its other existing exposures to the securtisation transaction.

Explanation –

If in a securitisation transaction of ₹100, the pool consists of 80 per cent of AAA securities, 10 per cent of BB securities and 10 per cent of unrated securities and the transaction does not meet the true sale criterion, then the originator shall be deemed to be holding all the exposures in that transaction. Consequently, the AAA rated securities shall attract a risk weight of 20 per cent and the face value of the BB rated securities and the unrated securities shall be deducted. Thus, the consequent impact on the capital shall be ₹21.44 (16*9 per cent + 20).

(iv) Operational criteria for Credit Analysis

In addition to the conditions specified in the Reserve Bank's guidelines dated February 1, 2006, May 7, 2012, and July 1, 2013, on securitisation of standard assets in order to qualify for de-recognition of assets securitised, a bank shall have the information specified below:

(a) A bank shall, on an ongoing basis, have a comprehensive understanding of the risk characteristics of its individual securitisation exposures, whether on balance sheet or off-balance sheet, as well as the risk characteristics of the pools underlying its securitisation exposures.

(b) A bank shall be able to access performance information on the underlying pools on an on-going basis in a timely manner. Such information may include, as appropriate: exposure type; percentage of loans 30, 60 and 90 days past due; default rates; prepayment rates; loans in foreclosure; property type; occupancy; average credit score or other measures of creditworthiness; average loan-to-value ratio; and industry and geographic diversification.

(c) A bank shall have a thorough understanding of all structural features of a securitisation transaction that shall materially impact the performance of a bank's exposures to the transaction, such as the contractual waterfall and waterfall-related triggers, credit enhancements, liquidity enhancements, market value triggers, and deal-specific definitions of default.

(2) Treatment of securitisation exposures

(i) Credit enhancements which are first loss positions shall be risk weighted at 1250 per cent.

(ii) Any rated securitisation exposure with a long-term rating of 'B+ and below' when not held by an originator, and a long-term rating of 'BB+ and below' when held by the originator shall receive a risk weight of 1250 per cent.

(iii) Any unrated securitisation exposure, except an eligible liquidity facility as specified in sub-paragraph (8) shall be risk weighted at 1250 per cent. In an unrated and ineligible liquidity facility, both the drawn and undrawn portions (after applying a CCF of 100 per cent) shall receive a risk weight of 1250 per cent.

(iv) The holdings of securities devolved on the originator through underwriting shall be sold to third parties within three-month period following the acquisition. In case of failure to off-load within the stipulated time limit, any holding in excess of 20 per cent of the original amount of issue, including secondary market purchases, shall receive a risk weight of 1250 per cent.

(3) Implicit support

(i) The originator shall not provide any implicit support to investors in a securitisation transaction.

(ii) When a bank is deemed to have provided implicit support to a securitisation:

(iii) It shall, at a minimum, hold capital against all of the exposures associated with the securitisation transaction as if they had not been securitised.

(iv) Furthermore, in respect of securitisation transactions where a bank is deemed to have provided implicit support it is required to disclose publicly that (i) it has provided non-contractual support (ii) the details of the implicit support and (iii) the impact of the implicit support on a bank's regulatory capital.

(v) Where a securitisation transaction contains a clean-up call and the clean up call can be exercised by the originator in circumstances where exercise of the clean up call effectively provides credit enhancement, the clean up

call shall be treated as implicit support and the concerned securitisation transaction shall attract the above prescriptions.

(4) Application of external ratings

The following operational criteria concerning the use of external credit assessments apply:

(i) A bank shall apply external credit assessments from eligible external credit rating agencies consistently across a given type of securitisation exposure. Furthermore, a bank shall not use the credit assessments issued by one external credit rating agency for one or more tranches and those of another external credit rating agency for other positions (whether retained or purchased) within the same securitisation structure that may or may not be rated by the first external credit rating agency. Where two or more eligible external credit rating agencies can be used and these assess the credit risk of the same securitisation exposure differently, provisions of paragraph 151 shall apply.

(ii) If the CRM provider is not recognised as an eligible guarantor as defined in paragraph 171, the covered securitisation exposures shall be treated as unrated.

(iii) In the situation where a credit risk mitigant is not obtained by the SPV but rather applied to a specific securitisation exposure within a given structure (e.g., ABS tranche), a bank shall treat the exposure as if it is unrated and then use the CRM treatment outlined in paragraphs 154 to 181 of these Directions.

(iv) The other aspects of application of external credit assessments shall be as per guidelines given in paragraphs 131 to 153 of these Directions.

(v) A bank is not permitted to use any external credit assessment for risk weighting purposes where the assessment is at least partly based on unfunded support provided by a bank. For example, if a bank buys an ABS / MBS where it provides an unfunded securitisation exposure extended to the securitisation programme (e.g., liquidity facility or credit enhancement), and that exposure plays a role in determining the credit assessment on the securitised assets / various tranches of the ABS / MBS, a bank shall treat

the securitised assets / various tranches of the ABS / MBS as if these were not rated. A bank shall continue to hold capital against the other securitisation exposures it provides (e.g., against the liquidity facility and / or credit enhancement).

(5) Risk weighted securitisation exposures

(i) A bank shall calculate the risk weighted amount of an on-balance sheet securitisation exposure by multiplying the principal amount (after deduction of specific provisions) of the exposures by the applicable risk weight.

(ii) The risk-weighted asset amount of a securitisation exposure is computed by multiplying the amount of the exposure by the appropriate risk weight determined in accordance with issue specific rating assigned to those exposures by the chosen external credit rating agencies as indicated in the following tables:

Table 23.1: Securitisation exposures - risk weight mapping to long-term ratings

Domestic rating agencies	AAA	AA	A	BBB	BB	B and below or unrated
Risk weight for a bank other than originators (%)	20	30	50	100	350	1250
Risk weight for originator (%)	20	30	50	100	1250	

(iii) The risk-weighted asset amount of a securitisation exposure in respect of MBS backed by commercial real estate exposure, as defined in paragraph 60, is computed by multiplying the amount of the exposure by the appropriate risk weight determined in accordance with issue specific rating assigned to those exposures by the chosen external credit rating agencies as indicated in the following tables:

Table 23.2: Commercial real estate securitisation exposures – risk weight mapping to long-term ratings

Domestic Rating Agencies	AAA	AA	A	BBB	BB	B and below or unrated
Risk weight for a bank other than originators (%)	100	100	100	150	400	1250
Risk weight for originator (%)	100	100	100	150	1250	

(iv) A bank is not permitted to invest in unrated securities issued by an SPV as a part of the securitisation transaction. However, securitisation exposures assumed by a bank which may become unrated or may be deemed to be unrated, shall be treated for capital adequacy purposes in accordance with the provisions of sub-paragraph (2).

(v) There shall be transfer of a significant credit risk associated with the securitised exposures to the third parties for recognition of risk transfer. In view of this, the total exposure of a bank to the loans securitised in the following forms shall not exceed 20 per cent of the total securitised instruments issued:

(a) Investments in equity / subordinate / senior tranches of securities issued by the SPV including through underwriting commitments; and

(b) Credit enhancements including cash and other forms of collaterals including over-collateralisation but excluding the credit enhancing interest only strip - Liquidity support.

(vi) If a bank exceeds the above limit, the excess amount shall be risk weighted at 1250 per cent. Credit exposure on account of interest rate swaps / currency swaps entered into with the SPV shall be excluded from the limit of 20 per cent as this shall not be within the control of a bank.

(vii) If an originating bank fails to meet the requirement laid down in the paragraphs 1.1 to 1.7 of paragraph A / paragraphs 1.1 to 1.6 of paragraph B of the circular DBOD.No.BP.BC.103// 21.04.177/2011-12 dated May 07, 2012 on 'Revision to the Guidelines on Securitisation Transactions', it shall have to maintain capital for the securtised assets / assets sold as if these were not securtised / sold. This capital shall be in addition to the capital which a bank is required to maintain on its other existing exposures to the securitisation transaction.

(viii) A investing bank shall assign a risk weight of 1250 per cent to the exposures relating to securtisation / or assignment where the requirements in the paragraphs 2.1 to 2.3 of paragraph A / or paragraphs 2.1 to 2.8 of paragraph B, respectively, of the circular DBOD.No.BP.BC.103//

21.04.177/2011-12 dated May 07, 2012 on 'Revision to the Guidelines on Securitisation Transactions' dated May 07, 2012 are not met.

(ix) Under the transactions involving transfer of assets through direct assignment of cash flows and the underlying securities, the capital adequacy treatment for direct purchase of corporate loans shall be as per the rules applicable to corporate loans directly originated by a bank. Similarly, the capital adequacy treatment for direct purchase of retail loans, shall be as per the rules applicable to retail portfolios directly originated by a bank except in cases where the individual accounts have been classified as NPA, in which case usual capital adequacy norms as applicable to retail NPAs shall apply. No benefit in terms of reduced risk weights shall be available to purchased retail loans portfolios based on rating because this is not envisaged under the Basel II Standardised Approach for credit risk.

(6) Off-balance sheet securitisation exposures

(i) A bank shall calculate the risk weighted amount of a rated off-balance sheet securitisation exposure by multiplying the credit equivalent amount of the exposure by the applicable risk weight. The credit equivalent amount shall be arrived at by multiplying the principal amount of the exposure (after deduction of specific provisions) with a 100 per cent CCF, unless otherwise specified.

(ii) If the off-balance sheet exposure is not rated, it shall be deducted from capital, except an unrated eligible liquidity facility for which the treatment has been specified separately in sub-paragraph (8).

(7) Recognition of credit risk mitigants (CRMs)

(i) The treatment below applies to a bank that has obtained a credit risk mitigant on a securitisation exposure. Credit risk mitigant include guarantees and eligible collateral as specified in these guidelines. Collateral in this context refers to that used to hedge the credit risk of a securitisation exposure rather than for hedging the credit risk of the underlying exposures of the securitisation transaction.

(ii) When a bank other than the originator provides credit protection to a securitisation exposure, it shall calculate a capital requirement on the

covered exposure as if it were an investor in that securitisation. If a bank provides protection to an unrated credit enhancement, it shall treat the credit protection provided as if it were directly holding the unrated credit enhancement.

(iii) Capital requirements for the guaranteed / protected portion shall be calculated according to CRM methodology for the standardised approach as specified in paragraphs 154 to 181 of these Directions. Eligible collateral is limited to that recognised under these guidelines in paragraph 161. For the purpose of setting regulatory capital against a maturity mismatch between the CRM and the exposure, the capital requirement shall be determined in accordance with paragraphs 177 to 180 of these Directions. When the exposures being hedged have different maturities, the longest maturity shall be used applying the methodology prescribed in paragraphs 179 and 180 of these Directions.

(8) Liquidity facilities

(i) A liquidity facility shall be considered as an 'eligible' facility only if it satisfies all minimum requirements prescribed in the guidelines issued on February 1, 2006. The rated liquidity facilities shall be risk weighted or deducted as per the appropriate risk weight determined in accordance with the specific rating assigned to those exposures by the chosen External Credit Assessment Institutions (ECAIs) as indicated in the tables presented above.

(ii) The unrated eligible liquidity facilities shall be exempted from deductions and treated as follows.

(iii) The drawn and undrawn portions of an unrated eligible liquidity facility shall attract a risk weight equal to the highest risk weight assigned to any of the underlying individual exposures covered by this facility.

(iv) The undrawn portion of an unrated eligible liquidity facility shall attract a credit conversion factor of 50 per cent.

(9) Re-Securitisation Exposures/ Synthetic Securitisations/ Securitisation with Revolving Structures (with or without early amortization features)

At present, a bank in India, including its overseas branches, is not permitted to assume exposures relating to re-securitisation / Synthetic Securitisations/ Securitisations with Revolving Structures (with or without early amortization features), as defined in circular DBOD.No.BP.BC.103/21.04.177/ 2011-12 dated May 07, 2012 on 'Revision to the Guidelines on Securitisation Transactions'. However, some of the Indian banks have invested in CDOs and other similar securitization exposures through their overseas branches before issuance of circular RBI/2008- 09/302.DBOD.No.BP.BC.89/21.04.141 /2008-09 dated December 1, 2008. Some of these exposures may be in the nature of re-securitisation. For such exposures, the risk weights would be assigned as under:

Table 24.1: Re-securitisation Exposures – Risk Weight Mapping to Long-Term Ratings

Domestic rating agencies	AAA	AA	A	BBB	BB	B and below or unrated
Risk weight for banks other than originators (%)	40	60	100	225	650	1250
Risk weight for originator (%)	40	60	100	225	1250	

Table 24.2: Commercial Real Estate Re-Securitisation Exposures – Risk Weight Mapping to Long-Term Ratings

Domestic rating agencies	AAA	AA	A	BBB	BB and below or unrated
Risk weight for banks other than originators (%)	200	200	200	400	1250
Risk weight for originator (%)	40	60	100	225	1250

A.17 Credit default swap (CDS) positions in the banking book

127. A bank can undertake transactions in CDS in terms of Master Direction – Reserve Bank of India (Credit Derivatives) Directions, 2022. As a user, a bank can buy CDS to hedge a banking book or trading book exposure. The prudential guidelines dealing with CDS are dealt with in the following paragraphs.

128. Operational requirements for CDS to be recognised as eligible external/ third-party hedges for trading book and banking book.

(1) A CDS contract shall represent a direct claim on the protection provider and shall be explicitly referenced to specific exposure, so that the extent of the cover is clearly defined and incontrovertible.

(2) Other than non-payment by a protection purchaser of premium in respect of the credit protection contract it shall be irrevocable.

(3) There shall be no clause in the contract that will allow the protection provider unilaterally to cancel the credit cover or that will increase the effective cost of cover as a result of deteriorating credit quality in the hedged exposure.

(4) The CDS contract shall be unconditional; there shall be no clause in the protection contract outside the direct control of the bank (protection buyer) that can prevent the protection provider from being obliged to pay out in a timely manner in the event that the original counterparty fails to make the payment(s) due.

(5) The credit events specified by the contracting parties shall at a minimum cover:

(i) failure to pay the amounts due under terms of the underlying obligation that are in effect at the time of such failure (with a grace period that is closely in line with the grace period in the underlying obligation);

(ii) bankruptcy, insolvency or inability of the obligor to pay its debts, or its failure or admission in writing of its inability generally to pay its debts as they become due, and analogous events;

(iii) restructuring of the underlying obligation involving forgiveness or postponement of principal, interest or fees that results in a credit loss event (i.e., charge-off, specific provision or other similar debit to the profit and loss account); and

(iv) when the restructuring of the underlying obligation is not covered by the CDS, but the other requirements in this paragraph are met, partial recognition of the CDS shall be allowed. If the amount of the CDS is less than or equal to the amount of the underlying obligation, 60 per cent of the amount of the hedge shall be recognised as covered. If the amount of the

CDS is larger than that of the underlying obligation, then the amount of eligible hedge is capped at 60 per cent of the amount of the underlying obligation.

(6) If the CDS specifies deliverable obligations that are different from the underlying obligation, the resultant asset mismatch shall be governed under sub-paragraph (11) below.

(7) The CDS shall not terminate prior to expiration of any grace period required for a default on the underlying obligation to occur as a result of a failure to pay.

Explanation – The maturity of the underlying exposure and the maturity of the hedge should be defined conservatively. The effective maturity of the underlying should be gauged as the longest possible remaining time before the counterparty is scheduled to fulfill its obligation, taking into account any applicable grace period.

(8) The CDS allowing for cash settlement are recognised for capital purposes insofar as a robust valuation process is in place to estimate loss reliably. There shall be a clearly specified period for obtaining post-credit event valuations of the underlying obligation. If the reference obligation specified in the CDS for purposes of cash settlement is different than the underlying obligation, the resultant asset mismatch shall be governed under sub-paragraph (11).

(9) If the protection purchaser's right / ability to transfer the underlying obligation to the protection provider is required for settlement, the terms of the underlying obligation shall provide that any required consent to such transfer may not be unreasonably withheld.

(10) The identity of the parties responsible for determining whether a credit event has occurred shall be clearly defined. This determination shall not be the sole responsibility of the protection seller. The protection buyer shall have the right / ability to inform the protection provider of the occurrence of a credit event.

(11) A mismatch between the underlying obligation and the reference obligation or deliverable obligation under the CDS (i.e. the obligation used for purposes of determining cash settlement value or the deliverable obligation) is permissible if (i) the reference obligation or deliverable obligation ranks *pari passu* with or is junior to the underlying obligation, and (ii) the underlying obligation and reference

obligation or deliverable obligation share the same obligor (i.e. the same legal entity) and legally enforceable cross-default or cross-acceleration clauses are in place.

(12) A mismatch between the underlying obligation and the obligation used for purposes of determining whether a credit event has occurred is permissible if (i) the latter obligation ranks *pari passu* with or is junior to the underlying obligation, and (ii) the underlying obligation and reference obligation share the same obligor (i.e., the same legal entity) and legally enforceable cross-default or cross acceleration clauses are in place.

129. Recognition of external / third-party CDS hedges

(1) In case of banking book positions hedged by bought CDS positions, no exposure shall be reckoned against the reference entity / underlying asset in respect of the hedged exposure, and exposure shall be deemed to have been substituted by the protection seller, subject to the following conditions:

(i) Operational requirements mentioned in paragraph 128 of these Directions are met;

(ii) The risk weight applicable to the protection seller under the Standardised Approach for credit risk is lower than that of the underlying asset; and

(iii) There is no maturity mismatch between the underlying asset and the reference / deliverable obligation. If this condition is not satisfied, then the amount of credit protection to be recognised shall be computed as indicated in sub-paragraph (3)(ii) below.

(2) If the conditions (i) and (ii) above are not satisfied or a bank breaches any of these conditions subsequently, the bank shall reckon the exposure on the underlying asset; and the CDS position shall be transferred to trading book where it shall be subject to specific risk, counterparty credit risk and general market risk (wherever applicable) capital requirements as applicable to trading book.

(3) The unprotected portion of the underlying exposure shall be risk-weighted as applicable under the Standardised Approach for credit risk. The amount of credit protection shall be adjusted if there are any mismatches between the underlying

asset / obligation and the reference / deliverable asset / obligation with regard to asset or maturity. These are dealt with in detail in the following paragraphs.

(i) Asset mismatches: Asset mismatch will arise if the underlying asset is different from the reference asset or deliverable obligation. Protection shall be reckoned as available by the protection buyer only if the mismatched assets meet the requirements that (a) the reference obligation or deliverable obligation ranks *pari passu* with or is junior to the underlying obligation, and (b) the underlying obligation and reference obligation or deliverable obligation share the same obligor (i.e., the same legal entity) and legally enforceable cross-default or cross-acceleration clauses are in place.

(ii) Maturity mismatches: The protection buyer shall be eligible to reckon the amount of protection if the maturity of the credit derivative contract were to be equal or more than the maturity of the underlying asset. If, however, the maturity of the CDS contract is less than the maturity of the underlying asset, then it would be construed as a maturity mismatch. In case of maturity mismatch the amount of protection shall be determined in the following manner:

(a) If the residual maturity of the credit derivative product is less than three months no protection shall be recognised.

(b) If the residual maturity of the credit derivative contract is three months or more protection proportional to the period for which it is available shall be recognised.

(c) When there is a maturity mismatch the following adjustment shall be applied.

$$P_a = P \times (t - 0.25) \div (T - 0.25)$$

Where:

P_a = value of the credit protection adjusted for maturity mismatch

P = credit protection

t = min (T, residual maturity of the credit protection arrangement) expressed in years

T = min (5, residual maturity of the underlying exposure) expressed in years

Example: Suppose the underlying asset is a corporate bond of Face Value of ₹100 where the residual maturity is of 5 years and the residual maturity of the CDS is 4 years. The amount of credit protection is computed as under:

100 * {(4 - 0.25) ÷ (5 - 0.25)} = 100*(3.75÷ 4.75) = 78.95

(d) Once the residual maturity of the CDS contract reaches three months, protection ceases to be recognised.

130. Internal hedges and other prudential requirements

(1) A bank can use CDS contracts to hedge against the credit risk in its existing corporate bonds portfolios. A bank can hedge a banking book credit risk exposure either by an internal hedge (the protection purchased from the trading desk of the bank and held in the trading book) or an external hedge (protection purchased from an eligible third-party protection provider). When a bank hedges a banking book credit risk exposure (corporate bonds) using a CDS booked in its trading book (i.e., using an internal hedge), the banking book exposure is not deemed to be hedged for capital purposes unless the bank transfers the credit risk from the trading book to an eligible third-party protection provider through a CDS meeting the requirements of paragraph 128 vis-à-vis the banking book exposure. Where such third-party protection is purchased and is recognised as a hedge of a banking book exposure for regulatory capital purposes, no capital is required to be maintained on internal and external CDS hedge. In such cases, the external CDS will act as indirect hedge for the banking book exposure and the capital adequacy in terms of paragraph 129, as applicable for external / third party hedges, shall be applicable.

(2) General Provisions Requirements

At present, general provisions (standard asset provisions) are required only for Loans and Advances and the positive marked-to-market values of derivatives contracts. For all CDS positions including the hedged positions, both in the Banking Book and Trading Book, banks should hold general provisions for gross positive marked-to-market values of the CDS contracts.

(3) Prudential Treatment Post-Credit Event

(i) Protection Buyer

In case the credit event payment is not received within the period as stipulated in the CDS contract, the protection buyer shall ignore the credit protection of the CDS and reckon the credit exposure on the underlying asset and maintain appropriate level of capital and provisions as warranted for the exposure. On receipt of the credit event payment, (a) the underlying asset shall be removed from the books if it has been delivered to the protection seller or (b) the book value of the underlying asset shall be reduced to the extent of credit event payment received if the credit event payment does not fully cover the book value of the underlying asset and appropriate provisions shall be maintained for the reduced value.

(ii) Protection Seller

(a) From the date of credit event and until the credit event payment in accordance with the CDS contract, the protection seller shall debit the Profit and Loss account and recognise a liability to pay to the protection buyer, for an amount equal to fair value of the contract (notional of credit protection less expected recovery value). In case, the fair value of the deliverable obligation (in case of physical settlement) / reference obligation (in case of cash settlement) is not available after the date of the credit event, then until the time that value is available, the protection seller should debit the Profit and Loss account for the full amount of the protection sold and recognise a liability to pay to the protection buyer equal to that amount.

(b) In case of physical settlement, after the credit event payment, the protection seller shall recognise the assets received, if any, from the protection buyer at the fair value. These investments will be classified as non-performing investments and valued in terms of Reserve Bank of India (Commercial Banks – Classification, Valuation and Operation of Investment Portfolio) Directions, 2025. Thereafter, the protection seller shall subject these assets to the appropriate prudential treatment as applicable to corporate bonds.

(4) Exposure Norms

(i) For the present, the CDS is primarily intended to provide an avenue to investors for hedging credit risk in the corporate bonds, after they have invested in the bonds. It should, therefore, not be used as a substitute for a bank guarantee. Accordingly, a bank should not sell credit protection by writing a CDS on a corporate bond on the date of its issuance in the primary market or undertake, before or at the time of issuance of the bonds, to write such protection in future.

Explanation – As per extant instructions issued by RBI, banks are not permitted to guarantee the repayment of principal and/or interest due on corporate bonds. Considering this restriction, writing credit protection through CDS on a corporate bond on the date of its issuance or undertaking, before or at the time of issuance, to write such protection in future, will be deemed to be a violation of the said instructions.

(ii) Exposure on account of all CDS contracts will be aggregated and combined with other on-balance sheet and off-balance sheet exposures against the reference entity for the purpose of complying with the exposure norms.

(iii) Protection Seller

(a) A protection seller will recognise an exposure to the reference entity of the CDS contract equal to the amount of credit protection sold, subject to the provision in (b) below.

(b) If a market maker has two completely identical opposite positions in CDS forming a hedged position which qualifies for capital adequacy treatment in terms of paragraph 202(1), no exposure would be reckoned against the reference entity.

(c) Protection seller will also recognise an exposure to the counterparty equal to the total credit exposure calculated under Current Exposure Method as prescribed in Basel II framework in the case of all CDS positions held in the Trading book.

(iv) Protection Buyer

(a) In respect of obligations hedged in the banking book as indicated in paragraph 129 and trading book as indicated in paragraph 202(2), the protection buyer will not reckon any exposure on the reference entity. The exposure will be deemed to have been transferred on the protection seller to the extent of protection available.

(b) In all other cases where the obligations in banking book or trading book are hedged by CDS positions, the protection buyer will continue to reckon the exposure on the reference entity equal to the outstanding position of the underlying asset.

(c) For all bought CDS positions (hedged and un-hedged) held in trading book, the protection buyer will also reckon exposure on the counterparties to the CDS contracts as measured by the Current Exposure Method.

(d) The protection buyer needs to adhere to all the criteria required for transferring the exposures fully to the protection seller in terms of (a) above on an on-going basis so as to qualify for exposure relief on the underlying asset. In case any of these criteria are not met subsequently, the bank will have to reckon the exposure on the underlying asset. Therefore, banks should restrict the total exposure to an obligor including that covered by way of various unfunded credit protections (guarantees, LCs, standby LCs, CDS, etc.) within an internal exposure ceiling considered appropriate by the Board of the bank in such a way that it does not breach the single / group borrower exposure limit prescribed by the RBI. In case of the event of any breach in the single / group borrower exposure limit, the entire exposure in excess of the limit will be risk weighted at 1250%. In order to ensure that consequent upon such a treatment, the bank does not breach the minimum capital requirement prescribed by the RBI, it should keep sufficient cushion in capital in case it assumes exposures in excess of normal exposure limit.

(e) In respect of bought CDS positions held in trading book which are not meant for hedging, the protection buyer will not reckon any exposure against the reference entity.

(5) Reporting requirements

Banks should report “total exposure” in all cases where they have assumed exposures against borrowers in excess of the normal single / group exposure limits due to the credit protections obtained by them through CDS, guarantees or any other instruments of credit risk transfer, to the Department of Supervision (DOS) on a quarterly basis.

B External credit assessments

B.1 Eligible credit rating agencies

131. In line with the provisions of the Revised Framework (Document 'International Convergence of Capital Measurement and Capital Standards' June 2006 released by the Basel Committee on Banking Supervision), where the facility provided by the bank possesses rating assigned by an eligible credit rating agency, the risk weight of the claim shall be based on this rating. A bank may use the ratings of the following domestic credit rating agencies (arranged in alphabetical order) for the purposes of risk weighting its claims for capital adequacy purposes:

    (i) Acuite Ratings & Research Limited (Acuite)

    (ii) Brickwork Ratings India Private Limited

    (iii) CARE Ratings Limited;

    (iv) CRISIL Ratings Limited;

    (v) ICRA Limited;

    (vi) India Ratings and Research Private Limited (India Ratings); and

    (vii) INFOMERICS Valuation and Rating Limited (INFOMERICS).

132. A bank may also use the ratings of the following international credit rating agencies (arranged in alphabetical order) for the purposes of risk weighting its claims for capital adequacy purposes where specified:

    (i) CareEdge Global IFSC Limited (for non-resident corporate exposures originating at International Financial Services Centre(IFSC));

    (ii) Fitch;

    (iii) Moody's; and

    (iv) Standard & Poor's.

B.2 Scope of application of external ratings

133. A bank shall use the chosen credit rating agency and its ratings consistently for each type of claim, for both risk weighting and risk management purposes. A bank shall not 'cherry pick' the assessments provided by different credit rating

agencies and arbitrarily change the use of credit rating agency. If a bank has decided to use the ratings of some of the chosen credit rating agency for a given type of claim, it can use only the ratings of that credit rating agency, despite the fact that some of these claims may also be rated by other credit rating agency whose ratings the bank has decided not to use. A bank shall not use one agency's rating for one corporate bond, while using another agency's rating for another exposure to the same counterparty, unless the respective exposures are rated by only one of the chosen credit rating agency, whose ratings the bank has decided to use. External assessments for one entity within a corporate group shall not be used to risk weight other entities within the same group.

134. A bank shall disclose the name of the credit rating agency that it uses for the risk weighting of its assets, the risk weights associated with the particular rating grades as determined by the Reserve Bank through the mapping process for each eligible credit rating agency as well as the aggregated RWA as required vide **Table DF-4 of Annex III**.

135. To be eligible for risk-weighting purposes, the external credit assessment shall take into account and reflect the entire amount of credit risk exposure the bank has with regard to all payments owed to it. For example, if a bank is owed both principal and interest, the assessment shall fully take into account and reflect the credit risk associated with timely repayment of both principal and interest.

136. To be eligible for risk weighting purposes, the rating shall be in force and confirmed from the monthly bulletin of the concerned rating agency. The rating agency should have reviewed the rating at least once during the previous 15 months.

137. An eligible credit assessment shall be publicly available i.e., a rating shall be published in an accessible form and included in the external credit rating agency's transition matrix. Consequently, a rating that is made available only to the parties to a transaction shall not satisfy this requirement.

138. For an asset in a bank's portfolio that has contractual maturity less than or equal to one-year, short term ratings accorded by the chosen credit rating agency shall be relevant. For other asset which has a contractual maturity of more than one-

year, long term ratings accorded by the chosen credit rating agency shall be relevant.

139. Cash credit exposure, even though sanctioned for period of one year or less, shall be reckoned as long-term exposures and accordingly the long-term ratings accorded by the chosen credit rating agency shall be relevant. Similarly, a bank may use long-term ratings of a counterparty as a proxy for an unrated short-term exposure on the same counterparty subject to strict compliance with the requirements for use of multiple rating assessments and applicability of issue rating to issuer / other claims as indicated in paragraphs 141 to 143, 144 to 149, 151 and 152 to 153 below.

B.3 Mapping process

140. This Capital Framework recommends development of a mapping process to assign the ratings issued by eligible credit rating agencies to the risk weights available under the Standardised risk weighting framework. The mapping process is required to result in a risk weight assignment consistent with that of the level of credit risk. A mapping of the credit ratings awarded by the chosen domestic credit rating agency has been furnished below in paragraphs 141 and 147, which shall be used by a bank in assigning risk weights to the various exposures.

B.4 Long term ratings

141. The rating-risk weight mapping furnished in the Table 25 below shall be adopted by a bank in India:

Table 25: Risk weight mapping of long-term ratings of the chosen domestic rating agencies

CARE	CRISIL Ratings Limited	India Ratings	ICRA	Brickwork	Acuite	INFOMERICS	Standardised approach risk weights (in per cent)
CARE AAA	CRISIL AAA	IND AAA	ICRA AAA	Brickwork AAA	Acuité AAA	IVR AAA	20
CARE AA	CRISIL AA	IND AA	ICRA AA	Brickwork AA	Acuité AA	IVR AA	30
CARE A	CRISIL A	IND A	ICRA A	Brickwork A	Acuité A	IVR A	50
CARE BBB	CRISIL BBB	IND BBB	ICRA BBB	Brickwork BBB	Acuité BBB	IVR BBB	100

CARE	CRISIL Ratings Limited	India Ratings	ICRA	Brickwork	Acuite	INFOMERICS	Standardised approach risk weights (in per cent)
CARE BB, CARE B, CARE C & CARE D	CRISIL BB, CRISIL B, CRISIL C & CRISIL D	IND BB, IND B, IND C & IND D	ICRA BB, ICRA B, ICRA C & ICRA D	Brickwork BB, Brickwork B, Brickwork C & Brickwork D	Acuité BB, Acuité B, Acuité C & Acuité D	IVR BB, IVR B, IVR C & IVR D	150
Unrated	Unrated	Unrated	Unrated	Unrated	Unrated	Unrated	100 [$]

[$] The risk weight shall be 150 per cent in the following two cases:

(i) if the aggregate exposure from banking system is more than ₹200 crore

(ii) if the aggregate exposure from banking system is more than ₹100 crore for exposures which were rated earlier and subsequently have become unrated.

142. Where '+' or '-' notation is attached to the rating, the corresponding main rating category risk weight shall be used. For example, A+ or A- shall be considered to be in the A rating category and assigned 50 per cent risk weight.

143. If an issuer has a long-term exposure with an external long-term rating that warrants a risk weight of 150 per cent, all unrated claims on the same counter-party, whether short-term or long-term, shall also receive a 150 per cent risk weight, unless the bank uses recognised credit risk mitigation techniques for such claims.

B.5 Short term ratings

144. For risk-weighting purposes, short-term ratings shall be deemed to be issue-specific. They shall be used to derive risk weights for claims arising from the rated facility. They shall not be generalised to other short-term claims. In no event a short-term rating shall be used to support a risk weight for an unrated long-term claim. Short-term assessments may only be used for short-term claims against banks and corporates.

145. Notwithstanding the above restriction on using an issue specific short-term rating for other short-term exposures, the following broad principles shall apply. The unrated short-term claim on counterparty shall attract a risk weight of at least one level higher than the risk weight applicable to the rated short-term claim on that counterparty. If a short-term rated facility to counterparty attracts a 20 per cent or a 50 per cent risk-weight, unrated short-term claims to the same counterparty shall not attract a risk weight lower than 30 per cent or 100 per cent respectively.

146. Similarly, if an issuer has a short-term exposure with an external short-term rating that warrants a risk weight of 150 per cent, all unrated claims on the same counter-party, whether long-term or short-term, shall also receive a 150 per cent risk weight, unless the bank uses recognised credit risk mitigation techniques for such claims.

147. In respect of the issue specific short-term ratings the following risk weight mapping shall be adopted by a bank:

Table 26: Risk weight mapping of short-term ratings of domestic rating agencies

CARE	CRISIL Ratings Limited	India Ratings	ICRA	Brickwork	Acuite	INFOMERICS	Standardised approach risk weights (in per cent)
CARE A1+	CRISIL A1+	IND A1+	ICRA A1+	Brickwork A1+	Acuité A1+	IVR A1+	20
CARE A1	CRISIL A1	IND A1	ICRA A1	Brickwork A1	Acuité A1	IVR A1	30
CARE A2	CRISIL A2	IND A2	ICRA A2	Brickwork A2	Acuité A2	IVR A2	50
CARE A3	CRISIL A3	IND A3	ICRA A3	Brickwork A3	Acuité A3	IVR A3	100
CARE A4 & D	CRISIL A4 & D	IND A4 & D	ICRA A4 & D	Brickwork A4 & D	Acuité A4 & D	IVR A4 and D	150
Unrated	Unrated	Unrated	Unrated	Unrated	Unrated	Unrated	100[$]

[$]The risk weight is 150% in the following two cases:

(i) if the aggregate exposure from banking system is more than ₹ 200 crore

(ii) if the aggregate exposure from banking system is more than ₹ 100 crore for exposures which were rated earlier and subsequently have become unrated.

148. Where '+' or '-' notation is attached to the rating, the corresponding main rating category risk weight should be used for A2 and below, unless specified otherwise. For example, A2+ or A2- would be considered to be in the A2 rating category and assigned 50 per cent risk weight.

149. The above risk weight mapping of both long term and short-term ratings of the chosen domestic rating agencies shall be reviewed annually by the Reserve Bank.

B.6 Use of unsolicited ratings

150. A rating shall be treated as solicited only if the issuer of the instrument has requested the credit rating agency for the rating and has accepted the rating assigned by the agency. A bank shall use only solicited rating from the chosen credit rating agencies**.** No ratings issued by the credit rating agency on an

unsolicited basis shall be considered for risk weight calculation as per the Standardised Approach.

B.7 Use of multiple rating assessments

151. A bank shall be guided by the following in respect of exposures / obligors having multiple ratings from the chosen credit rating agency chosen by the bank for the purpose of risk weight calculation:

(i) If there is only one rating by a chosen credit rating agency for a particular claim, that rating shall be used to determine the risk weight of the claim.

(ii) If there are two ratings accorded by chosen credit rating agencies that map into different risk weights, the higher risk weight shall be applied.

(iii) If there are three or more ratings accorded by chosen credit rating agencies with different risk weights, the ratings corresponding to the two lowest risk weights shall be referred to and the higher of those two risk weights shall be applied. i.e., the second lowest risk weight.

B.8 Applicability of 'issue rating' to issuer / other claims

152. Where a bank invests in a particular issue that has an issue specific rating by a chosen credit rating agency the risk weight of the claim shall be based on this assessment. Where the bank's claim is not an investment in a specific assessed issue, the following general principles shall apply:

(i) In circumstances where the borrower has a specific assessment for an issued debt - but the bank's claim is not an investment in this particular debt - the rating applicable to the specific debt (where the rating maps into a risk weight lower than that which applies to an unrated claim) may be applied to the bank's unassessed claim only if this claim ranks *pari passu* or senior to the specific rated debt in all respects and the maturity of the unassessed claim is not later than the maturity of the rated claim, except where the rated claim is a short term obligation as specified in paragraph 145. If not, the rating applicable to the specific debt can not be used and the unassessed claim shall receive the risk weight for unrated claims.

Illustration: In a case where a short-term claim on a counterparty is rated as A1+ and a long-term claim on the same counterparty is rated as AAA,

then a bank shall assign a 30 per cent risk weight to an unrated short-term claim and 20 per cent risk weight to an unrated long-term claim on that counterparty where the seniority of the claim ranks pari-passu with the rated claims and the maturity of the unrated claim is not later than the rated claim. In a similar case where a short-term claim is rated A1+ and a long-term claim is rated A, the bank shall assign 50 per cent risk weight to an unrated short term or long-term claim.

(ii) The Reserve Bank had advised the ECAIs vide a letter dated June 4, 2021 to disclose the name of the banks and the corresponding credit facilities rated by them in the press release issued on rating actions by August 31, 2021, after obtaining requisite consent from the borrowers. A loan rating without the above disclosure by the ECAI shall not be eligible for being reckoned for capital computation by a bank. A bank shall treat such exposures as unrated and assign applicable risk weights in terms of paragraph 47.

Illustration: Illustratively, a scenario may be assumed, where a borrower has availed credit facilities from banks A, B and C and external rating from an ECAI is obtained only in respect of the credit facility extended by the bank A. If the ECAI has disclosed the name of bank A and the corresponding credit facility rated by it, then bank A can reckon the said rating for risk weighting purpose. Banks B and C are permitted to derive risk weights for their respective unrated credit facilities subject to conditions stated in paragraph 152(i) , as permitted hitherto. In the event of ECAI not making the above disclosure, none of the banks shall reckon the said rating, and therefore shall apply risk weights of 100 percent or 150 percent as applicable in terms of extant instructions.

(iii) In circumstances where the borrower has an issuer assessment, this assessment typically applies to senior unsecured claims on that issuer. Consequently, only senior claims on that issuer shall benefit from a high-quality issuer assessment. Other unassessed claims of a highly assessed issuer shall be treated as unrated. If either the issuer or a single issue has a low-quality assessment (mapping into a risk weight equal to or higher than that which applies to unrated claims), an unassessed claim on the same

counterparty that ranks pari-passu or is subordinated to either the senior unsecured issuer assessment or the exposure assessment shall be assigned the same risk weight as is applicable to the low-quality assessment.

(iv) Where a bank intends to extend an issuer or an issue specific rating assigned by a chosen credit rating agency to any other exposure which the bank has on the same counterparty and which meets the above criterion, it shall be extended to the entire amount of credit risk exposure the bank has with regard to that exposure i.e., both principal and interest.

(v) With a view to avoiding any double counting of credit enhancement factors, no recognition of credit risk mitigation techniques shall be taken into account if the credit enhancement is already reflected in the issue specific rating accorded by a chosen credit rating agency relied upon by the bank.

(vi) Where unrated exposures are risk weighted based on the rating of an equivalent exposure to that borrower, foreign currency ratings shall be used only for exposures in foreign currency.

153. If the conditions indicated in paragraph 152 above are not satisfied, the rating applicable to the specific debt cannot be used and the claims on NABARD / SIDBI / NHB / MUDRA Ltd. on account of deposits placed in lieu of shortfall in achievement of priority sector lending targets / sub-targets shall be risk weighted as applicable for unrated claims, i.e., 100 per cent.

C Credit risk mitigation

C.1 General principles

154. Credit risk mitigation (CRM) approaches as detailed herein shall be applicable to the banking book exposures of a bank. These shall also be applicable for calculation of the counterparty risk charges for OTC derivatives and repo-style transactions booked in the trading book.

155. The general principles applicable to use of CRM techniques are as under:

(i) No transaction in which CRM techniques are used shall receive a higher capital requirement than an otherwise identical transaction where such techniques are not used.

(ii) The effects of CRM shall not be double counted. Therefore, no additional supervisory recognition of CRM for regulatory capital purposes shall be granted on claims for which an issue-specific rating is used that already reflects that CRM.

(iii) Principal-only ratings shall not be allowed within the CRM framework.

(iv) While the use of CRM techniques reduces or transfers credit risk, it simultaneously may increase other risks (residual risks). Residual risks include legal, operational, liquidity and market risks. Therefore, it is imperative that a bank employ robust procedures and processes to control these risks, including strategy, consideration of the underlying credit, valuation, policies and procedures, systems, control of roll-off risks, and management of concentration risk arising from the bank's use of CRM techniques and its interaction with the bank's overall credit risk profile. Where these risks are not adequately controlled, the Reserve Bank may impose additional capital charges or take other supervisory actions. The disclosure requirements prescribed in **Table DF-5 of** Annex III shall also be observed for a bank to obtain capital relief in respect of any CRM techniques.

C.2 Legal certainty

156. In order for a bank to obtain capital relief for any use of CRM techniques, the following minimum standards for legal documentation shall be met. All documentation used in collateralised transactions and guarantees shall be binding on all parties and legally enforceable in all relevant jurisdictions. A bank shall have conducted sufficient legal review, which shall be well documented, to verify this requirement. Such verification shall have a well-founded legal basis for reaching the conclusion about the binding nature and enforceability of the documents. A bank shall also undertake such further review as necessary to ensure continuing enforceability.

C.3 Credit risk mitigation (CRM) techniques - collateralised transactions

157. A collateralised transaction is one in which:

(1) a bank has a credit exposure, and that credit exposure is hedged in whole or in part by collateral posted by a counterparty or by a third party on behalf of the

counterparty. Here, 'counterparty' is used to denote a party to whom a bank has an on- or off-balance sheet credit exposure.

(2) a bank has a specific lien on the collateral and the requirements of legal certainty are met.

Overall framework and minimum conditions

158. There are two approaches under the Basel framework – the simple approach and the comprehensive approach. A bank in India shall adopt the comprehensive approach, which allows fuller offset of collateral against exposures, by effectively reducing the exposure amount by the value ascribed to the collateral. Under this approach, a bank, which take eligible financial collateral (e.g., cash or securities, more specifically defined below), is allowed to reduce its credit exposure to a counterparty when calculating its capital requirements to take account of the risk mitigating effect of the collateral. CRM is allowed only on an account-by-account basis, even within regulatory retail portfolio. However, the following standards shall be met before capital relief is granted:

(1) In addition to the general requirements for legal certainty, the legal mechanism by which collateral is pledged or transferred shall ensure that the bank has the right to liquidate or take legal possession of it, in a timely manner, in the event of the default, insolvency or bankruptcy (or one or more otherwise-defined credit events set out in the transaction documentation) of the counterparty (and, where applicable, of the custodian holding the collateral). Further, a bank shall take all steps necessary to fulfill those requirements under the law applicable to the bank's interest in the collateral for obtaining and maintaining an enforceable security interest, e.g., by registering it with a registrar.

(2) For collateral to provide protection, the credit quality of the counterparty and the value of the collateral shall not have a material positive correlation.

Explanation – securities issued by the counterparty or by any related group entity would provide little protection and so would be ineligible.

(3) A bank shall have clear and robust procedures for the timely liquidation of collateral to ensure that any legal conditions required for declaring the default of the counterparty and liquidating the collateral are observed, and that collateral can be liquidated promptly.

(4) Where the collateral is held by a custodian, a bank shall take reasonable steps to ensure that the custodian segregates the collateral from its own assets.

(5) A bank shall ensure that sufficient resources are devoted to the orderly operation of margin agreements with OTC derivative and securities-financing counterparties banks, as measured by the timeliness and accuracy of its outgoing calls and response time to incoming calls. A bank shall have collateral management policies in place to control, monitor and report the following to the Board or one of its committees:

(i) the risk to which margin agreements exposes them (such as the volatility and liquidity of the securities exchanged as collateral);

(ii) the concentration risk to particular types of collateral;

(iii) the reuse of collateral (both cash and non-cash) including the potential liquidity shortfalls resulting from the reuse of collateral received from counterparties; and

(iv) the surrender of rights on collateral posted to counterparties.

159. A capital requirement shall be applied to a bank on either side of the collateralised transaction : for example, both repos and reverse repos shall be subject to capital requirements. Likewise, both sides of securities lending and borrowing transactions shall be subject to explicit capital charges, as shall the posting of securities in connection with a derivative exposure or other borrowing.

160. The comprehensive approach

(1) A bank shall need to calculate its adjusted exposure to a counterparty for capital adequacy purposes in order to take account of the effects of the collateral taken. The bank shall adjust both, the amount of the exposure to the counterparty and the value of any collateral received in support of that counterparty, to account for possible future fluctuations in the value of either, occasioned by market movements. These adjustments are referred to as ‘haircuts’. The application of haircuts shall give volatility adjusted amounts for both – exposure and collateral. The volatility adjusted amount for the exposure shall be higher than the exposure and the volatility adjusted amount for the collateral shall be lower than the collateral, unless either side of the transaction is cash. Therefore, the ‘haircut’ for the exposure shall be a premium factor and the ‘haircut’ for the collateral shall

be a discount factor. Since the value of credit exposures acquired by a bank in the course of its banking operations would not be subject to market volatility, (as the loan disbursal / investment shall be a 'cash' transaction) haircut on such exposures shall not be applicable, though the haircut stipulated in **Table 27** shall apply only to the eligible collateral of the bank. On the other hand, exposures of a bank, arising out of repo-style transactions shall require upward adjustment for volatility, as the value of security sold / lent / pledged in the repo transaction, shall be subjected to market volatility. Hence, such exposures shall attract haircut.

(2) Additionally, where the exposure and collateral are held in different currencies an additional downwards adjustment shall be made to the volatility adjusted collateral amount to take account of possible future fluctuations in exchange rates.

(3) Where the volatility-adjusted exposure amount is greater than the volatility-adjusted collateral amount (including additional adjustment for foreign exchange risk), a bank shall calculate its RWA as the difference between the two multiplied by the risk weight of the counterparty. The framework for performing calculations of capital requirement is indicated in paragraph 162.

161. Eligible financial collateral

The following collateral instruments are eligible for recognition in the comprehensive approach:

(i) Cash (as well as certificates of deposit or comparable instruments, including fixed deposit receipts, issued by the lending bank) on deposit with the bank which is incurring the counterparty exposure.

(ii) Gold including both bullion and jewellery. However, the value of the collateralised jewellery should be arrived at after notionally converting these to 99.99 purity.

(iii) Securities issued by Central and State Governments.

(iv) Kisan Vikas Patra and National Savings Certificates provided no lock-in period is operational and if they can be encashed within the holding period.

(v) Life insurance policies with a declared surrender value of an insurance company which is regulated by an insurance sector regulator.

(vi) Debt securities rated by a chosen credit rating agency in respect of which a bank should be sufficiently confident about the market liquidity where these are either:

(a) Attracting 100 per cent or lesser risk weight, i.e., rated at least BBB(-) when issued by public sector entities and other entities (including banks and Primary Dealers); or

(b) Attracting 100 per cent or lesser risk weight, i.e., rated at least CARE A3 / CRISIL A3 / India Ratings and Research Private Limited (India Ratings) A3 / ICRA A3 / Brickwork A3 / Acuite A3 / IVR A3 (INFOMERICS) for short-term debt instruments.

Explanation - A debenture would meet the test of liquidity if it is traded on a recognised stock exchange(s) on at least 90 per cent of the trading days during the preceding 365 days. Further, liquidity can be evidenced in the trading during the previous one month in the recognised stock exchange if there are a minimum of 25 trades of marketable lots in securities of each issuer.

(vii) Debt securities not rated by a chosen credit rating agency in respect of which a bank should be sufficiently confident about the market liquidity where these are:

(a) issued by a bank;

(b) listed on a recognised exchange;

(c) classified as senior debt;

(d) all rated issues of the same seniority by the issuing bank are rated at least BBB (-) or CARE A3 / CRISIL A3 / India Ratings and Research Private Limited (India Ratings) A3 / ICRA A3 / Brickwork A3 / Acuite A3 / IVR A3 (INFOMERICS) by a chosen credit rating agency;

(e) the bank holding the securities as collateral has no information to suggest that the issue justifies a rating below BBB(-) or CARE A3 / CRISIL A3 / India Ratings and Research Private Limited (India

Ratings) A3 / ICRA A3 / Brickwork A3 / Acuite A3 / IVR A3 (INFOMERICS) (as applicable); and

(f) A bank should be sufficiently confident about the market liquidity of the security.

(viii) Units of mutual funds regulated by the securities regulator of the jurisdiction of the bank's operation mutual funds where:

(a) a price for the units is publicly quoted daily, i.e., where the daily NAV is available in public domain; and

(b) the mutual fund is limited to investing in the instruments listed in this paragraph.

(ix) Re-securitisations, irrespective of any credit ratings, are not eligible financial collateral.

(x) For foreign bank branches, cash / unencumbered approved securities, the source of which is interest-free funds from Head Office or remittable surplus retained in Indian books, held with the Reserve Bank under section 11(2)(b)(i) of the BR Act,1949, may be reckoned as CRM, for offsetting the gross exposure of the foreign bank branches in India to the Head Office (including overseas branches) for non-centrally cleared derivative transactions, subject to the following conditions:

(a) The amount so held shall be over and above the other regulatory and statutory requirements and shall be certified by the statutory auditors.

(b) The amount so held shall not be included in regulatory capital. (i.e., no double counting of the fund placed under Section 11(2) as both capital and CRM). Accordingly, while assessing the capital adequacy of a bank, the amount will form part of regulatory adjustments made to Common Equity Tier 1 Capital.

(c) The bank shall furnish an undertaking as on March 31 every year to the Department of Supervision (DoS), Reserve Bank of India, that the balance reckoned as CRM for the purpose will be maintained on a continuous basis.

(d) The CRM shall be compliant with the other principles / conditions prescribed in this Master Direction.

Excess amount over and above the CRM requirements shall be permitted to be withdrawn subject to certification by the Statutory Auditor and approval of the Department of Supervision (DoS), Reserve Bank of India.

162. Calculation of capital requirement

(1) For a collateralised transaction, the exposure amount after risk mitigation shall be calculated as follows:

$$E^* = \max \{0, [E \times (1 + H_e) - C \times (1 - H_c - H_{fx})]\}$$

where:

E^* = the exposure value after risk mitigation

E = current value of the exposure for which the collateral qualifies as a risk mitigant

H_e = haircut appropriate to the exposure

C = the current value of the collateral received

H_c = haircut appropriate to the collateral

H_{fx} = haircut appropriate for currency mismatch between the collateral and exposure

(2) The exposure amount after risk mitigation (i.e., E^*) shall be multiplied by the risk weight of the counterparty to obtain the RWA amount for the collateralised transaction.

(3) Illustrative examples for calculation of exposure amount for collateralised transactions is as under.

Sl. No.	Particulars	Case I	Case 2	Case 3	Case 4	Case 5
(1)	(2)	(3)	(4)	(5)	(6)	(7)
1	Exposure	100	100	100	100	100
2	Maturity of the exposure	2	3	6	3	3
3	Nature of the exposure	Corporate Loan	Corporate Loan	Corporate Loan	Corporate Loan	Corporate Loan
4	Currency	INR	INR	USD	INR	INR
5	Exposure in rupees	100	100	4000 (Row 1 x exch. rate[##])	100	100

Sl. No.	Particulars	Case I	Case 2	Case 3	Case 4	Case 5
(1)	(2)	(3)	(4)	(5)	(6)	(7)
6	Rating of exposure	BB	A	BBB-	AA	B-
	Applicable Risk weight	150	50	100@	30	150
7	Haircut for exposure*	0	0	0	0	0
8	Collateral	100	100	4000	2	100
9	Currency	INR	INR	INR	USD	INR
10	Collateral (in ₹)	100	100	4000	80 (Row 1 x Exch. Rate)	100
11	Residual maturity of collateral (years)	2	3	6	3	5
12	Nature of collateral	Sovereign (GoI) Security	Bank Bonds	Corporate Bonds	Foreign Corporate Bonds	Units of Mutual Funds
13	Rating of Collateral	NA	Unrated	BBB	AAA (S & P)	AA
14	Haircut for collateral (%)	0.02	0.06	0.12	0.04	0.08
15	Haircut for currency mismatches (%) [cf. paragraph 163(5)]	0	0	0.08	0.08	0
16	Total Haircut on collateral [Row 10 x (row 14+15)]	2	6	800	9.6	8.0
17	Collateral after haircut (Row 10 - Row 16)	98	94	3200	70.4	92
18	Net Exposure (Row 5 – Row 17)	2	6	800	29.6	8
19	Risk weight (%)	150	50	100@	30	150
20	RWA (Row 18 x 19)	3	3	800	8.88	12

##Exchange rate assumed to be 1 USD = ₹40

#Not applicable

@In case of long-term ratings, as per paragraph 142, where '+' or '-' notation is attached to the rating, the corresponding main rating category risk weight is to be used. Hence risk weight is 100 per cent.

*Haircut for exposure is taken as zero because the loans are not marked to market and hence are not volatile

Case 4: Haircut applicable as per Table 27

Case 5: It is assumed that the Mutual Fund meets the criteria specified in paragraph 161 and has investments in the securities all of which have residual maturity of more than five years are rated AA and above – which would attract a haircut of eight per cent in terms of Table 27.

(4) Illustration on computation of capital charge for Counterparty Credit Risk (CCR) – repo transactions is as under.

Let us assume the following parameters of a hypothetical repo transaction:

Type of the Security	GOI security
Residual Maturity	5 years
Coupon	6 %
Current Market Value	₹1050
Cash borrowed	₹1000
Modified Duration of the security	4.5 years
Assumed frequency of margining	Daily
Haircut for security	2%
Haircut on cash	Zero
Minimum holding period	5 business-days
Change in yield for computing the capital charge for general market risk	0.7 % p.a. (Cf. Zone 3 in Table 35)

Computation of total capital charge comprising the capital charge for CCR and Credit / Market risk for the underlying security:

In the books of the borrower of funds (for the off-balance sheet exposure due to lending of the security under repo) -

(In this case, the security lent is the exposure of the security lender while cash borrowed is the collateral)

Sr. No.	Items	Particulars	Amount (in ₹)
A.	**Capital Charge for CCR**		
1.	Exposure	MV of the security	1050
2.	CCF for Exposure	100 %	
3.	On-Balance Sheet Credit Equivalent	1050 * 100 %	1050
4.	Haircut	1.4 % @	
5.	Exposure adjusted for haircut as per Table 27	1050 * 1.014	1064.70
6.	Collateral for the security lent	Cash	1000

Sr. No.	Items	Particulars	Amount (in ₹)
7.	Haircut for exposure	0 %	
8.	Collateral adjusted for haircut	1000 * 1.00	1000
9.	Net Exposure (5- 8)	1064.70 – 1000	64.70
10.	Risk weight (for a Scheduled CRAR-compliant bank)	20 %	
11.	Risk weighted assets for CCR (9 x 10)	64.70 * 20 %	12.94
12.	Capital Charge for CCR (11 x 9%)	12.94 * 0.09	1.16
B.	**Capital for Credit / market Risk of the security**		
1.	Capital for credit risk (if the security is held under banking book)	Credit risk	Zero (Being Government security)
2.	Capital for market risk (if the security is held under trading book)	Specific Risk	Zero (Being Government security)
		General Market Risk (0.7 % * 1050) {Assumed yield change (%) * market value of security} ^	7.35
Total capital required (for CCR + credit risk + specific risk + general market risk)			8.51

@The supervisory haircut of 2 per cent has been scaled down using the formula indicated in paragraph 163.

^For the purpose of computation of general market risk, vertical and horizontal disallowances have been ignored.

In the books of the lender of funds (for the on-balance sheet exposure due to lending of funds under repo) -

(In this case, the cash lent is the exposure and the security borrowed is collateral)

Sr. No	**Items**	**Particulars**	**Amount (in ₹)**
A.	Capital Charge for CCR		
1.	Exposure	Cash	1000
2.	Haircut for exposure	0 %	
3.	Exposure adjusted for haircut as per Table 27	1000 * 1.00	1000
4.	Collateral for the cash lent	Market value of the security	1050

Sr. No	Items	Particulars	Amount (in ₹)
5.	Haircut for collateral	1.4 % @	
6.	Collateral adjusted for haircut	1050 * 0.986	1035.30
7.	Net Exposure (3 - 6)	Max {1000 -1035.30}	0
8.	Risk weight (for a Scheduled CRAR-compliant bank)	20 %	
9.	Risk weighted assets for CCR (7 x 8)	0 * 20 %	0
10.	Capital Charge for CCR	0	0
B.	Capital for Credit / market Risk of the security		
1.	Capital for credit risk (if the security is held under banking book)	Credit Risk	Not applicable, as it is maintained by the borrower of funds
2.	Capital for market risk (if the security is held under trading book)	Specific Risk	Not applicable, as it is maintained by the borrower of funds
		General Market Risk	Not applicable, as it is maintained by the borrower of funds

@The supervisory haircut of 2 per cent has been scaled down using the formula indicated in paragraph 163

163. Haircuts

(1) A bank in India shall use only the standard supervisory haircuts prescribed in these Directions for both the exposure as well as the collateral. The haircuts (assuming daily mark-to-market, daily re-margining and a 10 business-day holding period), expressed as percentages, shall be as furnished in Table 27.

Explanation - Holding period shall be the time normally required by the bank to realise the value of the collateral.

(2) The ratings indicated in Table 27 represent the ratings assigned by the domestic rating agencies. In the case of exposures toward debt securities issued by foreign sovereigns and foreign corporates, the haircut may be based on ratings of the international rating agencies, as indicated in Table 28.

(3) Sovereign shall include the Reserve Bank and DICGC which are eligible for zero per cent risk weight. Guarantees issued by CGTMSE, CRGFTLIH and individual schemes under National Credit Guarantee Trustee Company Ltd. (NCGTC)

which are backed by explicit Central Government guarantee shall also be included under Sovereign.

(4) A bank may apply a zero haircut for eligible collateral where it is a National Savings Certificate, Kisan Vikas Patras, surrender value of insurance policies and bank's own deposits.

(5) The standard supervisory haircut for currency risk where exposure and collateral are denominated in different currencies is eight per cent (also based on a 10-business day holding period and daily mark-to-market).

Table 27: Standard supervisory haircuts for sovereign and other securities which constitute exposure and collateral

Sr. No.		Issue rating for debt securities	Residual maturity (in years)	Haircut (in percentage)
A	Securities issued / guaranteed by the Government of India and issued by the State Governments (Sovereign securities)			
	I	Rating not applicable – as Government securities are not currently rated in India	≤ 1 year	0.5
			> 1 year and ≤ 5 years	2
			> 5 years	4
B	Domestic debt securities other than those indicated at Item No. A above including the securities guaranteed by Indian State Governments			
	II	AAA to AA A1	≤ 1 year	1
			> 1 year and ≤ 5 years	4
			> 5 years	8
	III	A to BBB A2, A3 and unrated bank securities as specified in paragraph 161 (vii)	≤ 1 year	2
			> 1 year and ≤ years	6
			> 5 years	12
	IV	Units of Mutual Funds		Highest haircut applicable to any of the above securities, in which the eligible mutual fund {cf. paragraph 161(viii)} can invest
C	Cash in the same currency			0
D	Gold			15

Sr. No.		Issue rating for debt securities	Residual maturity (in years)	Haircut (in percentage)
E	Securitisation Exposures (including those backed by securities issued by foreign sovereigns and foreign corporates)			
	II	AAA to AA	≤ 1 year	2
			> 1 year and ≤ 5 years	8
			> 5 years	16
	III	A to BBB and unrated bank securities as specified in paragraph 161(vii)	≤ 1 year	4
			> 1 year and ≤ years	12
			> 5 years	24

Table 28: Standard supervisory haircut for exposures and collaterals which are obligations of foreign central sovereigns / foreign corporates

Issue rating for debt securities as assigned by international rating agencies	Residual Maturity	Other Issues (%)	Other Issues (%)
AAA to AA / A1	< = 1 year	0.5	1
	> 1 year and < or = 5 years	2	4
	> 5 years	4	8
A to BBB / A2 / A3 and Unrated Bank Securities	< = 1 year	1	2
	> 1 year and < or = 5 years	3	6
	> 5 years	6	12

(6) For transactions in which a bank's exposures are unrated, or the bank lends non-eligible instruments (i.e., non-investment grade corporate securities), the haircut to be applied on the exposure shall be 25 per cent.

(7) Where the collateral is a basket of assets, the haircut on the basket shall be,

$$H = \sum_i a_i H_i$$

where a_i is the weight of the asset (as measured by the amount / value of the asset in units of currency) in the basket and H_i, the haircut applicable to that asset.

(8) Adjustment for different holding periods:

For some transactions, depending on the nature and frequency of the revaluation and remargining provisions, different holding periods (other than 10 business-days) are appropriate. The framework for collateral haircuts distinguishes between repo-style transactions (i.e., repo / reverse repos and securities lending / borrowing), 'other capital-market-driven transactionsy (i.e., OTC derivatives transactions and margin lending) and secured lending. In capital-market-driven transactions and repo-style transactions, the documentation contains remargining clauses; in secured lending transactions, it generally does not. In view of different holding periods, in the case of these transactions, the minimum holding period shall be taken as indicated in table below:

Table 29: Minimum holding period for different transaction types

Transaction type	Minimum holding Period	Condition
Repo-style transaction	five business days	daily remargining
Other capital market transactions	ten business days	daily remargining
Secured lending	twenty business days	daily revaluation

The haircut for the transactions with other than 10 business-days minimum holding period, as indicated above, shall have to be adjusted by scaling up / down the haircut for 10 business–days indicated in the Table 27, as per the formula given in sub-paragraph (10) below.

(9) Adjustment for non-daily mark-to-market or remargining:

In case a transaction has margining frequency different from daily margining assumed, the applicable haircut for the transaction shall also need to be adjusted by using the formula given in sub-paragraph (10).

(10) Formula for adjustment for different holding periods and / or non-daily mark-to-market or remargining: Adjustment for the variation in holding period and margining / mark-to-market, as indicated in sub-paragraphs (8) and (9) above shall be done as per the following formula:

$$H = H_{10}\sqrt{\frac{N_R + (T_M - 1)}{10}}$$

Where;

H = haircut

H_{10} = 10-business-day standard supervisory haircut for instrument

N_R = actual number of business days between remargining for capital market transactions or revaluation for secured transactions.

T_M = minimum holding period for the type of transaction

164. Capital adequacy framework for repo / reverse repo-style transactions

(1) The repo-style transactions also attract capital charge for counterparty credit risk (CCR), in addition to the credit risk and market risk. The CCR is defined as the risk of default by the counterparty in a repo-style transaction, resulting in non-delivery of the security lent / pledged / sold or non-repayment of the cash.

(2) Treatment in the books of the borrower of funds:

(i) Where a bank has borrowed funds by selling / lending or posting, as collateral, of securities, the ‘exposure’ shall be an off-balance sheet exposure equal to the market value of the securities sold / lent as scaled up after applying appropriate haircut. For the purpose, the haircut as per Table 27 shall be used as the basis which shall be applied by using the formula in paragraph 163(10), to reflect minimum (prescribed) holding period of five business-days for repo-style transactions and the variations, if any, in the frequency of re-margining, from the daily margining assumed for the standard supervisory haircut. The 'off-balance sheet exposure' shall be converted into 'on-balance sheet' equivalent by applying a CCF of 100 per cent, as per item 5 in Table 15.

(ii) The amount of money received shall be treated as collateral for the securities lent / sold / pledged. Since the collateral is cash, the haircut for it shall be zero.

(iii) The credit equivalent amount arrived at (a) above, net of amount of cash collateral, shall attract a risk weight as applicable to the counterparty.

(iv) As the securities shall come back to the books of the borrowing bank after the repo period, it shall continue to maintain the capital for the credit risk in the securities in the cases where the securities involved in repo are held under banking book, and capital for market risk in cases where the

securities are held under trading book. The capital charge for credit risk / specific risk shall be determined according to the credit rating of the issuer of the security. In the case of Government securities, the capital charge for credit / specific risk shall be 'zero'.

(3) Treatment in the books of the lender of funds

(i) The amount lent shall be treated as on-balance sheet / funded exposure on the counter party, collateralised by the securities accepted under the repo.

(ii) The exposure, being cash, shall receive a zero haircut.

(iii) The collateral shall be adjusted downwards / marked down as per applicable haircut.

(iv) The amount of exposure reduced by the adjusted amount of collateral, shall receive a risk weight as applicable to the counterparty, as it is an on-balance sheet exposure.

(v) The lending bank shall not maintain any capital charge for the security received by it as collateral during the repo period, since such collateral does not enter its balance sheet but is only held as a bailee.

(4) The formula in paragraph 162 shall be adapted as follows to calculate the capital requirements for transactions with bilateral netting agreements. The bilateral netting agreements shall meet the requirements set out in paragraph 87 of these guidelines.

$$E^* = \max \{0, [(\Sigma(E) - \Sigma(C)) + \Sigma (E_s \times H_s) + \Sigma(E_{fx} \times H_{fx})]\}$$

where:

E^* = the exposure value after risk mitigation

E = current value of the exposure

C = the value of the collateral received

E_s = absolute value of the net position in a given security

H_s = haircut appropriate to Es

E_{fx} = absolute value of the net position in a currency different from the settlement

currency

H_{fx} = haircut appropriate for currency mismatch

The net long or short position of each security included in the netting agreement shall be multiplied by the appropriate haircut. All other rules regarding the calculation of haircuts stated in paragraphs 162 and 163 equivalently apply for a bank using bilateral netting agreements for repo-style transactions.

165. Collateralised OTC derivatives transactions

The calculation of the counterparty credit risk charge for an individual contract shall be as follows:

counterparty charge = [(RC + add-on) – C_A] x r x 9%

where:

RC = the replacement cost,

add-on = the amount for potential future exposure calculated according to paragraph 85(2),

C_A = the volatility adjusted collateral amount under the comprehensive approach prescribed in paragraphs 162 and 163 or zero if no eligible collateral is applied to the transaction, and

r = the risk weight of the counterparty.

When effective bilateral netting contracts are in place, RC shall be the net replacement cost and the add-on shall be A_{Net} as calculated according to paragraphs 85(2) and paragraph 87. The haircut for currency risk (H_{fx}) shall be applied when there is a mismatch between the collateral currency and the settlement currency. Even in the case where there are more than two currencies involved in the exposure, collateral and settlement currency, a single haircut assuming a 10- business day holding period scaled up as necessary depending on the frequency of mark-to-market shall be applied.

C.4 Credit risk mitigation (CRM) techniques - on-balance sheet netting

166. On-balance sheet netting is confined to loans / advances and deposits, where a bank has legally enforceable netting arrangements, involving specific lien with

proof of documentation. The bank shall calculate capital requirements on the basis of net credit exposures subject to the following conditions:

Where a bank,

(i) has a well-founded legal basis for concluding that the netting or offsetting agreement is enforceable in each relevant jurisdiction regardless of whether the counterparty is insolvent or bankrupt;

(ii) is able at any time to determine the loans / advances and deposits with the same counterparty that are subject to the netting agreement;

(iii) monitors and controls the relevant exposures on a net basis; and

(iv) monitors and controls its roll-off risks.

It may use the net exposure of loans / advances and deposits as the basis for its capital adequacy calculation in accordance with the formula in paragraph 162. Loans / advances are treated as exposure and deposits as collateral. The haircuts shall be zero except when a currency mismatch exists. All the requirements contained in paragraph 162 and paragraphs 177 to 180 shall also apply.

C.5 Credit risk mitigation (CRM) techniques - guarantees

167. Where guarantees are direct, explicit, irrevocable and unconditional a bank shall take account of such credit protection in calculating capital requirements.

168. A range of guarantors are recognised and a substitution approach shall be applied. Thus, only guarantees issued by entities with a lower risk weight than the counterparty shall lead to reduced capital charges since the protected portion of the counterparty exposure is assigned the risk weight of the guarantor, whereas the uncovered portion retains the risk weight of the underlying counterparty.

169. Detailed operational requirements for guarantees eligible for being treated as a CRM are as under.

(i) A guarantee (counter-guarantee) shall represent a direct claim on the protection provider and shall be explicitly referenced to specific exposures or a pool of exposures, so that the extent of the cover is clearly defined and

incontrovertible. The guarantee shall be irrevocable; there shall be no clause in the contract that would allow the protection provider to unilaterally cancel the cover or that would increase the effective cost of cover as a result of deteriorating credit quality in the guaranteed exposure. The guarantee shall also be unconditional; there shall be no clause in the guarantee outside the direct control of the bank that shall prevent the protection provider from being obliged to pay out in a timely manner in the event that the original counterparty fails to make the payment(s) due.

(ii) All exposures shall be risk weighted after taking into account risk mitigation available in the form of guarantees. When a guaranteed exposure is classified as non-performing, the guarantee shall cease to be a credit risk mitigant and no adjustment shall be permissible on account of credit risk mitigation in the form of guarantees. The entire outstanding, net of specific provision and net of realisable value of eligible collaterals / credit risk mitigants, shall attract the appropriate risk weight.

170. In addition to the legal certainty requirements in paragraph 156, for a guarantee to be recognised, the following conditions shall be satisfied:

(i) On the qualifying default / non-payment of the counterparty, the bank is able in a timely manner to pursue the guarantor for any monies outstanding under the documentation governing the transaction. The guarantor shall make one lump sum payment of all monies under such documentation to the bank, or the guarantor shall assume the future payment obligations of the counterparty covered by the guarantee. The bank shall have the right to receive any such payments from the guarantor without first having to take legal actions in order to pursue the counterparty for payment.

(ii) The guarantee is an explicitly documented obligation assumed by the guarantor.

(iii) Except as noted in the following sentence, the guarantee covers all types of payments the underlying obligor is expected to make under the documentation governing the transaction, for example notional amount, margin payments etc. Where a guarantee covers payment of principal only,

interests and other uncovered payments shall be treated as an unsecured amount in accordance with paragraph 173.

171. Range of eligible guarantors (counter-guarantors)

Credit protection given by the following entities shall be recognised:

(i) Sovereigns, sovereign entities (including BIS, IMF, European Central Bank and European Community as well as those MDBs referred to in paragraph 41, ECGC and CGTMSE, CRGFTLIH, individual schemes under NCGTC which are backed by explicit Central Government Guarantee), banks and primary dealers with a lower risk weight than the counterparty.

(ii) Other entities that are externally rated except when credit protection is provided to a securitisation exposure. This shall include credit protection provided by parent, subsidiary and affiliate companies when they have a lower risk weight than the obligor.

(iii) When credit protection is provided to a securitisation exposure, other entities that currently are externally rated BBB- or better and that were externally rated A- or better at the time the credit protection was provided. This shall include credit protection provided by parent, subsidiary and affiliate companies when they have a lower risk weight than the obligor.

(iv) In case of securitisation transactions, special purpose entities (SPE) cannot be recognised as eligible guarantors.

172. Risk Weights

(1) The protected portion is assigned the risk weight of the protection provider. Exposures covered by State Government guarantees shall attract a risk weight of 20 per cent. The uncovered portion of the exposure is assigned the risk weight of the underlying counterparty subject to conditions stipulated in paragraph 172(2).

(2) As per Reserve Bank of India (Commercial Banks – Concentration Risk Management) Directions, 2025 on large exposures framework, any CRM instrument from which CRM benefits like shifting of exposure / risk weights etc. are not derived may not be counted as an exposure on the CRM provider. In case of non-fund-based credit facilities provided to a person resident outside

India where CRM benefits are not derived and the exposure is shifted to the non-resident person, such exposures to the non-resident person shall attract a minimum risk weight of 150 per cent.

173. Proportional cover

Where the amount guaranteed, or against which credit protection is held, is less than the amount of the exposure, and the secured and unsecured portions are of equal seniority, i.e., the bank and the guarantor share losses on a pro-rata basis capital relief shall be afforded on a proportional basis i.e., the protected portion of the exposure shall receive the treatment applicable to eligible guarantees, with the remainder treated as unsecured.

174. Currency mismatches

Where the credit protection is denominated in a currency different from that in which the exposure is denominated i.e., when there is a currency mismatch, the amount of the exposure deemed to be protected shall be reduced by the application of a haircut H_{FX}, i.e.,

$$\mathbf{GA = G \times (1- H_{FX})}$$

Where;

G = nominal amount of the credit protection

H_{FX} = haircut appropriate for currency mismatch between the credit protection and underlying obligation.

A bank using the supervisory haircuts shall apply a haircut of eight per cent for currency mismatch.

175. Sovereign guarantees and counter guarantees

A claim may be covered by a guarantee that is indirectly counter guaranteed by a sovereign. Such a claim shall be treated as covered by a sovereign guarantee provided that:

(i) the sovereign counter-guarantee covers all credit risk elements of the claim;

(ii) both the original guarantee and the counter-guarantee meet all operational requirements for guarantees, except that the counter-guarantee need not be direct and explicit to the original claim; and

(iii) the cover shall be robust and no historical evidence suggests that the coverage of the counter-guarantee is less than effectively equivalent to that of a direct sovereign guarantee.

176. ECGC guaranteed exposures

Risk weight applicable to the claims on ECGC shall be capped to the maximum liability amount specified in the whole turnover policy of the ECGC. A bank shall proportionately distribute the ECGC maximum liability amount to all individual export credits that are covered by the ECGC Policy. For the covered portion of individual export credits, the bank shall apply the risk weight applicable to claims on ECGC. For the remaining portion of individual export credit, the bank shall apply the risk weight as per the rating of the counterparty. The RWA computation can be mathematically represented as under:

Size of individual export credit exposure i	A_i
Size of individual covered export credit exposure i	B_i
Sum of individual covered export credit exposures	$\sum Bi$
Where:	
i = 1 to n, if total number of exposures is n	
Maximum Liability Amount	ML
Risk Weight of counter party for exposure i	RWi
RWA for ECGC Guaranteed Export Credit**:**	

$$\sum \left[\left(\frac{Bi}{\sum Bi} * ML * 20\% \right) + \{Ai - (\frac{Bi}{\sum Bi} * ML)\} * RWi \right]$$

C.6 Maturity mismatch

177. For calculating risk-weighted assets, a maturity mismatch occurs when the residual maturity of collateral is less than that of the underlying exposure. Where there is a maturity mismatch and the CRM has an original maturity of less than one year, the CRM is not recognised for capital purposes. In other cases where there is a maturity mismatch, partial recognition is given to the CRM for regulatory capital purposes as detailed below in paragraphs 178 to 180. In case of loans collateralised by the bank's own deposits, even if the tenor of such deposits is less than three months or deposits have maturity mismatch vis-à-vis the tenor of

the loan, the provisions of this paragraph regarding derecognition of collateral would not be attracted provided an explicit consent has been obtained from the depositor (i.e. borrower) for adjusting the maturity proceeds of such deposits against the outstanding loan or for renewal of such deposits till the full repayment of the underlying loan.

178. Definition of Maturity

The maturity of the underlying exposure and the maturity of the collateral should both be defined conservatively. The effective maturity of the underlying should be gauged as the longest possible remaining time before the counterparty is scheduled to fulfil its obligation, taking into account any applicable grace period. For the collateral, embedded options which may reduce the term of the collateral should be taken into account so that the shortest possible effective maturity is used. The maturity relevant here is the residual maturity.

179. Risk weights for maturity mismatches

As outlined in paragraph 177, collateral with maturity mismatches is only recognised when their original maturities are greater than or equal to one year. As a result, the maturity of collateral for exposures with original maturities of less than one year shall be matched to be recognised. In all cases, collateral with maturity mismatches shall no longer be recognised when they have a residual maturity of three months or less.

180. When there is a maturity mismatch with recognised credit risk mitigants (collateral, on-balance sheet netting and guarantees) the following adjustment shall be applied:

$$\mathbf{P_a = P \times (t - 0.25) \div (T - 0.25)}$$

where:

P_a = value of the credit protection adjusted for maturity mismatch

P = credit protection (e.g., collateral amount, guarantee amount) adjusted for any haircuts

t = min (T, residual maturity of the credit protection arrangement) expressed in years

T = min (5, residual maturity of the exposure) expressed in years

C.7 Treatment of pools of credit risk mitigation (CRM) techniques

181. In the case where a bank has multiple CRM techniques covering a single exposure (e.g., a bank has both collateral and guarantee partially covering an exposure), the bank shall be required to subdivide the exposure into portions covered by each type of CRM technique (e.g., portion covered by collateral, portion covered by guarantee) and the risk-weighted assets of each portion shall be calculated separately. When credit protection provided by a single protection provider has differing maturities, they shall be subdivided into separate protection as well.

D Capital charge for market risk

D.1 Scope and coverage

182. Market risk positions subject to capital charge requirement shall include:

(1) Positions in interest rate related instruments and equities in the trading book; and

(2) Foreign exchange positions (including open position in precious metals) throughout the bank (both banking and trading books).

183. A bank shall manage the market risk in its books on an ongoing basis and ensure that the capital requirements for market risks are being met on a continuous basis i.e., at the close of each business day. The bank shall also maintain strict risk management systems to monitor and control intra-day exposures to market risks.

184. A bank shall not compute capital charge for market risk for securities which have already matured and remain unpaid. These securities shall attract capital only for credit risk. On completion of 90 days delinquency, these shall be treated on par with NPAs for deciding the appropriate risk weights for credit risk.

185. A bank shall calculate the RWAs for market risk by multiplying the market risk capital charge by a factor of 12.5, as provided in paragraph 212. The market risk capital charge is the sum of the capital requirements arising from each of the three risk classes – namely interest rate risk, equity risk and foreign exchange risk as detailed in the formula below:

$$Capital\ Requirement = CR_{IRR} * SF_{IRR} + CR_{EQ} * SF_{EQ} + CR_{FX} * SF_{FX}$$

where:

CR_{IRR} = capital requirement prescribed for interest rate risk under paragraphs 186 to 194 and paragraphs 205 to 211 (including additional requirements for options such as non-delta risks);

CR_{EQ} = capital requirement prescribed for equity risk under paragraphs 195 to 198;

CR_{FX} = capital requirement prescribed for forex risk under paragraph 199 and paragraphs 205 to 211 (including additional requirements for options such as non-delta risks);

SF_{IRR} = Scaling factor of 1.2;

SF_{EQ} = Scaling factor of 2.0; and

SF_{FX} = Scaling factor of 1. 1.

Note: The scalars provided above are part of a transition arrangement. Upon implementation of 'final guidelines on minimum capital requirements for Market Risk - Simplified Standardised Approach', the scalars will be $SF_{IRR} = 1.3$; $SF_{EQ} = 3.5$; *and* $SF_{FX} = 1.2$.

D.2 Interest rate risk

186. The capital charge for interest rate related instruments shall apply to fair value of these items in a bank's Trading Book. Since a bank is required to maintain capital for market risks on an ongoing basis, it shall mark to market its trading positions on a daily basis. The fair value shall be determined as per extant Reserve Bank of India (Commercial Banks – Classification, Valuation, and Operation of Investment Portfolio) Directions, 2025.

187. The minimum capital requirement is expressed in terms of two separately calculated charges, (i) **specific risk** charge for each security, both for short and long positions, and (ii) **general market risk** charge towards interest rate risk in

the portfolio, where long and short positions in different securities or instruments can be offset.

Note - Short position is not allowed in India except in derivatives and Central Government Securities.

Specific Risk

188. The specific risk charges for various kinds of exposures shall be applied as detailed below:

Sr. No.	Nature of debt securities / issuer	Table / Paragraph to be followed
a.	Central, State and Foreign Central Governments' Bonds	Table 30
b.	Banks' Bonds	Table 31
c.	Corporate Bonds (other than Bank Bonds)	Table 32
d.	Non-common Equity Capital Instruments issued by Financial Entities other than Banks	Table 33
e.	Securitisation Exposure	Paragraph 190
f.	Debt mutual fund / exchange traded fund* (ETF) with underlying comprising of (i) Central, State and Foreign Central Governments' bonds (ii) Bank's Bonds and (iii) Corporate Bonds (other than Bank Bonds)	 Table 30 Table 31 Table 32
g.	Equity Investments in Banks	Table 37
h.	Equity Investments in Financial Entities (other than Banks)	Table 38
i.	Equity Investments in Non-financial (commercial) Entities	Table 39

Table 30: Specific risk capital charge for securities issued by Indian and foreign sovereigns

Sr. No.	Nature of investment	Residual maturity	Specific risk capital charge (as % of exposure)
A.	**Indian Central Government and State Governments**		

Sr. No.	Nature of investment	Residual maturity	Specific risk capital charge (as % of exposure)
1.	Central and State Government Securities	All	0.00
2.	Other approved securities guaranteed by Central Government	All	0.00
3.	Other approved securities guaranteed by State Government	6 months or less	0.28
		More than 6 months and up to and including 24 months	1.13
		More than 24 months	1.80
4.	Other securities where payment of interest and repayment of principal are guaranteed by Central Government	All	0.00
5.	Other securities where payment of interest and repayment of principal are guaranteed by State Government.	6 months or less	0.28
		More than 6 months and up to and including 24 months	1.13
		More than 24 months	1.80
B.	**Foreign Central Governments**		
1.	AAA to AA	All	0.00
2.	A to BBB	6 months or less	0.28
		More than 6 months and up to and including 24 months	1.13
		More than 24 months	1.80
3.	BB to B	All	9.00
4.	Below B	All	13.50
5.	Unrated	All	13.50

Table 31: Specific risk capital charge for bonds issued by banks

	Residual maturity	Specific risk capital charge (as % of exposure)			
		All Scheduled Banks (Commercial Banks, Regional Rural Banks, Local Area Banks and Co-operative Banks)		All Non-Scheduled Banks (Commercial Banks, Regional Rural Banks, Local Area Banks and Co-operative Banks)	
Level of CET1 capital including applicable capital conservation buffer (CCB) (%) of the investee bank (where applicable)		**Investments in capital instruments (other than equity[#]) referred to in paragraph 42(i)**	**All other claims**	**Investments in capital instruments (other than equity[#]) referred to in paragraph 42(i)**	**All other claims**
1	**2**	**3**	**4**	**5**	**6**
Applicable Minimum CET1 + Applicable CCB and above	≤6 months	1.75	0.28	1.75	1.75
	> 6 months and ≤ 24 months	7.06	1.13	7.06	7.06
	>24 months	11.25	1.8	11.25	11.25
Applicable Minimum CET1 + (CCB = 75% and <100% of applicable CCB)	All Maturities	13.5	4.5	22.5	13.5
Applicable Minimum CET1 + (CCB = 50% and <75% of applicable CCB)	All Maturities	22.5	9	31.5	22.5
Applicable Minimum CET1 + (CCB = 0% and <50% of applicable CCB)	All Maturities	31.5	13.5	56.25	31.5
Minimum CET1 less than applicable minimum	All Maturities	56.25	56.25	Full deduction*	56.25

*The deduction shall be made from CET1 Capital.

[#] refer to paragraph 198 below for specific risk capital charge on equity instruments.

Explanation –

(i) In case of banks where no capital adequacy norms have been prescribed by the RBI, the lending / investing bank shall calculate the applicable Common Equity Tier 1 and capital conservation buffer of the bank concerned, notionally, by obtaining necessary information from the investee bank and using the capital adequacy norms as applicable to the commercial banks. In case, it is not found

feasible to compute applicable Common Equity Tier 1 and capital conservation buffer on such notional basis, the specific risk capital charge of 31.5 per cent or 56.25 per cent, as per the risk perception of the investing bank, shall be applied uniformly to the investing bank's entire exposure.

(ii) In case of banks where capital adequacy norms are not applicable at present, the matter of investments in their capital-eligible instruments would not arise for now. However, this Table above shall become applicable to them, if in future they issue any capital instruments where other banks are eligible to invest.

Table 32: Specific risk capital charge for corporate bonds (other than bank bonds)

Rating by ECAI*	Residual maturity	Specific risk capital charge (as % of exposure)
AAA to BBB	6 months or less	0.28
	Greater than 6 months and up to and including 24 months	1.14
	Exceeding 24 months	1.80
BB and below	All maturities	13.5
Unrated (if permitted)	All maturities	9

*These ratings indicate the ratings assigned by Indian rating agencies / ECAIs or foreign rating agencies. In the case of foreign ECAIs, the rating symbols used here correspond to S&P. The modifiers '+' or '-' have been subsumed with the main rating category.

Table 33: Specific risk capital charge for non-common equity capital instruments issued by financial entities other than banks

Residual maturity	Specific risk capital charge (as % of exposure)
≤6 months	1.75
> 6 months and ≤ 24 months	7.06
>24 months	11.25

189. Investment in debt mutual fund / ETF for which full constituent debt details are available shall attract general market risk charge of 9 per cent. In case of debt mutual fund / ETF which contains a mix of the debt instruments listed in Tables 30, 31 and / or 32, the specific risk capital charge shall be computed based on the debt instrument attracting the highest specific risk capital charge in the fund. Debt mutual fund / ETF classified in trading book for which constituent debt

details are not available, at least as of each month-end, shall be treated on par with equity for computation of capital charge for market risk as prescribed in paragraphs 195 to 198.

190. Specific risk capital charge for securitisation exposures

For securitisation transactions undertaken subsequent to September 24, 2021, the specific risk capital requirement of securitisation exposures that are held under trading book shall be calculated according to the revised method as set out in paragraphs 88 to 125 of these Directions. Accordingly, a bank shall calculate the specific risk capital requirement applicable to each securitisation exposure in trading book by dividing the risk weight calculated, as if it were held in the banking book by 11.11, subject to a cap on specific risk capital requirement of 100 per cent.

For transactions undertaken prior to September 24, 2021, the treatment of securitisation exposures for capital adequacy shall be as provided below:

Table 34.1: Specific risk capital charge for transactions in Securitisation exposures prior to September 24, 2021

Rating by the ECAI*	Specific risk capital charge (as % of exposure)	
	Securtisation Exposures	Securtisation Exposures (SDIs) relating to Commercial Real Estate Exposures
AAA	1.8	9.0
AA	2.7	9.0
A	4.5	9.0
BBB	9.0	9.0
BB	31.5 (100.0 in the case of originators)	31.5 (100.0 in the case of originators)
B and below or Unrated	100.0	100.0

*These ratings indicate the ratings assigned by Indian rating agencies / ECAIs or foreign rating agencies. In the case of foreign ECAIs, the rating symbols used here correspond to Standard and Poor. The modifiers '+' or '-' have been subsumed with the main rating category.

Table 34.2: Specific Risk Capital Charge for transactions in Re-securitisation Exposures

Rating by the ECAI*	Specific Risk Capital Charge	
	Re-Securitisation Exposures (in %)	Re-Securitisation Exposures relating to Commercial Real Estate Exposures (in %)

AAA	3.6	18.0
AA	5.4	18.0
A	9.0	18.0
BBB	18.0	18.0
BB	63.0 (100.0 in the case of originators)	63.0 (100.0 in the case of originators)
B and below or Unrated	100.0	100.0

*These ratings indicate the ratings assigned by Indian rating agencies/ECAIs or foreign rating agencies. In the case of foreign ECAIs, the rating symbols used here correspond to Standard and Poor. The modifiers "+" or "-" have been subsumed with the main rating category.

Explanation –

Re-securitisation Exposures are not allowed in terms of Reserve Bank of India (Commercial Banks – Securitisation Transactions) Directions, 2025.

191. A bank shall, in addition to computing the counterparty credit risk (CCR) charge for OTC derivatives, as part of capital for credit risk as per the Standardised Approach covered in paragraphs 82 to 87, also compute the specific risk charge for OTC derivatives in the trading book as required in terms of paragraphs 205 to 211.

General Market Risk

192. The capital charge for general market risk shall be the sum of four components:

(i) the net short (short position is not allowed in India except in derivatives and Central Government Securities) or long position in the whole trading book;

(ii) a small proportion of the matched positions in each time-band (the 'vertical disallowance');

(iii) a larger proportion of the matched positions across different time-bands (the 'horizontal disallowance'); and

(iv) a net charge for positions in options, where appropriate.

193. Separate maturity ladders shall be used for each currency and capital charges shall be calculated for each currency separately and then summed with no offsetting between positions of opposite sign. In the case of those currencies in which business is insignificant (where the turnover in the respective currency is

less than 5 per cent of overall foreign exchange turnover), separate calculations for each currency shall not be required. The bank may instead, slot within each appropriate time-band, the net long or short position for each currency. However, these individual net positions shall be summed within each time-band, irrespective of whether they are long or short positions, to produce a gross position figure. The gross positions in each time-band shall be subject to the assumed change in yield set out in Table 35 with no further offsets.

194. A bank shall measure the general market risk charge by calculating the price sensitivity (modified duration) of each position separately as follows:

(i) calculate the price sensitivity (modified duration) of each instrument;

(ii) apply the assumed change in yield to the modified duration of each instrument between 0.6 and 1.0 percentage points depending on the maturity of the instrument (see Table 35);

(iii) slot the resulting capital charge measures into a maturity ladder with fifteen-time bands as set out in Table 35;

(iv) subject long and short positions in each time band to a 5 per cent vertical disallowance designed to capture basis risk; and

(v) carry forward the net positions in each time-band for horizontal offsetting subject to the disallowances set out in Table 36.

Table 35 - Duration Method – time bands and assumed changes in yield

Time bands	Assumed change in yield (in %)		Time bands	Assumed change in yield (in %)
Zone 1			**Zone 3**	
1 month or less	1.00		3.6 to 4.3 years	0.75
1 to 3 months	1.00		4.3 to 5.7 years	0.70
3 to 6 months	1.00		5.7 to 7.3 years	0.65
6 to 12 months	1.00		7.3 to 9.3 years	0.60
Zone 2			9.3 to 9.6 years	0.60
1.0 to 1.9 years	0.90		9.6 to 12 years	0.60
1.9 to 2.8 years	0.80		12 to 20 years	0.60
2.8 to 3.6 years	0.75		over 20 years	0.60

Table 36 - Horizontal disallowances

Zones	Time band	Within the zones	Between adjacent zones	Between zones 1 and 3
Zone 1	1 month or less	40%	40% 40%	100%
	1 to 3 months			
	3 to 6 months			
	6 to 12 months			
Zone 2	1.0 to 1.9 years	30%		
	1.9 to 2.8 years			
	2.8 to 3.6 years			
Zone 3	3.6 to 4.3 years	30%		
	4.3 to 5.7 years			
	5.7 to 7.3 years			
	7.3 to 9.3 years			
	9.3 to 9.6 years			
	9.6 to 12 years			
	12 to 20 years			
	over 20 years			

D.3 Equity risk

195. The capital charge for equities shall apply on their fair value in a bank's trading book. Minimum capital requirement to cover the risk of holding or taking positions in equities in the trading book is set out below. This shall be applied to all instruments that exhibit market behaviour similar to equities but not to non-convertible preference shares (which are covered by the interest rate risk requirements described earlier). The instruments covered include equity shares, whether voting or non-voting, convertible securities that behave like equities, for example : units of funds (other than debt mutual funds / ETFs mentioned in paragraph 189), and commitments to buy or sell equity.

Explanation –

A bank shall refer to the Reserve Bank of India (Commercial Banks – Classification, Valuation, and Operation of Investment Portfolio) Directions, 2025. Investments in subsidiaries, associates and joint ventures would be part of banking book; unlisted equity shall be part of banking book [FVTPL (non-HFT)], or under AFS in terms of the Direction *ibid*.; and listed equity is generally part of trading book (classified under HFT), unless such investment is classified under AFS in terms of the Directions *ibid*.

Specific and general market risk

196. Capital charge for specific risk shall be 11.25 per cent or capital charge in accordance with the risk warranted by external rating (or lack of it) of the counterparty, whichever is higher and specific risk is computed on a bank's gross equity positions (i.e., the sum of all long equity positions and of all short equity positions - short equity position is, however, not allowed for a bank in India). In addition, the general market risk charge shall also be 9 per cent on the gross equity positions. These capital charges shall also be applicable to all trading book exposures, which are exempted from capital market exposure ceilings for direct investments.

197. Specific risk capital charge for a bank's investment in Security Receipts shall be 13.5 per cent (equivalent to 150 per cent risk weight).

Explanation –

A bank shall refer to Reserve Bank of India (Commercial Banks – Classification, Valuation, and Operation of Investment Portfolio) Directions, 2025. Accordingly, Security Receipts can be part of banking book [classified under FVTPL (non-HFT)] or trading book (classified under HFT).

198. Specific risk capital charge for a bank's investments in the equity of other banks / other financial entities / non-financial entities shall be as under:

Table 37: Specific risk capital charge for bank's investments in the equity of other banks

Level of CET1 capital including applicable CCB (%) of the investee bank (where applicable)	**All scheduled banks (Commercial banks, RRBs, LABs, Cooperative Banks)**		**All Non-scheduled Banks (Commercial banks, RRBs, LABs, Cooperative Banks) (in %)**	
	Equity investments in other banks referred to in:		**Equity investments in other banks referred to in:**	
	paragraph 42(i)	paragraph 40(ii)	paragraph 40(i)	paragraph 42(ii)
Applicable Minimum CET1 + Applicable CCB and above	11.25	22.5	11.25	27
Applicable Minimum CET1 + (CCB = 75% and <100% of applicable CCB)	13.5	27	22.5	31.5

Level of CET1 capital including applicable CCB (%) of the investee bank (where applicable)	All scheduled banks (Commercial banks, RRBs, LABs, Cooperative Banks)		All Non-scheduled Banks (Commercial banks, RRBs, LABs, Cooperative Banks) (in %)	
Applicable Minimum CET1 + (CCB = 50% and <75% of applicable CCB)	22.5	31.5	31.5	40.5
Applicable Minimum CET1 + (CCB = 0% and <50% of applicable CCB)	31.5	40.5	56.25	Full deduction*
Minimum CET1 less than applicable minimum	50	Full deduction*	Full deduction*	Full deduction*

* Full deduction shall be made from CET1 capital

Table 38: Specific risk capital charge for bank's investments in the equity of financial entities other than banks

	Equity investments in financial entities other than banks referred to in:	
	paragraph 42(i)	paragraph 42(ii)
Specific risk capital charge (%)	11.25	22.5

Table 39: Specific risk capital charge for bank's investments in the equity of non-financial (commercial) entities

	Equity investments in non-financial entities	
	where a bank does not own more than 10% of the equity capital of investee companies	which are more than 10% of the equity capital of investee companies or which are affiliates of the bank (these exposures need not attract general market risk charge)
Specific risk capital charge (%)	11.25	100

D.4 Foreign exchange risk

199. The bank's net open position in each currency shall be calculated by summing:

(i) The net spot position (i.e., all asset items less all liability items, including accrued interest, denominated in the currency in question);

(ii) The net forward position (i.e., all amounts to be received less all amounts to be paid under forward foreign exchange transactions, including currency

futures and the principal on currency swaps not included in the spot position);

(iii) Guarantees (and similar instruments) that are certain to be called and are likely to be irrecoverable;

(iv) Net future income / expenses not yet accrued but already fully hedged (at the discretion of the reporting bank);

(v) Depending on accounting conventions in different countries, any other item representing a profit or loss in foreign currencies; and

(vi) The net delta-based equivalent of the total book of foreign currency options.

Foreign exchange open positions and gold open positions shall attract risk-weight of 100 per cent. Thus, the open positions, limits or actual, whichever is higher, shall attract capital charge at 9 per cent. This capital charge is in addition to the capital charge for credit risk on the on-balance sheet and off-balance sheet items pertaining to foreign exchange and gold transactions.

D.5 Credit default swap (CDS) positions in the trading book

200. General market risk

A CDS does not normally create a position for general market risk for either the protection buyer or protection seller. However, the present value of premium payable / receivable is sensitive to changes in the interest rates. To measure the interest rate risk in premium receivable / payable for a CDS, the present value of the premium shall be treated as a notional position in Government securities of relevant maturity. These positions shall attract appropriate capital charge for general market risk. The protection buyer / seller shall treat the present value of the premium payable / receivable equivalent to a short / long notional position in Government securities of relevant maturity.

201. Specific risk for exposure to reference entity

A CDS creates a notional long / short position for specific risk in the reference asset / obligation for protection seller / protection buyer. For calculating specific risk capital charge, the notional amount of the CDS and its maturity shall be used. The specific risk capital charge for CDS positions shall be as per Table 40 below.

Table 40: Specific risk capital charge for bought and sold CDS positions in the trading book

(1) Exposures to entities other than CRE companies

Up to 90 days			After 90 days	
Ratings by the ECAI*	**Residual Maturity of the instrument**	**Capital charge**	**Ratings by the ECAI***	**Capital charge**
AAA to BBB	6 months or less	0.28 %	AAA	1.8 %
	Greater than 6 months and up to and including 24 months	1.14%	AA	2.7%
	Exceeding 24 months	1.80%	A	4.5%
			BBB	9.0%
BB and below	All maturities	13.5%	BB and below	13.5%
Unrated (if permitted)	All maturities	9.0%	Unrated (if permitted)	9.0%

* These ratings indicate the ratings assigned by Indian rating agencies / ECAIs or foreign rating agencies. In the case of foreign ECAIs, the rating symbols used here correspond to Standard and Poor. The modifiers '+' or '-' have been subsumed within the main category.

(2) Exposures to CRE companies#

Ratings by the ECAI*	Residual Maturity of the instrument	Capital charge
AAA to BBB	6 months or less	1.4%
	Greater than 6 months and up to and including 24 months	7.7%
	Exceeding 24 months	9.0%
BB and below	All maturities	9.0%
Unrated (if permitted)	All maturities	9.0%

#The above table shall be applicable for exposures up to 90 days. Capital charge for exposures to CRE companies beyond 90 days shall be 9 per cent, regardless of rating of the reference / deliverable obligation.

*These ratings indicate the ratings assigned by Indian rating agencies / ECAIs or foreign rating agencies. In the case of foreign ECAIs, the rating symbols used here correspond to Standard and Poor. The modifiers '+' or '-' have been subsumed within the main category.

202. Specific risk capital charge for positions hedged by CDS

(1) A bank may fully offset the specific risk capital charges when the values of two legs (i.e., long and short in CDS positions) always move in the opposite direction and broadly to the same extent. This shall be the case when the two legs consist

of completely identical CDS. In these cases, no specific risk capital requirement applies to both sides of the CDS positions.

(2) A bank may offset 80 per cent of the specific risk capital charges when the value of two legs (i.e., long and short) always moves in the opposite direction but not broadly to the same extent. This shall be the case when a long cash position is hedged by a credit default swap and there is an exact match in terms of the reference / deliverable obligation, and the maturity of both the reference / deliverable obligation and the CDS. In addition, key features of the CDS (e.g., credit event definitions, settlement mechanisms) shall not cause the price movement of the CDS to materially deviate from the price movements of the cash position. To the extent that the transaction transfers risk, an 80 per cent specific risk offset shall be applied to the side of the transaction with the higher capital charge, while the specific risk requirement on the other side shall be zero.

(3) A bank may offset partially the specific risk capital charges when the value of the two legs (i.e., long and short) usually moves in the opposite direction. This shall be the case in the following situations:

(i) The position is captured in paragraph 202(2) but there is an asset mismatch between the cash position and the CDS. However, the underlying asset is included in the (reference / deliverable) obligations in the CDS documentation and meets the requirements in paragraph 129(3)(i).

(ii) The position is captured in paragraph 202(2) but there is maturity mismatch between credit protection and the underlying asset. However, the underlying asset is included in the (reference / deliverable) obligations in the CDS documentation.

(iii) In each of the cases in (i) and (ii) above, rather than applying specific risk capital requirements on each side of the transaction (i.e., the credit

protection and the underlying asset), only higher of the two capital requirements shall apply.

203. Specific risk capital charge in CDS positions which are not meant for Hedging

In cases not captured in paragraph 202, a specific risk capital charge shall be assessed against both sides of the positions.

204. Capital charge for counterparty credit risk

The credit exposure for the purpose of counterparty credit risk on account of CDS transactions in the trading book shall be calculated according to the Current Exposure Method.

Explanation - A CDS contract, which is required to be marked-to-market, creates bilateral exposure for the parties to the contract. The mark-to-market value of a CDS contract is the difference between the default-adjusted present value of protection payment (called 'protection leg' / 'credit leg') and the present value of premium payable called ('premium leg'). If the value of credit leg is less than the value of the premium leg, then the marked-to-market value for the protection seller is positive. Therefore, the protection seller will have exposure to the counterparty (protection buyer) if the value of premium leg is more than the value of credit leg. In case, no premium is outstanding, the value of premium leg will be zero and the mark-to-market value of the CDS contract will always be negative for the protection seller and therefore, protection seller will not have any exposure to the protection buyer. In no case, the protection seller's exposure on protection buyer can exceed the amount of the premium unpaid. For the purpose of capital adequacy as well as exposure norms, the measure of counterparty exposures in case of CDS transaction held in Trading Book is the Potential Future Exposure (PFE) which is measured and recognised as per Current Exposure Method.

(1) Protection seller

A protection seller will have exposure to the protection buyer only if the fee / premia is outstanding. In such cases, the counterparty credit risk charge for all single name long CDS positions in the trading book shall be calculated as the sum of the current marked-to-market value, if positive (zero, if marked-to-market value is negative) and the potential future exposure add-on factors based on table given below. However, for protection seller where the CDS positions are

outside netting and margin agreements, the add-on shall be capped to the amount of unpaid premia. A bank has the option to remove such CDS positions from its legal netting sets and treat them as individual unmargined transactions in order to apply the cap.

Table 41: Add on factor for protection seller

Type of reference obligation	**Add-on factor for protection seller (% of notional principal of CDS)**
Obligations rated BBB- and above	10
Below BBB- and unrated	20

(2) Protection buyer

A CDS contract creates a counterparty exposure on the protection seller on account of the credit event payment. The counterparty credit risk charge for all short CDS positions in the trading book shall be calculated as the sum of the current marked-to-market value, if positive (zero, if marked-to-market value is negative) and the potential future exposure add-on factors based on Table given below:

Table 42: Add on factor for protection buyer

Type of reference obligation	**Add-on factor for protection buyer (% of notional principal of CDS)**
Obligations rated BBB- and above	10
Below BBB- and unrated	20

(3) Capital charge for counterparty risk for collateralised transactions in CDS

The counterparty exposure for CDS traded in the OTC market shall be calculated as per the Current Exposure Method. Under this method, the calculation of the counterparty credit risk charge for an individual contract, taking into account the collateral, shall be as follows:

Counterparty risk capital charge = [(RC + add-on) – CA] x r x 9%

Where;

RC = the replacement cost,

add-on = the amount for potential future exposure calculated according to paragraph 85(2) above.

CA = the volatility adjusted amount of eligible collateral under the Comprehensive Approach prescribed in paragraphs 157 to 165 on "Credit Risk Mitigation Techniques - Collateralised Transactions" of these guidelines, or zero if no eligible collateral is applied to the transaction, and

r = the risk weight of the counterparty.

(4) Treatment of exposures below materiality thresholds of CDS

Materiality thresholds on payments below which no payment is made in the event of loss are equivalent to retained first loss positions and shall be assigned risk weight of 1250 per cent for capital adequacy purpose by the protection buyer.

D.6 Interest rate derivatives and options

Interest rate derivatives

205. The measurement system shall include all interest rate derivatives and off-balance-sheet instruments in the trading book, which react to changes in interest rates (e.g., futures and forward contracts, including forward rate agreements (FRAs), interest rate and cross-currency swaps, forward foreign exchange positions, etc.). A summary of the rules for dealing with interest rate derivatives is set out in Table 43.

206. Calculation of positions

(1) The derivatives shall be converted into positions in the relevant underlying and be subjected to specific and general market risk charges as described in the guidelines. To calculate the capital charge, the amounts reported shall be the market value of the principal amount of the underlying or of the notional underlying. For instruments where the apparent notional amount differs from the effective notional amount, a bank shall use the effective notional amount.

(2) Futures and forward contracts, including FRA

These instruments shall be treated as a combination of a long and a short position in a notional government security. The maturity of a future or an FRA shall be the period until delivery or exercise of the contract, plus - where applicable - the life of the underlying instrument. For example, a long position in a June three-month interest rate future (taken in April) is to be reported as a long

position in a government security with a maturity of five months and a short position in a government security with a maturity of two months. Where a range of deliverable instruments may be available to fulfil the contract, the bank shall have flexibility to elect which deliverable security goes into the duration ladder but shall take account of any conversion factor defined by the exchange.

(3) Swaps

Swaps shall be treated as two notional positions in government securities with relevant maturities. For example, an interest rate swap under which a bank is receiving floating rate interest and paying fixed shall be treated as a long position in a floating rate instrument of maturity equivalent to the period until the next interest fixing and a short position in a fixed-rate instrument of maturity equivalent to the residual life of the swap. For swaps that pay or receive a fixed or floating interest rate against some other reference price, e.g., a stock index, the interest rate component shall be slotted into the appropriate repricing maturity category, with the equity component being included in the equity framework. Separate legs of cross-currency swaps are to be reported in the relevant maturity ladders for the currencies concerned.

207. Calculation of capital charges for derivatives under the Standardised Methodology

(1) Allowable offsetting of matched positions

(i) A bank may exclude the following from the interest rate maturity framework altogether (for both specific and general market risk).

(a) Long and short positions (both actual and notional) in identical instruments with exactly the same issuer, coupon, currency and maturity.

(b) A matched position in a future or forward and its corresponding underlying may also be fully offset, (the leg representing the time to expiry of the future shall however be reported) and thus excluded from the calculation.

(ii) When the future or the forward comprises a range of deliverable instruments, offsetting of positions in the future or forward contract and its

underlying shall only be permissible in cases where there is a readily identifiable underlying security which is most profitable for the trader with a short position to deliver. The price of this security, sometimes called the 'cheapest-to-deliver', and the price of the future or forward contract shall in such cases move in close alignment.

(iii) No offsetting shall be allowed between positions in different currencies. The separate legs of cross-currency swaps or forward foreign exchange deals shall be treated as notional positions in the relevant instruments and included in the appropriate calculation for each currency.

(iv) Opposite positions in the same category of instruments may in certain circumstances be regarded as matched and allowed to offset fully. To qualify for this treatment the positions shall relate to the same underlying instruments, be of the same nominal value and be denominated in the same currency. In addition:

(a) for futures: offsetting positions in the notional or underlying instruments to which the futures contract relates shall be for identical products and mature within seven days of each other;

(b) for swaps and FRAs : the reference rate (for floating rate positions) shall be identical and the coupon closely matched (i.e., within 15 basis points); and

(c) for swaps, FRAs and forwards : the next interest fixing date or, for fixed coupon positions or forwards, the residual maturity shall correspond within the following limits:

(i) less than one month hence : same day;

(ii) between one month and one year hence : within seven days; and

(iii) over one year hence : within thirty days.

(v) A bank with a large swap book may use alternative formulae for these swaps to calculate the positions to be included in the duration ladder. The method shall be to calculate the sensitivity of the net present value implied

by the change in yield used in the Duration Method and allocate these sensitivities into the time-bands set out in Table 35.

(2) Specific risk

Interest rate and currency swaps, FRAs, forward foreign exchange contracts and interest rate futures shall not be subjected to a specific risk charge. This exemption also applies to futures on an interest rate index (e.g., SOFR). However, in the case of futures contracts where the underlying is a debt security, or an index representing a basket of debt securities, a specific risk charge shall apply according to the credit risk of the issuer as set out in paragraphs above.

(3) General market risk

General market risk applies to positions in all derivative products in the same manner as for cash positions, subject only to an exemption for fully or very closely matched positions in identical instruments as defined in paragraphs above. The various categories of instruments shall be slotted into the maturity ladder and treated according to the rules identified earlier.

Table 43: Summary of treatment of interest rate derivatives

Instrument	Specific risk charge	General Market risk charge
Exchange-traded Future		
- Government debt security	No	Yes, as two positions
- Corporate debt security	Yes	Yes, as two positions
- Index on interest rates (e.g., MIBOR)	No	Yes, as two positions
OTC Forward		
- Government debt security	No	Yes, as two positions
- Corporate debt security	Yes	Yes, as two positions
- Index on interest rates (e.g., MIBOR)	No	Yes, as two positions
FRAs, Swaps	No	Yes, as two positions
Forward Foreign Exchange	No	Yes, as one position in each currency
Options		
- Government debt security	No	
- Corporate debt security	Yes	
- Index on interest rates (e.g., MIBOR)	No	
- FRAs, Swaps	No	

Options

208. In recognition of the wide diversity of a bank's activities in options and the difficulties of measuring price risk for options, alternative approaches are permissible as under:

(i) Simplified Approach described in paragraph 210 for a bank that only has positions in purchased options

Explanation – This approach may also be adopted by a bank, in case it has all its written option positions hedged by perfectly matched long positions in exactly the same options, in which case no capital charge for market risk is required for these positions.

(ii) Intermediate Approaches as set out in paragraph 211 for a bank that has written options.

209. In the simplified approach, the positions for the options and the associated underlying, cash or forward, are not subject to the standardised methodology but are instead 'carved-out' and subject to separately calculated capital charges that incorporate both general market risk and specific risk. The risk numbers thus generated are then added to the capital charges for the relevant category, i.e.,

interest rate related instruments, equities, and foreign exchange as described in paragraphs 186 to 199 of these Directions. The delta-plus method uses the sensitivity parameters or 'Greek letters' associated with options to measure their market risk and capital requirements. Under this method, the delta-equivalent position of each option becomes part of the standardised methodology set out in paragraph 186 to 199 of these Directions with the delta-equivalent amount subject to the applicable general market risk charges. Separate capital charges are then applied to the gamma and vega risks of the option positions. The scenario approach uses simulation techniques to calculate changes in the value of an options portfolio for changes in the level and volatility of its associated underlying. Under this approach, the general market risk charge is determined by the scenario 'grid' (i.e., the specified combination of underlying and volatility changes) that produces the largest loss. For the delta-plus method and the scenario approach the specific risk capital charges are determined separately by multiplying the delta-equivalent of each option by the specific risk weights set out in paragraphs 186 to 198 of these Directions.

210. Simplified Approach

A bank which handles a limited range of purchased options only shall be free to use the simplified approach set out in Table 44 below, for particular trades. As an example of how the calculation shall work, if a holder of 100 shares currently valued at ₹10 each holds an equivalent put option with a strike price of ₹11, the capital charge shall be: ₹1,000 x 20.25 per cent (i.e., 11.25 per cent for specific risk plus 9 per cent for general market risk) = ₹202.50, less the amount the option is in the money (₹11 - ₹10) x 100 = ₹100, i.e., the capital charge shall be ₹102.50 . A similar methodology applies for options whose underlying is a foreign currency or an interest rate related instrument.

Table 44 - Simplified approach: capital charges

Capital charges Position	Treatment
Long cash and Long put Or Short cash and Long call	The capital charge shall be the market value of the underlying security[i] multiplied by the sum of specific and general market risk charges[ii] for the underlying less the amount the option is in the money (if any) bounded at zero[iii].
Long call	The capital charge shall be the lesser of:

Capital charges Position	Treatment
Or Long put	(i) the market value of the underlying security multiplied by the sum of specific and general market risk charges[iii] for the underlying; and (ii) the market value of the option

Note -

(i) In some cases, such as foreign exchange, it may be unclear which side is the 'underlying security'; this shall be taken to be the asset which shall be received if the option were exercised. In addition, the nominal value shall be used for items where the market value of the underlying instrument could be zero, e.g., caps and floors, swaptions etc.

(ii) Some options (e.g., where the underlying is an interest rate or a currency) bear no specific risk, but specific risk shall be present in the case of options on certain interest rate-related instruments (e.g., options on a corporate debt security or corporate bond index) and for options on equities and stock indices. The charge under this measure for currency options shall be 9 per cent.

(iii) For options with a residual maturity of more than six months, the strike price shall be compared with the forward, not current, price. A bank unable to do this shall take the 'in-the-money' amount to be zero.

(iv) Book value may be used in cases where the position does not fall within the trading book e.g., options on certain foreign exchange or commodities positions not belonging to the trading book.

211. Intermediate Approaches

(1) Delta-plus Method

(i) A bank which writes options shall be allowed to include delta-weighted options positions within the standardised methodology set out in paragraph 186 to 199 of these Directions. Such options shall be reported as a position equal to the market value of the underlying multiplied by the delta.

(ii) However, since delta does not sufficiently cover the risks associated with options positions, a bank shall also be required to measure gamma (which measures the rate of change of delta) and vega (which measures the

sensitivity of the value of an option with respect to a change in volatility) sensitivities in order to calculate the total capital charge. These sensitivities shall be calculated according to an approved exchange model or according to the bank's proprietary options pricing model subject to oversight by the Reserve Bank. Further, Reserve Bank may require a bank doing business in certain classes of exotic options (e.g., barriers, digitals) or in options 'at-the-money' that are close to expiry to use either the scenario approach or the internal models' alternative, both of which can accommodate more detailed revaluation approaches.

(iii) Delta-weighted positions with debt securities or interest rates as the underlying shall be slotted into the interest rate time-bands, as set out in Table 35, under the following procedure. A two-legged approach shall be used as for other derivatives, requiring one entry at the time the underlying contract takes effect and a second at the time the underlying contract matures. For instance, a call option bought on a June three-month interest-rate future shall in April be considered, on the basis of its delta-equivalent value, to be a long position with a maturity of five months and a short position with a maturity of two months. Similarly, a two-months call option on a bond future, where delivery of the bond takes place in September, shall be considered in April as being long the bond and short a five-month deposit, both positions being delta-weighted. The written option shall similarly be slotted as a long position with a maturity of two months and a short position with a maturity of five months. Floating rate instruments with caps or floors shall be treated as a combination of floating rate securities and a series of European-style options. For example, the holder of a three-year floating rate bond indexed to six-month SOFR with a cap of 15 per cent shall treat it as:

(a) a debt security that reprices in six months; and

(b) a series of five written call options on an FRA with a reference rate of 15 per cent, each with a negative sign at the time the underlying FRA takes effect and a positive sign at the time the underlying FRA

matures. The rules applying to closely matched positions set out in paragraph 207(1) shall also apply in this respect.

(iv) The capital charge for options with equities as the underlying shall also be based on the delta-weighted positions which shall be incorporated in the measure of market risk described in paragraphs 195 to 198 of these Directions. For purposes of this calculation, each national market is to be treated as a separate underlying. The capital charge for options on foreign exchange and gold positions shall be based on the method set out in paragraph 199. For delta risk, the net delta-based equivalent of the foreign currency and gold options shall be incorporated into the measurement of the exposure for the respective currency (or gold) position.

(v) In addition to the above capital charges arising from delta risk, there shall be further capital charges for gamma and for vega risk. A bank using the delta-plus method shall be required to calculate the gamma and vega for each option position (including hedge positions) separately. The capital charges shall be calculated in the following way:

(a) for each individual option a 'gamma impact' shall be calculated according to a Taylor series expansion as:

Gamma impact = ½ x Gamma x VU^2

where VU = Variation of the underlying of the option.

(b) VU shall be calculated as follows:

(i) for interest rate options if the underlying is a bond, the price sensitivity shall be worked out as explained. An equivalent calculation shall be carried out where the underlying is an interest rate.

(ii) for options on equities and equity indices, which are not permitted at present, the market value of the underlying shall be multiplied by 9 per cent.

Explanation - The basic rules set out here for interest rate and equity options do not attempt to capture specific risk when

calculating gamma capital charges. However, Reserve Bank may require specific banks to do so.

(iii) for foreign exchange and gold options, the market value of the underlying shall be multiplied by 9 per cent.

(c) For this calculation the following positions shall be treated as the same underlying:

(i) for interest rates, each time-band as set out in Table 35 (with separate maturity ladders for each currency);

(ii) for equities and stock indices, each national market; and

(iii) for foreign currencies and gold, each currency pair and gold.

(d) Each option on the same underlying will have a gamma impact that is either positive or negative. These individual gamma impacts shall be summed, resulting in a net gamma impact for each underlying that is either positive or negative. Only those net gamma impacts that are negative shall be included in the capital calculation.

(e) The total gamma capital charge shall be the sum of the absolute value of the net negative gamma impacts as calculated above.

(f) For volatility risk, a bank shall be required to calculate the capital charges by multiplying the sum of the Vegas for all options on the same underlying, as defined above, by a proportional shift in volatility of ± 25 per cent.

(g) The total capital charge for vega risk shall be the sum of the absolute value of the individual capital charges that have been calculated for vega risk.

(2) Scenario approach

(i) A more sophisticated bank shall also have the option to calculate the market risk capital charge for options portfolios and associated hedging positions based on scenario matrix analysis. This shall be accomplished by specifying a fixed range of changes in the option portfolio's risk factors and calculating changes in the value of the option portfolio at various points

along this ‘grid’. For calculating the capital charge, the bank shall revalue the option portfolio using matrices for simultaneous changes in the option’s underlying rate or price and in the volatility of that rate or price. A different matrix shall be set up for each individual underlying as defined in paragraph 211(1)(v) above. As an alternative, a bank which is significant trader in options for interest rate options shall be permitted to base the calculation on a minimum of six sets of time-bands. When using this method, not more than three of the time-bands as define in Table 35 shall be combined into any one set.

(ii) The options and related hedging positions shall be evaluated over a specified range above and below the current value of the underlying. The range for interest rates is consistent with the assumed changes in yield in Table 35. A bank using the alternative method for interest rate options set out in paragraph 211(2)(i) above shall use, for each set of time-bands, the highest of the assumed changes in yield applicable to the group to which the time-bands belong. The other ranges are ±9 per cent for equities and ±9 per cent for foreign exchange and gold. For all risk categories, at least seven observations (including the current observation) shall be used to divide the range into equally spaced intervals.

Explanation - If, for example, the time-bands 3 to 4 years, 4 to 5 years, and 5 to 7 years are combined for interest rate options, the highest assumed change in yield of these three bands shall be 0.75.

(iii) The second dimension of the matrix entails a change in the volatility of the underlying rate or price. A single change in the volatility of the underlying rate or price equal to a shift in volatility of + 25 per cent and - 25 per cent is expected to be sufficient in most cases. As circumstances warrant, however, the Reserve Bank may choose to require that a different change in volatility be used and / or that intermediate points on the grid be calculated.

(iv) After calculating the matrix, each cell contains the net profit or loss of the option and the underlying hedge instrument. The capital charge for each

underlying shall then be calculated as the largest loss contained in the matrix.

(v) In drawing up these intermediate approaches it has been sought to cover the major risks associated with options. In doing so, it is noted that so far as specific risk is concerned, only the delta-related elements are captured; to capture other risks would necessitate a much more complex regime. On the other hand, in other areas the simplifying assumptions used have resulted in a relatively conservative treatment of certain options positions.

(vi) Besides the options risks mentioned above, the Reserve Bank is conscious of the other risks also associated with options, e.g., rho (rate of change of the value of the option with respect to the interest rate) and theta (rate of change of the value of the option with respect to time). While not proposing a measurement system for those risks at present, it expects a bank undertaking significant options business at the very least to monitor such risks closely. Additionally, a bank shall be permitted to incorporate rho into its capital calculations for interest rate risk if it wishes to do so.

D.7 Aggregation of the capital charge for market risks

212. For computing the total capital charge and RWA for market risks, the calculations shall be plotted in the following table:

Table 45: Computation of total capital charge and RWA for market risk

(₹ in crore)

Risk Category	Capital charge	RWA
I. **Interest Rate (a+b)**		12.5 times the capital charge
a. General market risk		
i) Net position (parallel shift) ii) Horizontal disallowance (curvature) iii) Vertical disallowance (basis) iv) Options		
b. Specific risk		
II. **Equity (a+b)**		12.5 times the capital charge
a. General market risk		
b. Specific risk		
III. **Foreign Exchange and Gold**		12.5 times the capital charge

Risk Category	Capital charge	RWA
IV. **Total capital charge and RWA for market risks** (I+II+III)		

D.8 Treatment for illiquid positions

213. Requirements related to Prudent Valuation

A bank shall have a framework for prudent valuation practices (for positions that are accounted for at fair value) which, at the minimum, shall contain the following:

(1) Systems and Controls

A bank shall establish and maintain adequate systems and controls sufficient to give management and supervisors the confidence that its valuation estimates are prudent and reliable. These systems shall be integrated with other risk management systems within a bank (such as credit analysis). Such systems shall include:

(i) Documented policies and procedures for the process of valuation: This includes clearly defined responsibilities of the various areas involved in the determination of the valuation, sources of market information and review of their appropriateness, guidelines for the use of unobservable inputs reflecting the bank's assumptions of what market participants would use in pricing the position, frequency of independent valuation, timing of closing prices, procedures for adjusting valuations, end of the month and ad-hoc verification procedures; and

(ii) Clear and independent (i.e., independent of front office) reporting lines for the department accountable for the valuation process.

(2) Valuation methodologies

(i) Marking to market

(a) A bank shall mark-to-market to the extent possible. The more prudent side of bid / offer shall be used unless the bank is a significant market maker in a particular position type and it can close out at mid-market.

(b) A bank shall maximise the use of relevant observable inputs and minimise the use of unobservable inputs when estimating fair value

using a valuation technique. However, observable inputs or transactions may not be relevant, such as in a forced liquidation or distressed sale, or transactions may not be observable, such as when markets are inactive. In such cases, the observable data shall be considered, but may not be determinative.

Explanation – Marking-to-market is the valuation of positions at least on a daily basis at readily available close out prices in orderly transactions that are sourced independently. Examples of readily available close out prices include exchange prices, screen prices, or quotes from several independent reputable brokers.

(ii) Marking to model

Where marking-to-market is not possible, a bank shall follow the instructions on valuation of investments in the Reserve Bank of India (Commercial Banks – Classification, Valuation, and Operation of Investment Portfolio) Directions, 2025. For investment and derivative positions other than those covered in the Master Direction *ibid*, the valuation model used by a bank shall be demonstrated to be prudent. When marking to valuation model other than that prescribed in the Reserve Bank / FIMMDA guidelines, an extra degree of conservatism is appropriate. Reserve Bank will consider the following in assessing whether a mark-to-model valuation is prudent:

(a) Senior management shall be aware of the elements of the trading book or of other fair-valued positions which are subject to mark to model and shall understand the materiality of the uncertainty this creates in the reporting of the risk / performance of the business.

(b) Market inputs shall be sourced, to the extent possible, in line with market prices (as discussed above). The appropriateness of the

market inputs for the particular position being valued shall be reviewed regularly.

(c) Where available, generally accepted valuation methodologies for particular products shall be used as far as possible.

(d) Where the model is developed by the bank itself, it shall be based on appropriate assumptions, which have been assessed and challenged by suitably qualified parties independent of the development process. The model shall be developed or approved independently of the front office. It shall be independently tested. This includes validating the mathematics, the assumptions and the software implementation.

(e) There shall be formal change control procedures in place and a secure copy of the model shall be held and periodically used to check valuations.

(f) Risk management shall be aware of the weaknesses of the models used and how best to reflect those in the valuation output.

(g) The model shall be subject to periodic review to determine the accuracy of its performance (e.g., assessing continued appropriateness of the assumptions, analysis of P&L versus risk factors, comparison of actual close out values to model outputs).

(h) Valuation adjustments shall be made as appropriate, for example, to cover the uncertainty of the model valuation.

Explanation – Marking-to model is defined as any valuation which has to be benchmarked, extrapolated or otherwise calculated from a market input.

(iii) Independent Price Verification

(a) Independent price verification is distinct from daily mark-to-market. It is the process by which market prices or model inputs are regularly verified for accuracy. While daily marking-to-market may be performed by dealers, verification of market prices or model inputs shall be performed by a unit independent of the dealing room, at least monthly (or, depending on the nature of the market / trading activity,

more frequently). It need not be performed as frequently as daily mark-to-market, since the objective, i.e., independent, marking of positions shall reveal any error or bias in pricing, which shall result in the elimination of inaccurate daily marks.

(b) Independent price verification entails a higher standard of accuracy in that the market prices or model inputs are used to determine profit and loss figures, whereas daily marks are used primarily for management reporting in between reporting dates. For independent price verification, where pricing sources are more subjective, e.g., only one available broker quote, prudent measures such as valuation adjustments may be appropriate.

(iv) Valuation adjustments

(a) As part of its procedures for marking to market, a bank shall establish and maintain procedures for considering valuation adjustments. A bank using third-party valuations shall consider whether valuation adjustments are necessary. Such considerations are also necessary when marking to model.

(b) At a minimum, a bank shall consider the following valuation adjustments while valuing its derivatives portfolios:

(i) incurred CVA losses;

Explanation – Provisions against incurred CVA losses are akin to specific provisions required on impaired assets and depreciation in case of investments held in the Trading Book. These provisions shall be in addition to the general provisions at 0.4 per cent required on the positive MTM values. The provisions against incurred CVA losses may be netted off from the exposure value while calculating capital charge for default risk under the Current Exposure Method as required in terms of paragraph 85(2).

(ii) close-out costs, which factor in the cost of eliminating the market risk of the portfolio;

(iii) operational risks;

(iv) early termination, investing and funding costs (i.e., the cost of funding and investing cash flow mismatches at rates different from the rate which models typically assume);

(v) future administrative costs, which relate to the cost that will be incurred to administer the portfolio; and

(vi) where appropriate, model risk.

(c) A bank shall follow any recognised method / model to compute the above adjustments except provisions against incurred CVA losses. However, a bank shall use the following formula to calculate incurred CVA loss on derivatives transactions:

$$\mathbf{ICVAL_t = Max\ [0,\{(EE_t * RP_t) - (EE_0 * RP_0)\}]}$$

Where;

$ICVAL_t$ = Cumulative Incurred CVA loss at time 't'.

EE_t = Value of counterparty exposure projected after one year from 't' and discounted back to 't' using CEM and a risk free discount rate for one year

EE_0 = Counterparty exposure estimated at time '0' using CEM

RP_t = Credit spread of the counterparty as reflected in the CDS or bond

(d) In cases where market-based credit spreads are not available, risk premium applicable to the counterparty according to its credit grade as per the internal credit rating system of the bank used for pricing / loan approval purposes at time 't' shall be used.

RP_0 = Credit spread of the counterparty as reflected in the CDS or bond prices.

(e) In cases where market-based credit spreads are not available, risk premium applicable to the counterparty according to its credit grade as per the internal credit rating system of the bank used for pricing / loan approval purposes at time '0', i.e., the date of the transaction.

Explanation – The instructions in this paragraph are especially important for positions without actual market prices or observable inputs to

valuation, as well as less liquid positions which raise supervisory concerns about prudent valuation. The valuation guidance in this paragraph is not intended to require a bank to change valuation procedures for financial reporting purposes.

(3) Adjustment to the current valuation of less liquid positions for regulatory capital purposes

(i) A bank shall establish and maintain procedures for judging the necessity of and calculating an adjustment to the current valuation of less liquid positions for regulatory capital purposes. This adjustment shall be in addition to any changes to the value of the position required for financial reporting purposes and shall be designed to reflect the illiquidity of the position. An adjustment to a position's valuation to reflect current illiquidity shall be considered whether the position is marked to market using market prices or observable inputs, third-party valuations or marked to model.

(ii) Since assumptions made about liquidity in the market risk capital charge may not be consistent with the bank's ability to sell or hedge out less liquid positions where appropriate, a bank shall make an adjustment to the current valuation of these positions and review their continued appropriateness on an on-going basis. Reduced liquidity may have arisen from market events. Additionally, close-out prices for concentrated positions and / or stale positions shall be considered in establishing the adjustment. While the Reserve Bank has not prescribed any particular methodology for calculating the amount of valuation adjustment on account of illiquid positions, a bank shall consider all relevant factors when determining the appropriateness of the adjustment for less liquid positions. These factors shall include, but are not limited to, the amount of time it would take to hedge out the position / risks within the position, the average volatility of bid / offer spreads, the availability of independent market quotes (number and identity of market makers), the average and volatility of trading volumes (including trading volumes during periods of market stress), market concentrations, the aging of positions, the extent to which valuation relies on marking-to-model, and the impact of other model risks not included in this paragraph. The valuation adjustment on account of illiquidity shall be

considered irrespective of whether the guidelines issued by FIMMDA have taken into account the illiquidity premium or not, while fixing YTM / spreads for the purpose of valuation.

(iii) For complex products including, but not limited to, securitisation exposures, a bank shall explicitly assess the need for valuation adjustments to reflect two forms of model risk:

(a) the model risk associated with using a possibly incorrect valuation methodology; and

(b) the risk associated with using unobservable (and possibly incorrect) calibration parameters in the valuation model.

(iv) The adjustment to the current valuation of less liquid positions made under paragraph 213(3)(ii) shall not be debited to profit and loss account but shall be deducted from CET1 capital while computing CRAR of the bank. The adjustment may exceed those valuation adjustments made under financial reporting / Accounting Standards and paragraph 213(2)(iv).

(v) In calculating the eligible capital for market risk, a bank shall first calculate the minimum capital requirement for credit and operational risk and only afterwards its market risk requirement to establish the components of capital that are available to support market risk.

E Capital charge for operational risk

E.1 The measurement methodology

214. A bank shall compute the capital requirements for operational risk under the Basic Indicator Approach. The Reserve Bank shall review the capital requirement arrived at by the Basic Indicator Approach for general credibility, especially in relation to a bank's peers, and in the event that credibility is lacking, appropriate supervisory action under Pillar 2 shall be considered.

E.2 The Basic Indicator Approach

215. A bank shall hold capital for operational risk equal to the average over the previous three years of a fixed percentage (denoted as alpha) of positive annual gross income. Figures for any year in which annual gross income is negative or zero shall be excluded from both the numerator and denominator when

calculating the average. If negative gross income distorts a bank's Pillar 1 capital charge, the Reserve Bank shall consider appropriate supervisory action under Pillar 2. The capital charge is expressed as follows:

$$K_{BIA} = [\sum (GI_{1\ldots n} \times \alpha)] / n$$

Where:

K_{BIA} = the capital charge under the Basic Indicator Approach

GI = annual gross income, where positive, over the previous three years

n = number of the previous three years for which gross income is positive

α = 15 per cent, which is set by the BCBS, relating the industry wide level of required capital to the industry wide level of the indicator.

216. Gross income is defined as 'net interest income' plus 'net non-interest income'. Gross income shall:

(i) be gross of any provisions (e.g., for unpaid interest) and write-offs made during the year;

(ii) be gross of operating expenses (such as fees paid to outsourcing service providers, in addition to fees paid for services that are outsourced), and fees received by a bank for providing outsourcing services;

(iii) exclude reversal during the year in respect of provisions and write-offs made during the previous year(s);

(iv) exclude income recognised from the disposal of items of movable and immovable property;

(v) exclude realised profits / losses from the sale of securities in the 'banking book';

(vi) exclude income from legal settlements in favour of the bank;

(vii) exclude other extraordinary or irregular items of income and expenditure; and

(viii) exclude income derived from insurance activities (i.e., income derived by writing insurance policies) and from insurance claims in favour of the bank.

217. A bank shall compute capital charge for operational risk under the Basic Indicator Approach as follows:

(i) Average of [Gross Income * alpha(α)] for each of the last three financial years, excluding years of negative or zero gross income as mentioned in paragraph 215.

(ii) Gross income = Net profit (+) Provisions & contingencies (+) Operating expenses (Schedule 16) (–) items (iii) to (viii) of paragraph 216.

(iii) Alpha (α) = 15 per cent

218. As a point of entry for capital calculation, no specific criteria for use of the Basic Indicator Approach are set out in these guidelines. However, a bank is encouraged to comply with the 'Guidance Note on Operational Risk Management and Operational Resilience' issued by the Reserve Bank of India. Further, a bank is also encouraged to be in readiness for migrating to the new Standardised Approach prescribed in 'Reserve Bank of India (Commercial Banks – Forthcoming Instructions) Directions, 2025'.

219. The capital charge for operational risk calculated under the Basic Indicator Approach shall be multiplied with 12.5 to arrive at the notional RWA for operational risk.

Chapter V

Supervisory Review and Evaluation Process (SREP) and Market Discipline

A Introduction to SREP under Pillar 2

220. The objective of the SREP is to ensure that a bank has adequate capital to support all the risks in its business as also to encourage it to develop and use better risk management techniques for monitoring and managing risks. This in turn would require a well-defined internal assessment process within the bank through which it assures the RBI that adequate capital is indeed held towards the various risks to which it is exposed. The process of assurance could also involve an active dialogue between the bank and the RBI so that, when warranted, appropriate intervention could be made to either reduce the risk exposure of the bank or augment / restore its capital. Thus, Internal Capital Adequacy Assessment Process (ICAAP) is an important component of the SREP.

221. The main aspects to be addressed under the SREP, and therefore, under the ICAAP, shall be as under:

    (i) the risks that are not fully captured by the minimum capital ratio prescribed under Pillar 1;

    (ii) the risks that are not at all taken into account by the Pillar 1; and

    (iii) the factors external to a bank.

222. Since the capital adequacy ratio prescribed by the Reserve Bank under the Pillar 1 is only the regulatory minimum level, addressing only the three specified risks (viz., credit, market and operational risks), holding additional capital might be necessary for banks, on account of both – the possibility of some under-estimation of risks under the Pillar 1 and the actual risk exposure of a bank vis-à-vis the quality of its risk management architecture. Illustratively, some of the risks that the banks are generally exposed to but which are not captured or not fully captured in the regulatory CRAR would include:

    (i) Interest rate risk in the banking book;

    (ii) Credit concentration risk;

(iii) Liquidity risk;

(iv) Settlement risk;

(v) Reputational risk;

(vi) Strategic risk;

(vii) Risk of under-estimation of credit risk under the standardised approach;

(viii) Model risk;

(ix) Risk of weakness in the credit-risk mitigants;

(x) Residual risk of securitisation;

(xi) Cyber security / IT infrastructure risk;

(xii) Human capital risk;

(xiii) Group risk;

(xiv) Outsourcing / vendor management risk; and

(xv) Collateral risk.

223. The quantification of currency induced credit risk shall form a part of a bank's ICAAP and a bank is expected to address this risk in a comprehensive manner. The ICAAP should measure the extent of currency induced credit risk the bank is exposed to and also concentration of such exposures. A bank may also like to perform stress tests under various extreme but plausible exchange rate scenarios under ICAAP. Outcome of ICAAP may lead a bank to take appropriate risk management actions like risk reduction, maintenance of more capital or provision, etc. It is, therefore, only appropriate that a bank makes its own assessment of various risk exposures, through a well-defined internal process, and maintain an adequate capital cushion for such risks.

Note: A bank shall refer to Reserve Bank of India (Commercial Banks – Credit Risk Management) Directions, 2025 which cover provision on unhedged foreign currency exposures.

224. Under ICAAP, a bank shall make its own assessment of its various risk exposures, through a well-defined internal process, and maintain an adequate

capital cushion for all such risks. The ICAAP would be in addition to a bank's calculation of regulatory capital requirements under Pillar 1.

225. The ICAAP document should, *inter alia,* include the capital adequacy assessment and projections of capital requirement for the ensuing year, along with the plans and strategies for meeting the capital requirement. An illustrative outline of a format of the ICAAP document is furnished at paragraph 238, for guidance of a bank though the ICAAP documents of a bank could vary in length and format, in tune with its size, level of complexity, risk profile, and scope of operations.

226. Key principles in regard to the SREP

(1) The Basel Committee also lays down the following four key principles in regard to the SREP envisaged under Pillar 2:

(i) Principle 1: A bank should have a process for assessing its overall capital adequacy in relation to its risk profile and a strategy for maintaining its capital levels.

(ii) Principle 2: Supervisors should review and evaluate a bank's internal capital adequacy assessments and strategies, as well as its ability to monitor and ensure compliance with the regulatory capital ratios. Supervisors should take appropriate supervisory action if they are not satisfied with the result of this process.

(iii) Principle 3: Supervisors should expect a bank to operate above the minimum regulatory capital ratios and should have the ability to require a bank to hold capital in excess of the minimum.

(iv) Principle 4: Supervisors should seek to intervene at an early stage to prevent capital from falling below the minimum levels required to support the risk characteristics of a particular bank and should require rapid remedial action if capital is not maintained or restored.

(2) Principles 1 and 3 relate to the supervisory expectations from a bank while the Principles 2 and 4 deal with the role of the supervisors under Pillar 2. Pillar 2 requires a bank to implement an internal process, called the ICAAP, for assessing its capital adequacy in relation to their risk profiles as well as a

strategy for maintaining their capital levels. Pillar 2 also requires the supervisory authorities to subject a bank to an evaluation process, hereafter called SREP, and to initiate such supervisory measures on that basis, as might be considered necessary.

(3) An analysis of the foregoing principles indicates that the following broad responsibilities have been cast on banks and the supervisors:

(i) Bank's responsibilities

(a) A bank should have in place a process for assessing its overall capital adequacy in relation to its risk profile and a strategy for maintaining its capital levels. (Principle 1)

(b) A bank should operate above the minimum regulatory capital ratios. (Principle 3)

(ii) Supervisor's responsibilities

(a) Supervisors should review and evaluate a bank's ICAAP. (Principle 2)

(b) Supervisors should take appropriate action if they are not satisfied with the results of this process. (Principle 2)

(c) Supervisors should review and evaluate a bank's compliance with the regulatory capital ratios. (Principle 2)

(d) Supervisors should have the ability to require a bank to hold capital in excess of the minimum. (Principle 3)

(e) Supervisors should seek to intervene at an early stage to prevent capital from falling below the minimum levels. (Principle 4)

(f) Supervisors should require rapid remedial action if capital is not maintained or restored. (Principle 4)

(4) Thus, the ICAAP and SREP are the two important components of Pillar 2 and could be broadly defined as follows:

(i) The ICAAP comprises a bank's procedures and measures designed to ensure the following:

(a) An appropriate identification and measurement of risks;

(b) An appropriate level of internal capital in relation to the bank's risk profile; and

(c) Application and further development of suitable risk management systems in a bank.

(ii) The SREP consists of a review and evaluation process adopted by the supervisor, which covers all the processes and measures defined in the principles listed above. Essentially, these include the review and evaluation of a bank's ICAAP, conducting an independent assessment of a bank's risk profile, and if necessary, taking appropriate prudential measures and other supervisory actions.

These Directions seek to provide broad guidance to a bank by outlining the manner in which the SREP would be carried out by the Reserve Bank, the expected scope and design of their ICAAP, and the expectations of the Reserve Bank from a bank in regard to implementation of the ICAAP.

227. Conduct of SREP by the Reserve Bank

(1) Regulatory capital ratios permit some comparative analysis of capital adequacy across regulated banking entities because they are based on certain common methodology / assumptions. However, supervisors need to perform a more comprehensive assessment of capital adequacy that considers risks specific to a bank, conducting analyses that go beyond minimum regulatory capital requirements.

(2) The Reserve Bank generally expects a bank to hold capital above its minimum regulatory capital levels, commensurate with its individual risk profiles, to account for all material risks. Under the SREP, the Reserve Bank will assess the overall capital adequacy of a bank through a comprehensive evaluation that takes into account all relevant available information.

(3) In determining the extent to which a bank should hold capital in excess of the regulatory minimum, the Reserve Bank would take into account the combined implications of the bank's compliance with regulatory minimum capital requirements, the quality and results of the bank's ICAAP, and supervisory assessment of the bank's risk management processes, control systems and other relevant information relating to the bank's risk profile and capital position.

(4) The SREP of a bank would, thus, be conducted as part of the Reserve Bank's Risk Based Supervision (RBS) of a bank and in the light of the data in the off-site returns received from bank in the Reserve Bank, in conjunction with the ICAAP

document, which is required to be submitted every year by a bank to the Reserve Bank as per paragraph 228(8)(iii)of these Directions.

(5) Through the SREP, the Reserve Bank would evaluate the adequacy and efficacy of the ICAAP of a bank and the capital requirements derived by them therefrom.

(6) While in the course of evaluation, there would be no attempt to reconcile the difference between the regulatory minimum CRAR and the outcome of the ICAAP of a bank (as the risks covered under the two processes are different), a bank would be expected to demonstrate to the Reserve Bank that the ICAAP adopted by it is fully responsive to its size, level of complexity, scope, and scale of operations and the resultant risk profile / exposures, and adequately captures its capital requirements. Such an evaluation of the effectiveness of the ICAAP would help the Reserve Bank in understanding the capital management processes and strategies adopted by a bank.

(7) If considered necessary, the SREP could also involve a dialogue between a bank's top management and the Reserve Bank from time to time.

(8) In addition to the periodic reviews, independent external experts may also be commissioned by the Reserve Bank, if deemed necessary, to perform ad hoc reviews and comment on specific aspects of the ICAAP process of a bank; the nature and extent of such a review would be determined by the Reserve Bank.

(9) Pillar 1 capital requirements will include a buffer for uncertainties surrounding the Pillar 1 regime that affect the banking population as a whole. Bank-specific uncertainties will be treated under Pillar 2. Buffers under Pillar 1 will be set to provide reasonable assurance that a bank with good internal systems and controls, a well-diversified risk profile and a business profile well covered by the Pillar 1 regime, and which operates with capital equal to Pillar 1 requirements, will meet the minimum goals for soundness embodied in Pillar 1. However, the Reserve Bank may require a particular bank to operate with a buffer, over and above the Pillar 1 standard. A bank should maintain this buffer for a combination of the following:

(i) Pillar 1 minimums are anticipated to be set to achieve a level of bank creditworthiness in markets that is below the level of creditworthiness sought by a bank for its own reasons. For example, most international

banks appear to prefer to be highly rated by internationally recognised rating agencies. Thus, a bank is likely to choose to operate above Pillar 1 minimums for competitive reasons.

(ii) In the normal course of business, the type and volume of activities may change, as will the different risk exposures, causing fluctuations in the overall capital ratio.

(iii) It may be costly for a bank to raise additional capital, especially if this needs to be done quickly or at a time when market conditions are unfavourable.

(iv) For a bank to fall below minimum regulatory capital requirements is a serious matter. It may place a bank in breach of the provisions of the BR Act, 1949 and / or attract prompt corrective action on the part of Reserve Bank.

(v) There may be risks, either specific to an individual bank, or more generally to an economy at large, that are not taken into account in Pillar 1. If a bank has identified some capital add-on to take care of an identified Pillar 2 risk or inadequately capitalised Pillar 1 risk, that add-on can be translated into risk weighted assets (RWAs) which should be added to the RWAs of the bank. No additional Pillar 2 buffer need be maintained for such identified risks.

(10) As a part of SREP under Pillar 2, Reserve Bank may review the risk management measures taken by a bank and its adequacy to manage currency induced credit risk, especially if exposure to such risks is assessed to be on higher side. A bank shall also refer to Reserve Bank of India (Commercial Banks – Credit Risk Management) Directions, 2025 which cover provision on unhedged foreign currency exposures.

(11) Under the SREP, the Reserve Bank would make an assessment as to whether a bank maintains adequate capital cushion to take care of the above situations. Such a cushion should be in addition to the CCB and CCCB, if any, required to be maintained by a bank according to the applicable guidelines. Such cushion would generally be reflected in more than minimum capital adequacy ratio maintained by a bank after taking into account CCB and CCCB.

(12) Under the SREP, the Reserve Bank would also seek to determine whether a bank's overall capital remains adequate as the underlying conditions change. Generally, material increases in risk that are not otherwise mitigated should be accompanied by commensurate increases in capital. Conversely, reductions in overall capital (to a level still above regulatory minima) may be appropriate if the Reserve Bank's supervisory assessment leads it to a conclusion that risk has materially declined or that it has been appropriately mitigated. Based on such assessment, the Reserve Bank could consider initiating appropriate supervisory measures to address its supervisory concerns. The measures could include requiring a modification or enhancement of the risk management and internal control processes of a bank, a reduction in risk exposures, or any other action as deemed necessary to address the identified supervisory concerns. These measures could also include the stipulation of a bank-specific additional capital requirement over and above what has been determined under Pillar 1.

(13) As and when the advanced approaches envisaged in the Basel capital adequacy framework are permitted to be adopted in India, the SREP would also assess the ongoing compliance by a bank with the eligibility criteria for adopting the advanced approaches.

B Internal capital adequacy assessment process (ICAAP) of a bank

228. The Structural aspects of the ICAAP

(1) Every bank shall have an ICAAP.

(2) The ICAAP shall be prepared, on a solo basis, at every tier for each banking entity within the banking group, as also at the level of the consolidated bank. This requirement shall also apply to a foreign bank operating in branch mode in India and its ICAAP shall cover its Indian operations only as per the scope of consolidation of the capital adequacy requirements.

(3) General firm-wide risk management principles

(i) Senior management should understand the importance of taking an integrated, firm-wide perspective of a bank's risk exposure, in order to support its ability to identify and react to emerging and growing risks in a timely and effective manner. The purpose of this guidance is the need to enhance firm-wide oversight, risk management and controls around a

bank's capital markets activities, including securitisation, off-balance sheet exposures, structured credit, and complex trading activities.

(ii) A sound risk management system should have the following key features:

(a) Active board and senior management oversight;

(b) Appropriate policies, procedures and limits;

(c) Comprehensive and timely identification, measurement, mitigation, controlling, monitoring and reporting of risks;

(d) Appropriate management information systems (MIS) at the business and bank-wide level; and

(e) Comprehensive internal controls.

(4) Board and senior management oversight:

(i) The ultimate responsibility for designing and implementation of the ICAAP shall be with the Board of Directors of a bank (in case of a bank incorporated in India including a foreign bank operating under the WOS model) and with the Chief Executive Officer (in the case of the foreign bank operating in branch mode in India).

(ii) A bank's risk function and its chief risk officer (CRO) or equivalent position shall be independent of the individual business lines and report directly to the chief executive officer (CEO) / Managing Director and the institution's board of directors or its committee in line with extant requirements. In addition, the risk function shall highlight to senior management and the board risk management concerns, such as risk concentrations and violations of risk appetite limits.

(iii) Since the risk management process provides the basis for ensuring that a bank maintains adequate capital, the Board of Directors of a bank shall set the tolerance level for risk.

(iv) It shall be the responsibility of the Board of Directors and senior management to define the institution's risk appetite and to ensure that a bank's risk management framework includes detailed policies that set

specific firm-wide prudential limits on a bank's activities, which are consistent with its risk-taking appetite and capacity.

(v) To determine the overall risk appetite, the Board and senior management shall first have an understanding of risk exposures on a firm-wide basis. To achieve this understanding, the appropriate members of senior management shall bring together the perspectives of the key business and control functions.

(vi) To develop an integrated firm-wide perspective on risk, senior management shall overcome organisational silos between business lines and share information on market developments, risks, and risk mitigation techniques. As the banking industry is exhibiting the tendency to move increasingly towards market-based intermediation, there is a greater probability that many areas of a bank may be exposed to a common set of products, risk factors or counterparties. Senior management should establish a risk management process that is not limited to credit, market, liquidity, and operational risks, but incorporates all material risks. This includes reputational and strategic risks, as well as risks that do not appear to be significant in isolation, but when combined with other risks could lead to material losses.

(vii) The Board of Directors and senior management should possess sufficient knowledge of all major business lines to ensure that appropriate policies, controls and risk monitoring systems are effective. They should have the necessary expertise to understand the capital markets activities in which a bank is involved - such as securitisation and off-balance sheet activities - and the associated risks. The Board and senior management should remain informed on an on-going basis about these risks as financial markets, risk management practices and a bank's activities evolve.

(viii) The Board and senior management should ensure that accountability and lines of authority are clearly delineated. With respect to new or complex products and activities, senior management should understand the underlying assumptions regarding business models, valuation, and risk

management practices. In addition, senior management should evaluate the potential risk exposure if those assumptions fail.

(ix) Before embarking on new activities or introducing products new to the institution, the Board and senior management should identify and review the changes in firm-wide risks arising from these potential new products or activities and ensure that the infrastructure and internal controls necessary to manage the related risks are in place. In this review, a bank should also consider the possible difficulty in valuing the new products and how they might perform in a stressed economic environment. The Board should ensure that the senior management of a bank:

(a) establishes a risk framework in order to assess and appropriately manage the various risk exposures of a bank;

(b) develops a system to monitor a bank's risk exposures and to relate them to a bank's capital and reserve funds;

(c) establishes a method to monitor a bank's compliance with internal policies, particularly in regard to risk management; and

(d) effectively communicates all relevant policies and procedures throughout a bank.

(5) Policies, procedures, limits and controls:

(i) The structure, design and contents of a bank's ICAAP should be approved by the Board of Directors to ensure that the ICAAP forms an integral part of the management process and decision-making culture of a bank.

(ii) Firm-wide risk management programmes should include detailed policies that set specific firm-wide prudential limits on the principal risks relevant to a bank’s activities.

(iii) A bank’s policies and procedures should provide specific guidance for the implementation of broad business strategies and should establish, where appropriate, internal limits for the various types of risks to which a bank may be exposed. These limits should consider a bank’s role in the financial system and be defined in relation to a bank’s capital, total assets, earnings or, where adequate measures exist, its overall risk level.

(iv) A bank's policies, procedures and limits shall:

(a) Provide for adequate and timely identification, measurement, monitoring, control and mitigation of the risks posed by its lending, investing, trading, securitisation, off-balance sheet, fiduciary and other significant activities at the business line and firm-wide levels;

(b) Ensure that the economic substance of a bank's risk exposures, including reputational risk and valuation uncertainty, are fully recognised and incorporated into its risk management processes;

(c) Be consistent with a bank's stated goals and objectives, as well as its overall financial strength;

(d) Clearly delineate accountability and lines of authority across the bank's various business activities, and ensure there is a clear separation between business lines and the risk function;

(e) Escalate and address breaches of internal position limits;

(f) Provide for the review of new businesses and products by bringing together all relevant risk management, control, and business lines to ensure that a bank is able to manage and control the activity prior to it being initiated; and

(g) Include a schedule and process for reviewing the policies, procedures, and limits and for updating them as appropriate.

(6) Identifying, measuring, monitoring, and reporting of risk

(i) A bank's MIS should provide the Board and senior management in a clear and concise manner with timely and relevant information concerning its institutions' risk profile. This information should include all risk exposures, including those that are off-balance sheet.

(ii) Management should understand the assumptions behind and limitations inherent in specific risk measures. The key elements necessary for the aggregation of risks are an appropriate infrastructure and MIS that allow for the aggregation of exposures and risk measures across business lines and support customised identification of concentrations and emerging risks. MIS developed to achieve this objective should support the ability to

evaluate the impact of various types of economic and financial shocks that affect the whole of the financial institution.

(iii) Further, a bank's systems should be flexible enough to incorporate hedging and other risk mitigation actions to be carried out on a firm-wide basis while taking into account the various related basis risks.

(iv) To enable proactive management of risk, the Board and senior management need to ensure that MIS is capable of providing regular, accurate and timely information on a bank's aggregate risk profile, as well as the main assumptions used for risk aggregation.

(v) MIS should be:

(a) adaptable and responsive to changes in a bank's underlying risk assumptions and should incorporate multiple perspectives of risk exposure to account for uncertainties in risk measurement;

(b) sufficiently flexible so that the institution can generate forward-looking bank-wide scenario analyses that capture management's interpretation of evolving market conditions and stressed conditions;

(c) capable of capturing limit breaches and there should be procedures in place to promptly report such breaches to senior management, as well as to ensure that appropriate follow-up actions are taken. For instance, similar exposures should be aggregated across business platforms (including the banking and trading books) to determine whether there is a concentration or a breach of an internal position limit.

(vi) Third-party inputs or other tools used within MIS (e.g., credit ratings, risk measures, models) should be subject to initial and ongoing validation.

(7) Internal controls: Risk management processes should be frequently monitored and tested by independent control areas and internal, as well as external auditor. The aim is to ensure that the information on which decisions are based is accurate so that processes fully reflect management policies and that regular reporting, including the reporting of limit breaches and other exception-based reporting, is undertaken effectively. The risk management function of a bank shall

be independent of the business lines in order to ensure an adequate separation of duties and to avoid conflicts of interest.

(8) Submission of the outcome of the ICAAP to the Board and the Reserve Bank

(i) As the ICAAP is an ongoing process, a written record on the outcome of the ICAAP shall be periodically submitted by a bank to its Board of Directors. It shall include *inter alia*, the risks identified, the manner in which those risks are monitored and managed, the impact of a bank's changing risk profile on the bank's capital position, details of stress tests / scenario analysis conducted and the resultant capital requirements.

(ii) The reports shall be sufficiently detailed to allow the Board of Directors to evaluate the level and trend of material risk exposures, whether a bank maintains adequate capital against the risk exposures and in case of additional capital being needed, the plan for augmenting capital. The Board of Directors shall make timely adjustments to the strategic plan, as necessary.

(iii) Based on the outcome of the ICAAP as submitted to and approved by the Board, the ICAAP Document, in the format furnished at paragraph 238, shall be furnished to the Reserve Bank (i.e., to the CGM-in-Charge, DoS, Central Office, Reserve Bank of India, with a copy addressed to Senior Supervisory Manager of the bank). The document shall reach the Reserve Bank latest by end of the first quarter (i.e., April-June) of the relevant financial year.

229. Review of the ICAAP outcomes

(1) The Board of Directors shall, at least once a year, assess and document whether the processes relating to the ICAAP implemented by a bank successfully achieve the objectives envisaged by the Board.

(2) The senior management should receive and review the reports regularly to evaluate the sensitivity of the key assumptions and to assess the validity of a bank's estimated future capital requirements. In the light of such an assessment, appropriate changes in the ICAAP should be instituted to ensure that the underlying objectives are effectively achieved.

(3) The ICAAP should form an integral part of the management and decision-making culture of a bank. This integration could range from using the ICAAP to internally allocate capital to various business units, to having it play a role in the individual credit decision process and pricing of products or more general business decisions such as expansion plans and budgets. The integration would also mean that ICAAP should enable a bank's management to assess, on an ongoing basis, the risks that are inherent in their activities and material to the institution.

230. The Principle of Proportionality

(1) The implementation of ICAAP shall be guided by the principle of proportionality. Though a bank is encouraged to migrate to and adopt progressively sophisticated approaches in designing its ICAAP, the Reserve Bank would expect the degree of sophistication adopted in the ICAAP in regard to risk measurement and management to be commensurate with the nature, scope, scale, and the degree of complexity in a bank's business operations.

(2) Given below is the broad approach which could be considered by a bank with varying levels of complexity in its operations, in formulating its ICAAP:

(i) In relation to a bank that defines its activities and risk management practices as simple, in carrying out its ICAAP, the bank can:

(a) identify and consider that bank's largest losses over the last 3 to 5 years and whether those losses are likely to recur;

(b) prepare a short list of the most significant risks to which that bank is exposed;

(c) consider how that bank would act, and the amount of capital that would be absorbed in the event that each of the risks identified were to materialise;

(d) consider how that bank's capital requirement might alter under the scenarios in paragraph 230(2)(i)(c) above) above and how its capital requirement might alter in line with its business plans for the next 3 to 5 years; and

(e) document the ranges of capital required in the scenarios identified above and form an overall view on the amount and quality of capital

which that bank should hold, ensuring that its senior management is involved in arriving at that view.

(ii) In relation to a bank that defines its activities and risk management practices as moderately complex, in carrying out its ICAAP, the bank can:

(a) having consulted the operational management in each major business line, prepare a comprehensive list of the major risks to which the business is exposed;

(b) estimate, with the aid of historical data, where available, the range and distribution of possible losses which might arise from each of those risks and consider using shock stress tests to provide risk estimates;

(c) consider the extent to which that bank's capital requirement adequately captures the risks identified in paragraph 230(2)(ii)(a) and 230(2)(ii)(b) above;

(d) for areas in which the capital requirement is either inadequate or does not address a risk, estimate the additional capital needed to protect the bank and its customers, in addition to any other risk mitigation action the bank plans to take;

(e) consider the risk that a bank's own analyses of capital adequacy may be inaccurate and that it may suffer from management weaknesses which affect the effectiveness of its risk management and mitigation;

(f) project the bank's business activities forward in detail for one year and in less detail for the next 3 to 5 years, and estimate how the bank's capital and capital requirement would alter, assuming that business develops as expected;

(g) assume that business does not develop as expected and consider how the bank's capital and capital requirement would alter and what the bank's reaction to a range of adverse economic scenarios might be;

(h) document the results obtained from the analyses in (b), (d), (f), and (g) above in a detailed report for the bank's top management / board of directors; and

(i) ensure that systems and processes are in place to review the accuracy of the estimates made in (b), (d), (f), and (g) above (i.e., systems for back testing) vis-à-vis the performance / actuals.

(iii) In relation to a bank that defines its activities and risk management practices as complex, in carrying out its ICAAP, the bank can follow a proportional approach to the bank's ICAAP which shall cover the issues identified at (a) to (d) in paragraph 230(2)(ii) above but is likely also to involve the use of models, most of which will be integrated into its day-to-day management and operations.

(iv) Models of the kind referred to above may be linked so as to generate an overall estimate of the amount of capital that a bank considers appropriate to hold for its business needs. A bank may also link such models to generate information on the economic capital considered desirable for that bank. A model which a bank uses to generate its target amount of economic capital is known as an economic capital model. Economic capital is the target amount of capital which optimises the return for a bank's stakeholders for a desired level of risk. For example, a bank is likely to use value-at-risk (VaR) models for market risk and advanced modelling approaches for credit risk. A bank might also use economic scenario generators to model stochastically its business forecasts and risks. However, a bank shall take prior approval of the Reserve Bank for migrating to the advanced approaches. Such a bank is also likely to be part of a group and to be operating internationally. There is likely to be centralised control over the models used throughout the group, the assumptions made and their overall calibration.

231. Regular independent review and validation

(1) The ICAAP shall be subject to regular and independent review through an internal or external audit process, separately from the SREP conducted by the Reserve Bank, to ensure that the ICAAP is comprehensive and proportionate to the nature, scope, scale, and level of complexity of a bank's activities so that it accurately reflects the major sources of risk that a bank is exposed to.

(2) A bank shall ensure appropriate and effective internal control structures, particularly in regard to the risk management processes, in order to monitor a bank's continued compliance with internal policies and procedures. As a minimum, a bank shall conduct periodic reviews of its risk management processes, which shall ensure:

(i) the integrity, accuracy, and reasonableness of the processes;

(ii) the appropriateness of a bank's capital assessment process based on the nature, scope, scale and complexity of a bank's activities;

(iii) the timely identification of any concentration risk;

(iv) the accuracy and completeness of any data inputs into a bank's capital assessment process;

(v) the reasonableness and validity of any assumptions and scenarios used in the capital assessment process; and

(vi) that the bank conducts appropriate stress testing.

232. ICAAP to be a forward-looking process

(1) The ICAAP shall be forward looking in nature, and thus, shall take into account the expected estimated future developments such as strategic plans, macro-economic factors, etc., including the likely future constraints in the availability and use of capital. As a minimum, the management of a bank shall develop and maintain an appropriate strategy that would ensure that the bank maintains adequate capital commensurate with the nature, scope, scale, complexity and risks inherent in the bank's on-balance-sheet and off-balance-sheet activities, and should demonstrate as to how the strategy dovetails with the macro-economic factors.

(2) A bank shall have an explicit, Board-approved capital plan which should spell out the institution's objectives in regard to level of capital, the time horizon for achieving those objectives, and in broad terms, the capital planning process and the allocated responsibilities for that process.

233. ICAAP to be a risk-based process

(1) A bank shall set its capital targets which are consistent with its risk profile and operating environment.

(2) ICAAP shall include all material risk exposures incurred by the bank. There are some types of risks (such as reputation risk and strategic risk) which are less readily quantifiable; for such risks, the focus of the ICAAP should be more on qualitative assessment, risk management and mitigation than on quantification of such risks.

(3) A bank's ICAAP document shall clearly indicate for which risks a quantitative measure is considered warranted, and for which risks a qualitative measure is considered to be the correct approach.

234. ICAAP to include stress tests and scenario analyses

(1) As part of the ICAAP, a bank shall, as a minimum, conduct relevant stress tests periodically, particularly in respect of a bank's material risk exposures, in order to evaluate the potential vulnerability of a bank to some unlikely but plausible events or movements in the market conditions that could have an adverse impact on a bank.

(2) The use of stress testing framework can provide a bank's management a better understanding of a bank's likely exposure in extreme circumstances. Annex IV of these Directions contains guidelines on overall objectives, governance, design and implementation of stress testing programmes to be implemented by a bank. A bank is urged to take necessary measures for implementing an appropriate formal stress testing framework which would also meet the stress testing requirements under the ICAAP of the banks.

235. Use of capital models for ICAAP

(1) While the Reserve Bank does not expect a bank to use complex and sophisticated econometric models for internal assessment of its capital requirements, and there is no Reserve Bank-mandated requirement for adopting such models, a bank, with international presence, is required to develop suitable methodologies for estimating and maintaining economic capital. However, a bank, which has relatively complex operations and is adequately equipped in this regard, may like to place reliance on such models as part of its ICAAP.

(2) While there is no single prescribed approach as to how a bank should develop its capital model, a bank adopting a model-based approach to its ICAAP shall be able to, inter alia, demonstrate:

(i) Well documented model specifications, including the methodology / mechanics and the assumptions underpinning the working of the model;

(ii) The extent of reliance on the historical data in the model and the system of back testing to be carried out to assess the validity of the outputs of the model vis-à-vis the actual outcomes;

(iii) A robust system for independent validation of the model inputs and outputs;

(iv) A system of stress testing the model to establish that the model remains valid even under extreme conditions / assumptions;

(v) The level of confidence assigned to the model outputs and its linkage to a bank's business strategy; and

(vi) The adequacy of the requisite skills and resources within a bank to operate, maintain and develop the model.

C Select operational aspects of the internal capital adequacy assessment process (ICAAP)

This paragraph outlines in greater detail the scope of the risk universe expected to be normally captured by a bank in its ICAAP.

236. Identifying and measuring material risks in ICAAP

(1) The first objective of an ICAAP is to identify all material risks. Risks that can be reliably measured and quantified should be treated as rigorously as data and methods allow. The appropriate means and methods to measure and quantify those material risks are likely to vary across banks.

(2) The Reserve Bank has issued guidelines to banks on asset liability management, management of country risk, credit risk, operational risk, etc., from time to time. A bank's risk management processes, including its ICAAP, should, therefore, be consistent with this existing body of guidance. However, certain other risks, such as reputational risk and business or strategic risk, may be equally important for a bank and, in such cases, should be given same consideration as the more

formally defined risk types. For example, a bank may be engaged in businesses for which periodic fluctuations in activity levels, combined with relatively high fixed costs, have the potential to create unanticipated losses that shall be supported by adequate capital. Additionally, a bank might be involved in strategic activities (such as expanding business lines or engaging in acquisitions) that introduce significant elements of risk and for which additional capital would be appropriate.

(3) If a bank employs risk mitigation techniques, it should understand the risk to be mitigated and the potential effects of that mitigation, reckoning its enforceability and effectiveness, on the risk profile of a bank.

237. Scope of risk universe to be captured in ICAAP

(1) Credit risk:

(i) A bank should have methodologies that enable them to assess the credit risk involved in exposures to individual borrowers or counterparties as well as at the portfolio level. A bank should be particularly attentive to identifying credit risk concentrations and ensuring that their effects are adequately assessed. This should include consideration of various types of dependence among exposures, incorporating the credit risk effects of extreme outcomes, stress events, and shocks to the assumptions made about the portfolio and exposure behaviour.

(ii) A bank should also carefully assess concentrations in counterparty credit exposures, including counterparty credit risk exposures emanating from trading in less liquid markets, and determine the effect that these might have on a bank’s capital adequacy.

(iii) A bank should assess exposures, regardless of whether they are rated or unrated. If an exposure is unrated, it would be in order for a bank to derive notional external ratings of the unrated exposure by mapping their internal credit risk ratings / grades of the exposure used for pricing purposes with the external ratings scale. Thereafter, the bank should determine whether the risk weights applied to such exposures, under the standardised approach, are appropriate for its inherent risk. In those instances where a bank determines that the inherent risk of such an exposure, particularly if it

is unrated, is significantly higher than that implied by the risk weight to which it is assigned, a bank should consider the higher degree of credit risk in the evaluation of its overall capital adequacy.

(iv) For a more sophisticated bank, the credit review assessment of capital adequacy, at a minimum, should cover four areas: risk rating systems, portfolio analysis / aggregation, securitisation / complex credit derivatives, and large exposures and risk concentrations.

(2) Counterparty credit risk (CCR)

(i) A bank shall have counterparty credit risk management policies, processes and systems that are conceptually sound and implemented with integrity relative to the sophistication and complexity of a bank's holdings of exposures that give rise to CCR.

(ii) A sound counterparty credit risk management framework should include the identification, measurement, management, approval, and internal reporting of CCR.

(iii) A bank's risk management policies shall take into account the market, liquidity and operational risks that can be associated with CCR and, to the extent practicable, interrelationships among those risks. A bank should not undertake business with a counterparty without assessing its creditworthiness and shall take due account of both settlement and pre-settlement credit risk. These risks shall be managed as comprehensively as practicable at the counterparty level (aggregating counterparty exposures with other credit exposures) and at the enterprise-wide level.

(iv) The Board of Directors and senior management shall be actively involved in the CCR control process and shall regard this as an essential aspect of the business to which significant resources need to be devoted. The daily reports prepared on a firm's exposures to CCR shall be reviewed by a level of management with sufficient seniority and authority to enforce both reductions of positions taken by individual credit managers or traders and reductions in a bank's overall CCR exposure.

(v) A bank's CCR management system shall be used in conjunction with internal credit and trading limits.

(vi) The measurement of CCR shall include monitoring daily and intra-day usage of credit lines. A bank shall measure current exposure gross and net of collateral held where such measures are appropriate and meaningful (e.g., OTC derivatives, margin lending, etc.).

(vii) Measuring and monitoring peak exposure or potential future exposure (PFE), both the portfolio and counterparty levels is one element of a robust limit monitoring system. A bank shall take account of large or concentrated positions, including concentrations by groups of related counterparties, by industry, by market, customer investment strategies, etc.

(viii) A bank shall have an appropriate stress testing methodology in place to assess the impact on the counterparty credit risk of abnormal volatilities in market variables driving the counterparty exposures and changes in the creditworthiness of the counterparty. The results of this stress testing shall be reviewed periodically by senior management and shall be reflected in the CCR policies and limits set by management and the Board of Directors. Where stress tests reveal particular vulnerability to a given set of circumstances, management should explicitly consider appropriate risk management strategies (e.g., by hedging against that outcome, or reducing the size of the firm's exposures).

(ix) A bank shall have a routine in place for ensuring compliance with a documented set of internal policies, controls and procedures concerning the operation of the CCR management system. The firm's CCR management system should be well documented, for example, through a risk management manual that describes the basic principles of the risk management system and that provides an explanation of the empirical techniques used to measure CCR.

(x) A bank shall conduct an independent review of the CCR management system regularly through its own internal auditing process. This review shall include both the activities of the business credit and trading units and of the independent CCR control unit.

(xi) A review of the overall CCR management process shall take place at regular intervals (ideally not less than once a year) and shall specifically address, at a minimum:

(a) the adequacy of the documentation of the CCR management system and process;

(b) the organisation of the collateral management unit;

(c) the organisation of the CCR control unit;

(d) the integration of CCR measures into daily risk management;

(e) the approval process for risk pricing models and valuation systems used by front and back- office personnel;

(f) the validation of any significant change in the CCR measurement process;

(g) the scope of counterparty credit risks captured by the risk measurement model;

(h) the integrity of the management information system;

(i) the accuracy and completeness of CCR data;

(j) the accurate reflection of legal terms in collateral and netting agreements into exposure measurements;

(k) the verification of the consistency, timeliness and reliability of data sources used to run internal models, including the independence of such data sources;

(l) the accuracy and appropriateness of volatility and correlation assumptions;

(m) the accuracy of valuation and risk transformation calculations; and

(n) the verification of the model's accuracy through frequent back-testing.

(xii) A bank should make an assessment as part of its ICAAP as to whether its evaluation of the risks contained in the transactions that give rise to CCR and its assessment of whether the current exposure method (CEM), as per paragraph 85(2) captures those risks appropriately and satisfactorily.

(xiii) In cases where, under SREP, it is determined that CEM does not capture the risk inherent in a bank's relevant transactions (as could be the case with structured, more complex OTC derivatives), the Reserve Bank may require a bank to apply the CEM on a transaction-by-transaction basis (i.e., no netting will be recognised even if it is permissible legally).

(3) Market risk

(i) A bank should be able to identify risks in trading activities resulting from a movement in market prices. This determination should consider factors such as illiquidity of instruments, concentrated positions, one-way markets, non-linear / deep out-of-the money positions, and the potential for significant shifts in correlations.

(ii) Exercises that incorporate extreme events and shocks should also be tailored to capture key portfolio vulnerabilities to the relevant market developments.

(4) Operational risk

A bank should be able to assess the potential risks resulting from inadequate or failed internal processes, people, and systems, as well as from events external to the bank. This assessment should include the effects of extreme events and shocks relating to operational risk. Events could include a sudden increase in failed processes across business units or a significant incidence of failed internal controls.

(5) Interest rate risk in the banking book (IRRBB)

(i) A bank should identify the risks associated with the changing interest rates on its on-balance sheet and off-balance sheet exposures in the banking book from both, a short-term and long-term perspective. This may include the impact of changes due to parallel shocks, yield curve twists, yield curve inversions, changes in the relationships of rates (basis risk), and other relevant scenarios.

(ii) The bank should be able to support its assumptions about the behavioural characteristics of its non-maturity deposits and other assets and liabilities, especially those exposures characterised by embedded optionality.

(iii) Stress testing and scenario analysis should be used in the analysis of interest rate risks. While there could be several approaches to measurement of IRRBB, an illustrative approach for measurement of IRRBB is furnished at paragraph 237(5)(iv) below. A bank would, however, be free to adopt any other variant of these approaches or entirely different methodology for computing / quantifying the IRRBB provided the technique is based on objective, verifiable and transparent methodology and criteria.

(iv) Reference is also invited to the updated guidelines on IRRBB issued vide circular no. DOR.MRG.REC.102/00-00-009/2022-23 dated February 17, 2023 on 'Governance, measurement and management of Interest Rate Risk in Banking Book'. As mentioned in the circular *ibid*, the date for implementation will be communicated in due course. A bank is advised to be in preparedness for measuring, monitoring, and disclosing its exposure to interest rate risk in the banking book in terms of the circular *ibid*. Meanwhile, a bank shall submit the disclosures as advised in the circular *ibid*.

(v) An Illustrative Approach for Measurement of Interest Rate Risk in the Banking Book (IRRBB) under Pillar 2

(a) The Basel II framework- International Convergence of Capital Measurement and Capital Standards (June 2006) released by the Basel Committee on Banking Supervision- BCBS (paragraphs 739 and 762 to 764 - requires a bank to measure the IRRBB and hold capital commensurate with it. If supervisors determine that a bank is not holding capital commensurate with the level of interest rate risk, they shall require the bank to reduce its risk, to hold a specific additional amount of capital or some combination of the two. To comply with the requirements of Pillar 2 relating to IRRBB, the guidelines on Pillar 2 issued by many regulators contain definite provisions indicating the approach adopted by the supervisors to assess the level of interest rate risk in the banking book and the action to be taken in case the level of interest rate risk found is significant.

(b) In terms of paragraph 764 of the Basel II framework, a bank can follow the indicative methodology prescribed in the supporting document 'Principles for the Management and Supervision of Interest Rate Risk' issued by BCBS for assessment of sufficiency of capital for IRRBB.

(c) The main components of the approach prescribed in the BCBS paper on 'Principles for the Management and Supervision of Interest Rate Risk (July 2004)' are as under:

(i) The assessment shall take into account both the earnings perspective and economic value perspective of interest rate risk;

(ii) The impact on income or the economic value of equity shall be calculated by applying a notional interest rate shock of 200 basis points; and

(iii) The usual methods followed in measuring the interest rate risk are:

(a) Earnings perspective: Gap Analysis, simulation techniques and internal models based on VaR; and

(b) Economic perspective: Gap analysis combined with duration gap analysis, simulation techniques and internal models based on VaR.

(d) Methods for measurement of the IRRBB

(i) Impact on earnings: The major methods used for computing the impact on earnings are the gap analysis, simulations and VaR based techniques. If a bank in India has been using the gap reports to assess the impact of adverse movements in the interest rate on income through gap method, the bank may continue with the same. However, the bank may use the simulations also. The bank may calculate the impact on the earnings by gap analysis or any other method with the assumed change in yield on 200 bps over one year. However, no capital needs to be allocated for the impact on the earnings.

(ii) Impact of IRRBB on the Market Value of Equity (MVE): A bank may use the method indicated in the BCBS paper "Principles for the Management and Supervision of Interest rate Risk" (July 2004) for computing the impact of the interest rate shock on the MVE. The following steps are involved in this approach:

(a) The variables such as maturity / re-pricing date, coupon rate, frequency, principal amount for each item of asset / liability (for each category of asset / liability) are generated;

(b) The longs and shorts in each time band are offset;

(c) The resulting short and long positions are weighted by a factor that is designed to reflect the sensitivity of the positions in the different time bands to an assumed change in interest rates. These factors are based on an assumed parallel shift of 200 basis points throughout the time spectrum, and on a proxy of modified duration of positions situated at the middle of each time band and yielding 5 per cent;

(d) The resulting weighted positions are summed up, offsetting longs and shorts, leading to the net short or long weighted position;

(e) The weighted position is seen in relation to capital;

For details a bank may refer to the Annex III and IV of aforementioned paper issued by the BCBS.

(iii) Other techniques for Interest rate risk measurement: A bank can also follow different versions / variations of the above techniques or entirely different techniques to measure the IRRBB if it finds them conceptually sound. In this context, Annex I and II of the BCBS paper referred to above provide broad details of interest rate risk measurement techniques and overview of some of the factors which the supervisory authorities might consider in obtaining and analysing the information on individual bank’s exposures to interest rate risk.

(e) Suggested approach for measuring the impact of IRRBB on capital

(i) As per Basel II Framework, if the supervisor feels that a bank is not holding capital commensurate with the level of IRRBB, it may either require the bank to reduce the risk or allocate additional capital or a combination of the two.

(ii) A bank can decide, with the approval of the Board, on the appropriate level of interest rate risk in the banking book which it would like to carry keeping in view its capital level, interest rate management skills and the ability to re-balance the banking book portfolios quickly in case of adverse movement in the interest rates. In any case, a level of interest rate risk which generates a drop in the MVE of more than 20 per cent with an interest rate shock of 200 basis points, will be treated as excessive and such a bank would normally be required by the Reserve Bank to hold additional capital against IRRBB as determined during the SREP. A bank which has IRRBB exposure equivalent to less than 20 per cent drop in the MVE may also be required to hold additional capital if the level of interest rate risk is considered, by the Reserve Bank, to be high in relation to its capital level or the quality of interest rate risk management framework in the bank.

(iii) While a bank may on its own decide to hold additional capital towards IRRBB keeping in view the potential drop in its MVE, the IRR management skills and the ability to re-balance the portfolios quickly in case of adverse movement in the interest rates, the amount of exact capital add-on, if considered necessary, shall be decided by the Reserve Bank as part of the SREP, in consultation with the bank.

(f) Limit setting: A bank may consider setting the internal limits for controlling its IRRBB. The following are some of the indicative ways for setting the limits:

(i) Internal limits could be fixed in terms of the maximum decline in earnings (as a percentage of the base-scenario income) or

decline in capital (as a percentage of the base-scenario capital position) as a result of 200 or 300 basis point interest-rate shock;

(ii) The limits could also be placed in terms of PV01 value (present value of a basis point) of the net position of a bank as a percentage of net worth / capital of a bank.

(6) Credit concentration risk

(i) A risk concentration is any single exposure or a group of exposures with the potential to produce losses large enough (relative to a bank's capital, total assets, or overall risk level) to threaten a bank's health or ability to maintain its core operations. Concentration risk resulting from concentrated portfolios could be significant for most of the banks.

(ii) The following qualitative criteria could be adopted by a bank to demonstrate that the credit concentration risk is being adequately addressed:

(a) While assessing the exposure to concentration risk, a bank should keep in view that the calculations of Basel capital adequacy framework are based on the assumption that a bank is well diversified;

(b) While bank's single borrower exposures, the group borrower exposures and capital market exposures are regulated as per Reserve Bank of India (Commercial Banks – Concentration Risk Management) Directions, 2025, there could be concentrations in these portfolios as well. In assessing the degree of credit concentration, therefore, a bank shall consider not only the foregoing exposures but also consider the degree of credit concentration in a particular economic sector or geographical area. A bank with operational concentration in a few geographical regions, by virtue of the pattern of its branch network, should also consider the impact of adverse economic developments in that region, and their impact on the asset quality;

(c) The performance of specialised portfolios may, in some instances, also depend on key individuals / employees of the bank. Such a situation could exacerbate the concentration risk because the skills of those individuals, in part, limit the risk arising from a concentrated

portfolio. The impact of such key employees / individuals on the concentration risk is likely to be correspondingly greater in smaller banks. In developing its stress tests and scenario analyses, a bank shall, therefore, also consider the impact of losing key personnel on its ability to operate normally, as well as the direct impact on its revenues.

(iii) As regards the quantitative criteria to be used to ensure that credit concentration risk is being adequately addressed:

(a) the credit concentration risk calculations shall be performed at the counterparty level (i.e., large exposures), at the portfolio level (i.e., sectoral and geographical concentrations) and at the asset class level (i.e., liability and assets concentrations). In this regard, a reference is invited to Reserve Bank of India (Commercial Banks – Concentration Risk Management) Directions, 2025.

(b) A bank may like to ensure that its aggregate exposure (including non-funded exposures) to all 'large borrowers' does not exceed at any time, 800 per cent of its 'capital funds' (as defined for the purpose of extant exposure norms of the Reserve Bank). The 'large borrower' for this purpose could be taken to mean as one to whom the bank's aggregate exposure (funded as well as non-funded) exceeds 10 per cent of the bank's capital funds.

(c) A bank may also pay special attention to its industry-wise exposures where its exposure to a particular industry exceeds 10 per cent of its aggregate credit exposure (including investment exposure) to the industrial sector as a whole.

(d) There could be several approaches to the measurement of credit concentration of a bank's portfolio. For instance, Herfindahl-Hirshman Index (HHI) could be one of possible methods for measuring concentration risk. However, a bank is free to adopt any other appropriate method for the purpose, which has objective and transparent criteria for such measurement.

(iv) Risk concentrations should be analysed on both solo and consolidated basis.

(v) Risk concentrations should be viewed in the context of a single or a set of closely related risk-drivers that may have different impacts on a bank. These concentrations should be integrated when assessing a bank's overall risk exposure.

(vi) A bank should consider concentrations that are based on common or correlated risk factors that reflect more subtle or more situation-specific factors than traditional concentrations, such as correlations between market, credit risks, and liquidity risk.

(vii) Through its risk management processes and MIS, a bank should be able to identify and aggregate similar risk exposures across the firm, including across legal entities, asset types (e.g., loans, derivatives and structured products), risk areas (e.g., the trading book) and geographic regions. In addition to the situations described in paragraph 237(6)(iii) above, risk concentrations can arise include:

(a) exposures to a single counterparty, or group of connected counterparties;

(b) exposures to both regulated and non-regulated financial institutions such as hedge funds and private equity firms;

(c) trading exposures / market risk;

(d) exposures to counterparties (e.g., hedge funds and hedge counterparties) through the execution or processing of transactions (either product or service);

(e) funding sources;

(f) assets that are held in banking book or trading book, such as loans, derivatives and structured products; and

(g) off-balance sheet exposures, including guarantees, liquidity lines and other commitments.

(viii) Risk concentrations can also arise through a combination of exposures across these broad categories.

(ix) A bank should have an understanding of its firm-wide risk concentrations resulting from similar exposures across its different business lines. Examples of such business lines include subprime exposure in lending books; counterparty exposures; conduit exposures and SIVs; contractual and non-contractual exposures; trading activities; and underwriting pipelines.

(x) While risk concentrations often arise due to direct exposures to borrowers and obligors, a bank may also incur a concentration to a particular asset type indirectly through investments backed by such assets (e.g., collateralised debt obligations – CDOs), as well as exposure to protection providers guaranteeing the performance of the specific asset type (e.g., monoline insurers). A bank should have in place adequate, systematic procedures for identifying high correlation between the creditworthiness of a protection provider and the obligors of the underlying exposures due to their performance being dependent on common factors beyond systematic risk (i.e., 'wrong way risk').

(xi) Procedures should be in place to communicate risk concentrations to the board of directors and senior management in a manner that clearly indicates where in the organisation each segment of a risk concentration resides.

(xii) A bank should have credible risk mitigation strategies in place that have senior management approval. This may include altering business strategies, reducing limits or increasing capital buffers in line with the desired risk profile. While it implements risk mitigation strategies, the bank should be aware of possible concentrations that might arise as a result of employing risk mitigation techniques.

(xiii) A bank should employ several techniques, as appropriate, to measure risk concentrations. These techniques include shocks to various risk factors; use of business level and firm-wide scenarios; and the use of integrated stress testing and economic capital models.

(xiv) Identified concentrations should be measured in a number of ways, including for example consideration of gross versus net exposures, use of notional amounts, and analysis of exposures with and without counterparty hedges.

(xv) A bank should establish internal position limits for concentrations to which it may be exposed. When conducting periodic stress tests, a bank should incorporate all major risk concentrations and identify and respond to potential changes in market conditions that could adversely impact its performance and capital adequacy.

(xvi) The assessment of such risks under a bank's ICAAP and the supervisory review process should not be a mechanical process, but one in which each bank determines, depending on its business model, its own specific vulnerabilities. An appropriate level of capital for risk concentrations should be incorporated in a bank's ICAAP, as well as in Pillar 2 assessments. Each bank should discuss such issues with its supervisor.

(xvii) A bank should have in place effective internal policies, systems, and controls to identify, measure, monitor, manage, control and mitigate its risk concentrations in a timely manner. Not only should normal market conditions be considered, but also the potential build-up of concentrations under stressed market conditions, economic downturns and periods of general market illiquidity.

(xviii) A bank should assess scenarios that consider possible concentrations arising from contractual and non-contractual contingent claims. The scenarios should also combine the potential build-up of pipeline exposures together with the loss of market liquidity and a significant decline in asset values.

(7) Liquidity risk

(i) A bank should understand the risks resulting from its inability to meet its obligations as they come due, because of difficulty in liquidating assets (market liquidity risk) or in obtaining adequate funding (funding liquidity risk).

(ii) An assessment of liquidity risk should include analysis of sources and uses of funds, an understanding of the funding markets in which the bank operates, and an assessment of the efficacy of a contingency funding plan for events that could arise.

(iii) Senior management should consider the relationship between liquidity and capital since liquidity risk can impact capital adequacy which, in turn, can aggravate a bank's liquidity profile.

(iv) A bank should maintain a liquidity cushion, made up of unencumbered, high quality liquid assets, to protect against liquidity stress events, including potential losses of unsecured and typically available secured funding sources.

(v) A bank should have strong governance of liquidity risk, including the setting of a liquidity risk tolerance by the board. The risk tolerance should be communicated throughout the bank and reflected in the strategy and policies that senior management set to manage liquidity risk.

(vi) A bank should appropriately price the costs, benefits, and risks of liquidity into the internal pricing, performance measurement, and new product approval process of all significant business activities.

(vii) A bank should be able to thoroughly identify, measure and control liquidity risks, especially with regard to complex products and contingent commitments (both contractual and non-contractual). This process should involve the ability to project cash flows arising from assets, liabilities, and off-balance sheet items over various time horizons, and should ensure diversification in both the tenor and source of funding.

(viii) A bank should utilise early warning indicators to identify the emergence of increased risk or vulnerabilities in its liquidity position or funding needs. It should have the ability to control liquidity risk exposure and funding needs, regardless of its organisation structure, within and across legal entities, business lines, and currencies, taking into account any legal, regulatory and operational limitations to the transferability of liquidity.

(ix) A bank's management of intraday liquidity risks should be considered as a crucial part of liquidity risk management.

(x) It should also actively manage its collateral positions and have the ability to calculate all of its collateral positions.

(xi) A bank should perform stress tests or scenario analyses on a regular basis in order to identify and quantify its exposures to possible future liquidity stresses, analysing possible impacts on the institutions' cash flows, liquidity positions, profitability, and solvency. The results of these stress tests should be discussed thoroughly by management, and based on this discussion, should form the basis for taking remedial or mitigating actions to limit the bank's exposures, build up a liquidity cushion, and adjust its liquidity profile to fit its risk tolerance. The results of stress tests should also play a key role in shaping the bank's contingency funding planning, which should outline policies for managing a range of stress events and clearly set out strategies for addressing liquidity shortfalls in emergency situations.

(xii) It is important that a bank publicly disclose information on a regular basis that enables market participants to make informed decisions about the soundness of its liquidity risk management framework and liquidity position.

(8) Off-balance sheet exposures and securitisation risk

(i) A bank's on and off-balance sheet securitisation activities should be included in its risk management disciplines, such as product approval, risk concentration limits, and estimates of market, credit, and operational risk.

(ii) All risks arising from securitisation, particularly those that are not fully captured under Pillar 1, should be addressed in a bank's ICAAP. These risks include:

(a) Credit, market, liquidity and reputational risk of each exposure;

(b) Potential delinquencies and losses on the underlying securitised exposures;

(c) Exposures from credit lines or liquidity facilities to special purpose entities;

(d) Exposures from guarantees provided by monolines and other third parties.

(iii) Securitisation exposures should be included in a bank's MIS to help ensure that senior management understands the implications of such exposures for liquidity, earnings, risk concentration and capital. More specifically, a bank should have the necessary processes in place to capture in a timely manner, updated information on securitisation transactions including market data, if available, and updated performance data from the securitisation trustee or servicer.

(9) Provision of implicit support for securitisation transactions

(i) Contractual support can include over collateralisation, credit derivatives, spread accounts, contractual recourse obligations, subordinated notes, credit risk mitigants provided to a specific tranche, the subordination of fee or interest income or the deferral of margin income, and clean-up calls that exceed 10 percent of the initial issuance. Examples of implicit support include the purchase of deteriorating credit risk exposures from the underlying pool, the sale of discounted credit risk exposures into the pool of securitised credit risk exposures, the purchase of underlying exposures at above market price or an increase in the first loss position according to the deterioration of the underlying exposures.

(ii) For traditional securitisation structures the provision of implicit support undermines the clean break criteria, which when satisfied would allow the bank to exclude the securitised assets from regulatory capital calculations. For synthetic securitisation structures, it negates the significance of risk transference. By providing implicit support, a bank signals to the market that the risk is still with the bank and has not in effect been transferred and hence its capital calculation therefore understates the true risk. Accordingly, supervisors may take appropriate action when a banking organisation provides implicit support.

(iii) When a bank has been found to provide implicit support to a securitisation, it will be required to hold capital against all of the underlying exposures associated with the structure as if they had not been securitised. It will also be required to disclose publicly that it was found to have provided non-contractual support, as well as the resulting increase in the capital charge

(as noted above). The aim is to require a bank to hold capital against exposures for which it assumes the credit risk, and to discourage it from providing non-contractual support.

(iv) If a bank is found to have provided implicit support on more than one occasion, the bank is required to disclose its transgression publicly and the Reserve Bank will take appropriate action that may include, but is not limited to, one or more of the following:

(a) The bank may be prevented from gaining favourable capital treatment on securitised assets for a period of time to be determined by the Reserve Bank;

(b) The bank may be required to hold capital against all securitised assets as though the bank had created a commitment to them, by applying a conversion factor to the risk weight of the underlying assets;

(c) For purposes of capital calculations, the bank may be required to treat all securitised assets as if they remained on the balance sheet; and

(d) A bank may be required by the Reserve Bank to hold regulatory capital in excess of the minimum risk-based capital ratios.

(v) During the SREP, Reserve Bank will determine implicit support and may take appropriate supervisory action to mitigate the effects. Pending any investigation, the bank may be prohibited from any capital relief for planned securitisation transactions (moratorium). The action of Reserve Bank will be aimed at changing the bank’s behaviour with regard to the provision of implicit support, and to correct market perception as to the willingness of the bank to provide future recourse beyond contractual obligations.

(10) Reputational risk on account of implicit support

(i) Reputational risk can be defined as the risk arising from negative perception on the part of customers, counterparties, shareholders, investors, debt holders, market analysts, other relevant parties or regulators that can adversely affect a bank's ability to maintain existing, or establish new, business relationships and continued access to sources of funding (e.g., through the interbank or securitisation markets).

(ii) Reputational risk can lead to the provision of implicit support, which may give rise to credit, liquidity, market, and legal risk - all of which can have a negative impact on a bank's earnings, liquidity, and capital position. A bank should identify potential sources of reputational risk to which it is exposed. These include the bank's business lines, liabilities, affiliated operations, off-balance sheet vehicles and the markets in which it operates. The risks that arise should be incorporated into the bank's risk management processes and appropriately addressed in its ICAAP and liquidity contingency plans.

(iii) A bank should incorporate the exposures that could give rise to reputational risk into its assessments of whether the requirements under the securitisation framework have been met and the potential adverse impact of providing implicit support.

(iv) Reputational risk may arise, for example, from a bank's sponsorship of securitisation structures such as Asset Backed Commercial Paper (ABCP) conduits and Structured Investment Vehicles (SIVs), as well as from the sale of credit exposures to securitisation trusts. It may also arise from a bank's involvement in asset or funds management, particularly when financial instruments are issued by owned or sponsored entities and are distributed to the customers of the sponsoring bank. In the event that the instruments were not correctly priced or the main risk drivers not adequately disclosed, a sponsor may feel some responsibility to its customers, or be economically compelled, to cover any losses. Reputational risk also arises when a bank sponsors activities such as money market mutual funds, in-house hedge funds and real estate investment trusts. In these cases, a bank may decide to support the value of shares / units held by investors even though is not contractually required to provide the support.

(v) Reputational risk may also affect a bank's liabilities, since market confidence and a bank's ability to fund its business are closely related to its reputation. For instance, to avoid damaging its reputation, a bank may call its liabilities even though this might negatively affect its liquidity profile. This is particularly true for liabilities that are components of regulatory capital, such as hybrid / subordinated debt. In such cases, a bank's capital position is likely to suffer.

(vi) A bank’s management should have appropriate policies in place to identify sources of reputational risk when entering new markets, products or lines of activities.

(vii) A bank's stress testing procedures should take account of reputational risk so management has a firm understanding of the consequences and second round effects of reputational risk.

(viii) Once a bank identifies potential exposures arising from reputational concerns, it should measure the amount of support it might have to provide (including implicit support of securitisations) or losses it might experience under adverse market conditions.

(ix) A bank should develop methodologies to measure as precisely as possible the effect of reputational risk in terms of other risk types (e.g., credit, liquidity, market, or operational risk) to which it may be exposed to avoid reputational damages and to maintain market confidence. This could be accomplished by including reputational risk scenarios in regular stress tests. For instance, non-contractual off-balance sheet exposures could be included in the stress tests to determine the effect on a bank's credit, market, and liquidity risk profiles. Methodologies also could include comparing the actual amount of exposure carried on the balance sheet versus the maximum exposure amount held off-balance sheet, that is, the potential amount to which the bank could be exposed.

(x) A bank should pay particular attention to the effects of reputational risk on its overall liquidity position, taking into account both possible increases in the asset side of the balance sheet and possible restrictions on funding, should the loss of reputation result in various counterparties' loss of confidence.

(xi) In contrast to contractual credit exposures, such as guarantees, implicit support is a more subtle form of exposure. Implicit support arises when a bank provides post-sale support to a securitisation transaction in excess of any contractual obligation. Implicit support may include any letter of comfort provided by the originator in respect of the present or future liabilities of the SPV. Such non-contractual support exposes a bank to the risk of loss, such

as loss arising from deterioration in the credit quality of the securitisation's underlying assets.

(xii) By providing implicit support, a bank signals to the market that all of the risks inherent in the securitised assets are still held by the organisation and, in effect, had not been transferred. Since the risk arising from the potential provision of implicit support is not captured ex ante under Pillar 1, it shall be considered as part of the Pillar 2 process. In addition, the processes for approving new products or strategic initiatives should consider the potential provision of implicit support and should be incorporated in a bank's ICAAP.

(11) Risk evaluation and management

(i) A bank should conduct analyses of the underlying risks when investing in the structured products (permitted by Reserve Bank) and shall not solely rely on the external credit ratings assigned to securitisation exposures by the credit rating agencies. A bank should be aware that external ratings are a useful starting point for credit analysis but are no substitute for full and proper understanding of the underlying risk, especially where ratings for certain asset classes have a short history or have been shown to be volatile.

(ii) A bank also should conduct credit analysis of the securitisation exposure at acquisition and on an ongoing basis. It should also have in place the necessary quantitative tools, valuation models and stress tests of sufficient sophistication to reliably assess all relevant risks.

(iii) When assessing securitisation exposures, a bank should ensure that it fully understands the credit quality and risk characteristics of the underlying exposures in structured credit transactions, including any risk concentrations. In addition, a bank should review the maturity of the exposures underlying structured credit transactions relative to the issued liabilities in order to assess potential maturity mismatches.

(iv) A bank should track credit risk in securitisation exposures at the transaction level and across securitisations exposures within each business line and across business lines. It should produce reliable measures of aggregate risk.

(v) A bank also should track all meaningful concentrations in securitisation exposures, such as name, product, or sector concentrations, and feed this information to firm-wide risk aggregation systems that track, for example, credit exposure to a particular obligor.

(vi) A bank's own assessment of risk needs to be based on a comprehensive understanding of the structure of the securitisation transaction. It should identify the various types of triggers, credit events and other legal provisions that may affect the performance of its on- and off-balance sheet exposures and integrate these triggers and provisions into its funding / liquidity, credit, and balance sheet management. The impact of the events or triggers on a bank's liquidity and capital position should also be considered.

(vii) As part of its risk management processes, a bank should consider, where appropriate, mark-to-market warehoused positions, as well as those in the pipeline, regardless of the probability of securitising the exposures.

(viii) A bank should consider scenarios which may prevent it from securitising its assets as part of its stress testing and identify the potential effect of such exposures on its liquidity, earnings, and capital adequacy.

(ix) A bank should develop prudent contingency plans specifying how it would respond to funding, capital and other pressures that arise when access to securitisation markets is reduced. The contingency plans should also address how the bank would address valuation challenges for potentially illiquid positions held for sale or for trading.

(x) The risk measures, stress testing results and contingency plans should be incorporated into the bank's risk management processes and its ICAAP and should result in an appropriate level of capital under Pillar 2 in excess of the minimum requirements.

(xi) A bank that employs risk mitigation techniques should fully understand the risks to be mitigated, the potential effects of that mitigation and whether or not the mitigation is fully effective. This is to help ensure that the bank does not understate the true risk in its assessment of capital. In particular, it should consider whether it would provide support to the securitisation

structures in stressed scenarios due to the reliance on securitisation as a funding tool.

(12) Valuation practices

(i) The characteristics of complex structured products, including securitisation transactions, make their valuation inherently difficult due, in part, to the absence of active and liquid markets, the complexity and uniqueness of the cash waterfalls, and the links between valuations and underlying risk factors. The absence of a transparent price from a liquid market means that the valuation should rely on models or proxy-pricing methodologies, as well as on expert judgment. The outputs of such models and processes are highly sensitive to the inputs and parameter assumptions adopted, which may themselves be subject to estimation error and uncertainty. Moreover, calibration of the valuation methodologies is often complicated by the lack of readily available benchmarks. Therefore, a bank is expected to have adequate governance structures and control processes for fair valuing exposures for risk management and financial reporting purposes.

(ii) The valuation governance structures and related processes should be embedded in the overall governance structure of the bank, and consistent for both risk management and reporting purposes. The governance structures and processes should explicitly cover the role of the Board and senior management. In addition, the Board should receive reports from senior management on the valuation oversight and valuation model performance issues that are brought to senior management for resolution, as well as all significant changes to valuation policies.

(iii) A bank should have clear and robust governance structures for the production, assignment and verification of financial instrument valuations. Policies should ensure that the approvals of all valuation methodologies are well documented. In addition, policies and procedures should set forth the range of acceptable practices for the initial pricing, marking-to-market / model, valuation adjustments and periodic independent revaluation. New product approval processes should include all internal stakeholders

relevant to risk measurement, risk control, and the assignment and verification of valuations of financial instruments.

(iv) A bank's control processes for measuring and reporting valuations should be consistently applied across the firm and integrated with risk measurement and management processes. In particular, valuation controls should be applied consistently across similar instruments (risks) and consistent across business lines (books). These controls should be subject to internal audit. Regardless of the booking location of a new product, reviews and approval of valuation methodologies shall be guided by a minimum set of considerations. Furthermore, the valuation / new product approval process should be supported by a transparent, well-documented inventory of acceptable valuation methodologies that are specific to products and businesses.

(v) To establish and verify valuations for instruments and transactions in which it engages, a bank should have adequate capacity, including during periods of stress. This capacity should be commensurate with the importance, riskiness and size of these exposures in the context of the business profile of the institution.

(vi) For exposures representing material risk, a bank is expected to have the capacity to produce valuations using alternative methods in the event that primary inputs and approaches become unreliable, unavailable or not relevant due to market discontinuities or illiquidity. A bank shall test and review the performance of its models under stress conditions so that it understands the limitations of the models under stress conditions.

(vii) The relevance and reliability of valuations is directly related to the quality and reliability of the inputs. A bank is expected to apply the accounting guidance provided to determine the relevant market information and other factors likely to have a material effect on an instrument's fair value when selecting the appropriate inputs to use in the valuation process. Where values are determined to be in an active market, a bank should maximise the use of relevant observable inputs and minimise the use of unobservable inputs when estimating fair value using a valuation technique. However,

where a market is deemed inactive, observable inputs or transactions may not be relevant, such as in a forced liquidation or distress sale, or transactions may not be observable, such as when markets are inactive. In such cases, accounting fair value guidance provides assistance on what should be considered, but may not be determinative. In assessing whether a source is reliable and relevant, a bank should consider, among other things:

(a) the frequency and availability of the prices / quotes;

(b) whether those prices represent actual regularly occurring transactions on an arm's length basis;

(c) the breadth of the distribution of the data and whether it is generally available to the relevant participants in the market;

(d) the timeliness of the information relative to the frequency of valuations;

(e) the number of independent sources that produce the quotes / prices;

(f) whether the quotes / prices are supported by actual transactions;

(g) the maturity of the market; and

(h) the similarity between the financial instrument sold in a transaction and the instrument held by the institution.

(viii) A bank’s external reporting should provide timely, relevant, reliable and decision useful information that promotes transparency. Senior management should consider whether disclosures around valuation uncertainty can be made more meaningful. For instance, the bank may describe the modelling techniques and the instruments to which they are applied; the sensitivity of fair values to modelling inputs and assumptions; and the impact of stress scenarios on valuations. A bank should regularly review its disclosure policies to ensure that the information disclosed continues to be relevant to its business model and products and to current market conditions.

(13) Sound stress testing practices

(i) Stress testing plays a particularly important role in:

(a) providing forward looking assessments of risk;

(b) overcoming limitations of models and historical data;

(c) supporting internal and external communication;

(d) feeding into capital and liquidity planning procedures;

(e) informing the setting of a bank's risk tolerance;

(f) addressing existing or potential, firm-wide risk concentrations; and

(g) facilitating the development of risk mitigation or contingency plans across a range of stressed conditions.

(ii) Stress testing should form an integral part of the overall governance and risk management culture of the bank. Board and senior management involvement in setting stress testing objectives, defining scenarios, discussing the results of stress tests, assessing potential actions and decision making is critical in ensuring appropriate use of stress testing in a bank's risk governance and capital planning. Senior management should take an active interest in the development in, and operation of, stress testing. The results of stress tests should contribute to strategic decision making and foster internal debate regarding assumptions, such as the cost, risk and speed with which new capital could be raised or that positions could be hedged or sold.

(iii) A bank's capital planning process should incorporate rigorous, forward looking stress testing that identifies possible events or changes in market conditions that could adversely impact the bank.

(iv) A bank, under its ICAAP, should examine future capital resources and capital requirements under adverse scenarios. In particular, the results of forward-looking stress testing should be considered when evaluating the adequacy of a bank's capital buffer. Capital adequacy should be assessed under stressed conditions against a variety of capital ratios, including regulatory ratios, as well as ratios based on the bank's internal definition of capital resources. In addition, the possibility that a crisis impairs the ability

of even a very healthy bank to raise funds at reasonable cost should be considered.

(v) A bank should develop methodologies to measure the effect of reputational risk in terms of other risk types, namely credit, liquidity, market, and other risks that it may be exposed to in order to avoid reputational damages and in order to maintain market confidence. This could be done by including reputational risk scenarios in regular stress tests. For instance, including non-contractual off-balance sheet exposures in the stress tests to determine the effect on a bank's credit, market, and liquidity risk profiles.

(vi) A bank should carefully assess the risks with respect to commitments to off-balance sheet vehicles and third-party firms related to structured credit securities and the possibility that assets will need to be taken on balance sheet for reputational reasons. Therefore, in its stress testing programme, a bank should include scenarios assessing the size and soundness of such vehicles and firms relative to its own financial, liquidity, and regulatory capital positions. This analysis should include structural, solvency, liquidity, and other risk issues, including the effects of covenants and triggers.

(vii) A bank shall also refer to Annex IV for further instructions on Stress Testing.

(14) Compensation practices

(i) Risk management shall be embedded in the culture of a bank. It should be a critical focus of the CEO / Managing Director, CRO, senior management, trading desk and other business line heads and employees in making strategic and day-to-day decisions.

(ii) For a broad and deep risk management culture to develop and be maintained over time, compensation policies shall not be unduly linked to short-term accounting profit generation. Compensation policies should be linked to longer-term capital preservation and the financial strength of a bank and should consider risk-adjusted performance measures.

(iii) A bank should provide adequate disclosure regarding its compensation policies to stakeholders.

(iv) Each bank's board of directors and senior management have the responsibility to mitigate the risks arising from remuneration policies in order to ensure effective firm-wide risk management.

(v) A bank's board of directors shall actively oversee the compensation system's design and operation, which should not be controlled primarily by the CEO and management team. Relevant board members and employees shall have independence and expertise in risk management and compensation. In addition, the Board of Directors shall monitor and review the compensation system to ensure the system includes adequate controls and operates as intended. The practical operation of the system should be regularly reviewed to ensure compliance with policies and procedures. Compensation outcomes, risk measurements, and risk outcomes should be regularly reviewed for consistency with intentions.

(vi) Staff that are engaged in the financial and risk control areas shall be independent, have appropriate authority, and be compensated in a manner that is independent of the business areas they oversee and commensurate with their key role in the firm. Effective independence and appropriate authority of such staff is necessary to preserve the integrity of financial and risk management's influence on incentive compensation.

(vii) Compensation shall be adjusted for all types of risk so that remuneration is balanced between the profit earned and the degree of risk assumed in generating the profit. In general, both quantitative measures and human judgment should play a role in determining the appropriate risk adjustments, including those that are difficult to measure such as liquidity risk and reputation risk.

(viii) Compensation outcomes shall be symmetric with risk outcomes and compensation systems should link the size of the bonus pool to the overall performance of a firm. Employees' incentive payments should be linked to the contribution of the individual and business to a firm's overall performance.

(ix) Compensation payout schedules shall be sensitive to the time horizon of risks. Profits and losses of different activities of a financial firm are realised

over different periods of time. Variable compensation payments should be deferred accordingly. Payments should not be finalised over short periods where risks are realised over long periods. Management should question payouts for income that cannot be realised or whose likelihood of realisation remains uncertain at the time of payout.

(x) The mix of cash, equity, and other forms of compensation shall be consistent with risk alignment. The mix will vary depending on the employee's position and role. A bank should be able to explain the rationale for its mix.

(xi) Reserve Bank will review compensation practices in a rigorous and sustained manner and deficiencies, if any, will be addressed promptly with the appropriate supervisory action.

(xii) The risk factors discussed above should not be considered an exhaustive list of those affecting any given bank. All relevant factors that present a material source of risk to capital should be incorporated in a well-developed ICAAP. Furthermore, a bank should be mindful of the capital adequacy effects of concentrations that may arise within each risk type.

(15) Quantitative and qualitative approaches in ICAAP

(i) All measurements of risk incorporate both quantitative and qualitative elements, but to the extent possible, a quantitative approach should form the foundation of a bank's measurement framework. In some cases, quantitative tools can include the use of large historical databases; when data are scarcer, a bank may choose to rely more heavily on the use of stress testing and scenario analyses. A bank should understand when measuring risks that measurement error always exists, and in many cases the error is itself difficult to quantify. In general, an increase in uncertainty related to modeling and business complexity should result in a larger capital cushion.

(ii) Quantitative approaches that focus on most likely outcomes for budgeting, forecasting, or performance measurement purposes may not be fully applicable for capital adequacy because the ICAAP should also take less likely events into account. Stress testing and scenario analysis can be

effective in gauging the consequences of outcomes that are unlikely but would have a considerable impact on safety and soundness.

(iii) To the extent that risks cannot be reliably measured with quantitative tools – for example, where measurements of risk are based on scarce data or unproven quantitative methods – qualitative tools, including experience and judgment, may be more heavily utilised. A bank should be cognisant that qualitative approaches have their own inherent biases and assumptions that affect risk assessment; and accordingly, a bank should recognise these limitations of the qualitative approaches used.

(16) Risk aggregation and diversification effects

(i) An effective ICAAP should assess the risks across the entire bank. A bank choosing to conduct risk aggregation among various risk types or business lines should understand the challenges in such aggregation.

(ii) When aggregating risks, a bank should ensure that any potential concentrations across more than one risk dimension are addressed, recognising that losses could arise in several risk dimensions at the same time, stemming from the same event or a common set of factors. For example, a localised natural disaster could generate losses from credit, market, and operational risks at the same time.

(iii) In considering the possible effects of diversification, management should be systematic and rigorous in documenting decisions, and in identifying assumptions used in each level of risk aggregation. Assumptions about diversification should be supported by analysis and evidence. The bank should have systems capable of aggregating risks based on the bank's selected framework. For example, a bank calculating correlations within or among risk types should consider data quality and consistency, and the volatility of correlations over time and under stressed market conditions.

D Format of an internal capital adequacy assessment process (ICAAP) document

238. An illustrative outline of a format of the ICAAP document is furnished below:

(1) What is an ICAAP document?

(i) The ICAAP Document shall be a comprehensive paper furnishing detailed information on the ongoing assessment of a bank's entire spectrum of risks, how the bank intends to mitigate those risks and how much current and future capital is necessary for the bank, reckoning other mitigating factors. The purpose of the ICAAP document is to apprise the Board of a bank on these aspects as also to explain to the Reserve Bank the bank's internal capital adequacy assessment process and the bank's approach to capital management. The ICAAP can also be based on the existing internal documentation of a bank.

(ii) The ICAAP document submitted to the Reserve Bank shall be formally approved by a bank's Board. It is expected that the document shall be prepared in a format that shall be easily understood at the senior levels of management and shall contain all the relevant information necessary for a bank and the Reserve Bank to make an informed judgment as to the appropriate capital level of the bank and its risk management approach. Where appropriate, technical information on risk measurement methodologies, capital models, if any, used and all other work carried out to validate the approach (e.g., board papers and minutes, internal or external reviews) can be furnished to the Reserve Bank as appendices to the ICAAP Document.

(2) The ICAAP Document shall contain the following sections:

(i) Executive summary;

(ii) Background;

(iii) Summary of current and projected financial and capital positions;

(iv) Capital adequacy;

(v) Key sensitivities and future scenarios;

(vi) Aggregation and diversification;

(vii) Testing and adoption of the ICAAP; and

(viii) Use of the ICAAP within a bank.

(3) A detailed description of the above sections is as under:

(i) Executive Summary: The purpose of the executive summary is to present an overview of the ICAAP methodology and results. This overview shall typically include:

(a) the purpose of the report and the regulated entities within a banking group that are covered by the ICAAP;

(b) the main findings of the ICAAP analysis:

(i) how much and what composition of internal capital a bank considers it should hold as compared with the minimum CRAR requirement under Pillar 1 calculation; and

(ii) the adequacy of a bank's risk management processes;

(c) a summary of the financial position of a bank, including the strategic position of the bank, its balance sheet strength, and future profitability;

(d) brief descriptions of the capital raising and dividend distribution plan including how a bank intends to manage its capital in the days ahead and for what purposes;

(e) commentary on the most material risks to which a bank is exposed, why the level of risk is considered acceptable or, if it is not, what mitigating actions are planned;

(f) commentary on major issues where further analysis and decisions are required; and

(g) who has carried out the assessment, how it has been challenged / validated stress tested, and who has approved it.

(ii) Background: This section shall cover the relevant organisational and historical financial data for a bank. e.g., group structure (legal and operational), operating profit, profit before tax, profit after tax, dividends, shareholders' funds, capital funds held vis-à-vis the regulatory requirements, customer deposits, deposits by banks, total assets, and any conclusions that can be drawn from trends in the data which may have implications for a bank's future.

(iii) Summary of current and projected financial and capital positions

(a) This section shall explain the present financial position of a bank and expected changes to the current business profile, the environment in which it expects to operate, its projected business plans (by appropriate lines of business), projected financial position, and future planned sources of capital.

(b) The starting balance sheet used as reference and date as of which the assessment is carried out shall be indicated.

(c) The projected financial position can reckon both the projected capital available and projected capital requirements based on envisaged business plans. These might then provide a basis against which adverse scenarios might be compared.

(iv) Capital adequacy

(a) This section may start with a description of a bank's risk appetite, in quantitative terms, as approved by a bank's Board and used in the ICAAP. It shall be necessary to clearly spell out in the document whether what is being presented represents the bank's view of the amount of capital required to meet minimum regulatory needs or whether represents the amount of capital that a bank believes it shall need to meet its business plans. For instance, it shall be clearly brought out whether the capital required is based on a particular credit rating desired by a bank or includes buffers for strategic purposes or seeks to minimise the chance of breaching regulatory requirements. Where economic capital models are used for internal capital assessment, the confidence level, time horizon, and description of the event to which the confidence level relates, shall also be enumerated. Where scenario analyses or other means are used for capital assessment, then the basis / rationale for selecting the chosen severity of scenarios used, shall also be included.

(b) The section shall also include a detailed review of the capital adequacy of a bank. The information provided shall include the following elements:

(i) Timing

(a) the effective date of the ICAAP calculations together with details of any events between this date and the date of submission to the Board / the Reserve Bank which shall materially impact the ICAAP calculations together with their effects; and

(b) details of, and rationale for, the time period selected for which capital requirement has been assessed.

(ii) Risks analysed:

(a) an identification of the major risks faced by a bank in each of the following categories:

(i) credit risk;

(ii) market risk;

(iii) operational risk;

(iv) liquidity risk;

(v) concentration risk;

(vi) interest rate risk in the banking book;

(vii) residual risk of securitization;

(viii) strategic risk;

(ix) business risk;

(x) reputation risk;

(xi) group risk;

(xii) pension obligation risk;

(xiii) other residual risk; and

(xiv) any other risks that might have been identified.

for each of these risks, an explanation of how the risk has been assessed and to the extent possible, the quantitative results of that assessment;

(b) where some of these risks have been highlighted in the report of the Reserve Bank's on-site inspection of a bank, an explanation of how the bank has mitigated these risks;

(c) where relevant, a comparison of the Reserve Bank assessed CRAR during on-site inspection with the results of the CRAR calculations of a bank under the ICAAP;

(d) a clear articulation of a bank's risk appetite, in quantitative terms, by risk category and the extent of its consistency (its 'fit') with the overall assessment of the bank's various risks; and

(e) where relevant, an explanation of any other methods, apart from capital, used by a bank to mitigate the risks.

(iii) Methodology and assumptions

(a) A description of how assessments for each of the major risks have been approached and the main assumptions made.

(b) For instance, a bank may choose to base its ICAAP on the results of the CRAR calculation with the capital for additional risks (e.g., concentration risk, interest rate risk in the banking book, etc.) assessed separately and added to the Pillar 1 computations. Alternatively, a bank may choose to base its ICAAP on internal models for all risks, including those covered under the CRAR (i.e., credit, market, and operational risks).

(c) The description here shall make clear which risks are covered by which modelling or calculation approach. This shall include details of the methodology and process used to calculate risks in each of the categories identified and reason for choosing the method used in each case.

(d) Where a bank uses an internal model for the quantification of its risks, this section shall explain for each of those models:

(i) the key assumptions and parameters within the capital modelling work and background information on the derivation of any key assumptions;

(ii) how parameters have been chosen, including the historical period used and the calibration process;

(iii) the limitations of the model;

(iv) the sensitivity of the model to changes in those key assumptions or parameters chosen; and

(v) the validation work undertaken to ensure the continuing adequacy of the model.

(e) Where stress tests or scenario analyses have been used to validate, supplement, or probe the results of other modelling approaches, then this section shall provide:

(i) details of simulations to capture risks not well estimated by a bank's internal capital model (e.g., non-linear products, concentrations, illiquidity and shifts in correlations in a crisis period);

(ii) details of the quantitative results of stress tests and scenario analyses a bank carried out and the confidence levels and key assumptions behind those analyses, including, the distribution of outcomes obtained for the main individual risk factors;

(iii) details of the range of combined adverse scenarios which have been applied, how these were derived and the resulting capital requirements; and

(iv) where applicable, details of any additional business-unit-specific or business-plan-specific stress tests selected.

(v) Capital transferability

In case of a bank with conglomerate structure, details of any restrictions on the management's ability to transfer capital into or out of the banking business(es) arising from, for example, by contractual, commercial, regulatory or statutory constraints that apply, shall be furnished. Any restrictions applicable and flexibilities available for distribution of dividend by the entities in the group can also be enumerated. In case of overseas banking subsidiaries of a bank, the regulatory restrictions shall include the minimum regulatory capital level acceptable to the host-country regulator of the subsidiary, after declaration of dividend.

(vi) Firm-wide risk oversight and specific aspects of risk management

(a) Risk management system in a bank

This section shall describe the risk management infrastructure within a bank along the following lines:

(i) The oversight of Board and senior management;

(ii) Policies, procedures and limits;

(iii) Identification, measurement, mitigation, controlling and reporting of risks;

(iv) Management information system (MIS) at the bank wide level; and

(v) Internal controls.

(b) Off-balance sheet exposures with a focus on securitisation

This section shall comprehensively discuss and analyse underlying risks inherent in the off-balance sheet exposures particularly its investment in structured products. When assessing securitisation exposures, a bank shall thoroughly analyse the credit quality and risk characteristics of the underlying exposures. This section shall also comprehensively explain the maturity of the exposures underlying securitisation transactions relative to issued liabilities in order to assess potential maturity mismatches.

(c) Assessment of reputational risk and implicit support

This section shall discuss the possibilities of reputational risk leading to provision of implicit support, which might give rise to credit, market, and legal risks. This section shall thoroughly discuss potential sources of reputational risk to a bank.

(d) Assessment of valuation and liquidity risk

This section shall describe the governance structures and control processes for valuing exposures for risk management and financial reporting purposes, with a special focus on valuation of illiquid positions. This section shall have relevant details leading to establishment and verification of valuations for instruments and transactions in which it engages.

(e) Stress testing practices

This section shall explain the role of board and senior management in setting stress testing objectives, defining scenarios, discussing the results of stress tests, assessing potential actions and decision making on the basis of results of stress tests. This section shall also describe the rigorous and forward-looking stress testing that identifies possible events or changes in market conditions that could adversely impact a bank. The Reserve Bank will assess the effectiveness of a bank's stress testing programme in identifying relevant vulnerabilities.

(f) Sound compensation practices

This section shall describe the compensation practices followed by a bank and how far the compensation practices are linked to long-term capital preservation and the financial strength of the firm. The calculation of risk-adjusted performance measure for the employees and its link, if any, with the compensation shall clearly be disclosed in this section.

(vii) Key sensitivities and future scenarios

(a) This section shall explain how a bank would be affected by an economic recession or downswings in the business cycle or markets

relevant to its activities. The Reserve Bank would like to be apprised as to how a bank manages its business and capital so as to survive a recession while meeting the minimum regulatory standards. The analysis shall include future financial projections for, say, three to five years based on business plans and solvency calculations.

(b) For the purpose of this analysis, the severity of the recession reckoned shall typically be one that occurs only once in a 25-year period. The time horizon shall be from the day of the ICAAP calculation to at least the deepest part of the recession envisaged. Typical scenarios shall include:

(i) how an economic downturn shall affect:

(a) a bank's capital funds and future earnings; and

(b) the bank's CRAR taking into account future changes in its projected balance sheet;

(ii) In both cases, it shall be helpful if these projections show separately the effects of management actions to change the bank's business strategy and the implementation of contingency plans;

(iii) projections of the future CRAR shall include the effect of changes in the credit quality of a bank's credit risk counterparties (including migration in its ratings during a recession) and a bank's capital and its credit risk capital requirement;

(iv) an assessment by a bank of any other capital planning actions to enable it to continue to meet its regulatory capital requirements throughout a recession such as new capital injections from related companies or new share issues; and

(v) This section shall also explain which key macroeconomic factors are being stressed, and how those have been identified as drivers of a bank's earnings. The bank shall also explain how the macroeconomic factors affect the key parameters of the internal

model by demonstrating, for instance, how the relationship between the two has been established.

(viii) Management actions

This section shall elaborate on the management actions assumed in deriving the ICAAP, in particular:

(a) the quantitative impact of management actions – sensitivity testing of key management actions and revised ICAAP figures with management actions excluded; and

(b) evidence of management actions implemented in the past during similar periods of economic stress.

(ix) Aggregation and diversification

This section shall describe how the results of the various separate risk assessments are brought together and an overall view taken on capital adequacy. At a technical level, this shall, therefore, require some method to be used to combine the various risks using some appropriate quantitative techniques. At the broader level, the overall reasonableness of the detailed quantification approaches may be compared with the results of an analysis of capital planning and a view taken by senior management as to the overall level of capital that is considered appropriate.

(a) In enumerating the process of technical aggregation, the following aspects can be covered:

(i) any allowance made for diversification, including any assumed correlations within risks and between risks and how such correlations have been assessed, including in stressed conditions;

(ii) the justification for any credit taken for diversification benefits between legal entities, and the justification for the free movement of capital, if any assumed, between them in times of financial stress; and

(iii) the impact of diversification benefits with management actions excluded. It might be helpful to work out revised ICAAP figures

with all correlations set to ‘1’ i.e., no diversification; and similar figures with all correlations set to ‘0’ i.e., assuming all risks are independent i.e., full diversification.

(b) As regards the overall assessment, this shall describe how a bank has arrived at its overall assessment of the capital it needs taking into account such matters as:

(i) the inherent uncertainty in any modelling approach;

(ii) weaknesses in the bank’s risk management procedures, systems or controls;

(iii) the differences between regulatory capital and internal capital; and

(iv) the differing purposes that capital serves: shareholder returns, rating objectives for a bank as a whole or for certain debt instruments the bank has issued, avoidance of regulatory intervention, protection against uncertain events, depositor protection, working capital, capital held for strategic acquisitions, etc.

(x) Testing and adoption of the ICAAP

This section shall describe the extent of challenging and testing that the ICAAP has been subjected to. It shall thus include the testing and control processes applied to the ICAAP models and calculations. It shall also describe the process of review of the test results by the senior management or the Board and the approval of the results by them.

(a) A copy of any relevant report placed before the senior management or the Board of a bank in this regard, along with its response, can be attached to the ICAAP document sent to the Reserve Bank.

(b) Details of the reliance placed on any external service providers or consultants in the testing process, for instance, for generating economic scenarios, can also be detailed here.

(c) In addition, a copy of any report obtained from an external reviewer or internal audit shall also be sent to the Reserve Bank.

(xi) Use of the ICAAP within a bank

(a) This section shall contain information to demonstrate the extent to which the concept of capital management is embedded within a bank, including the extent and use of capital modelling or scenario analyses and stress testing within the bank's capital management policy. For instance, use of ICAAP in setting pricing and charges and the level and nature of future business, can be an indicator in this regard.

(b) This section can also include a statement of a bank's actual operating philosophy on capital management and how this fits into the ICAAP document submitted. For instance, differences in risk appetite used in preparing the ICAAP document vis-à-vis that used for business decisions may be discussed.

(c) Lastly, a bank may also furnish the details of any anticipated future refinements envisaged in the ICAAP (highlighting those aspects which are work-in-progress) apart from any other information that the bank believes would be helpful to the Reserve Bank in reviewing the ICAAP Document.

E Market discipline

239. The requirements related to market discipline shall complement the minimum capital requirements (detailed under Pillar 1) and the supervisory review process (detailed under Pillar 2). The disclosure requirements shall encourage market discipline by allowing market participants to assess key pieces of information on the scope of application, capital, risk exposures, risk assessment processes and hence, the capital adequacy of a bank.

240. A bank's disclosures shall be consistent with how senior management and the Board of Directors assess and manage the risks of the bank.

241. Non-compliance with the prescribed disclosure requirements will attract a penalty, including financial penalty. In specific cases, wherever disclosure is a qualifying criterion under Pillar 1 to obtain lower risk weightings and / or to apply specific methodologies, there shall be a direct sanction (not being allowed to apply the lower risk weighting or use the specific methodology).

242. Interaction with accounting disclosures

The Pillar 3 disclosure framework does not conflict with requirements under applicable Accounting Standards, which are broader in scope. The Reserve Bank will consider future modifications to the market discipline disclosures as necessary in light of its ongoing monitoring of this area and industry developments.

243. Validation

(1) The disclosures shall be subjected to adequate validation. For example, since information in the annual financial statements would generally be audited, the additional material published with such statements shall be consistent with the audited statements.

(2) Supplementary material (such as management's discussion and analysis) that is published shall also be subjected to sufficient scrutiny (e.g., internal control assessments, etc.) to satisfy the validation requirement.

(3) If material is not published under a validation regime, for instance in a stand-alone report or as a section on a website, then management shall ensure that appropriate verification of the information takes place, in accordance with the general disclosure principle set out below. In the light of the above, Pillar 3 disclosures are not required to be audited by an external auditor, unless specified.

244. Materiality

(1) A bank shall decide which disclosures are relevant for it based on the materiality concept.

(2) Information shall be regarded as material if its omission or misstatement could change or influence the assessment or decision of a user relying on that information for the purpose of making economic decisions. This definition is consistent with International Accounting Standards and with the national accounting framework. The Reserve Bank recognises the need for a qualitative judgment of whether, in light of the particular circumstances, a user of financial information would consider the item to be material (user test). The Reserve Bank does not consider it necessary to set specific thresholds for disclosure as the

user test is a useful benchmark for achieving sufficient disclosure. A bank is encouraged to apply the user test to these specific disclosures and where considered necessary, make disclosures below the specified thresholds also.

245. General disclosure Principle

(1) A bank shall have a formal disclosure policy approved by the Board of Directors that addresses a bank's approach for determining what disclosures it shall make and the internal controls over the disclosure process.

(2) A bank shall implement a process for assessing the appropriateness of its disclosures, including validation and frequency.

246. Scope and frequency of disclosures

(1) Pillar 3 applies at the top consolidated level of the banking group to which the Capital Adequacy Framework applies. Disclosures related to individual banks within the group would not generally be required to be made by the parent bank. An exception to this arises in the disclosure of capital ratios by the top consolidated entity where an analysis of significant bank subsidiaries within the group shall be appropriate, in order to recognize the need of these subsidiaries to comply with the framework and other applicable limitations on the transfer of funds or capital within the group.

(2) Pillar 3 disclosures shall be required to be made by an individual bank on a stand-alone basis when it is not the top consolidated entity in the banking group.

(3) A bank shall make Pillar 3 disclosures at least on a half yearly basis, irrespective of whether financial statements are audited. However, following disclosures listed in Annex III shall be made at least on a quarterly basis by a bank:

(i) Table DF-2: Capital adequacy;

(ii) Table DF-3: Credit risk: General disclosures for all banks; and

(iii) Table DF-4: Credit risk: Disclosures for portfolios subject to the standardised approach.

(4) All disclosures shall either be included in a bank's published financial results / statements or, at a minimum, shall be disclosed on the bank's website.

(5) A bank shall make Pillar 3 disclosures concurrently with publication of financial results / statements. If a bank finds it operationally inconvenient to make these disclosures along with published financial results / statements, it shall provide in these financial results / statements, a direct link to where the Pillar 3 disclosures can be found on the bank's website. However, a bank shall ensure that in the case of main features template [as indicated in paragraph 248(2)(iii) and provision of the full terms and conditions of capital instruments [as indicated in paragraph 248(2)(iv)], the bank shall update these disclosures concurrently whenever a new capital instrument is issued and included in capital or whenever there is a redemption, conversion / write-down or other material change in the nature of an existing capital instrument.

Note - It may be noted that Pillar 3 disclosures are required to be made by all banks including those which are not listed on stock exchanges and / or not required to publish financial results / statement. Therefore, such banks are also required to make Pillar 3 disclosures at least on their websites within reasonable period.

247. Regulatory disclosure section

(1) A bank shall make disclosures in the format as specified in Annex III of these Directions.

(2) A bank shall maintain a 'Regulatory Disclosures Section' on its website, where all the information relating to disclosures shall be made available to the market participants.

(3) The direct link to 'Regulatory Disclosures Section' page shall be prominently provided on the home page of a bank's website and it shall be easily accessible.

(4) An archive for at least three years of all templates relating to prior reporting periods shall be made available by a bank on its website.

248. Pillar 3 under Basel III Framework

(1) The disclosure requirements are set out in the form of following templates:

(i) Disclosure Template: A common template shall be used by a bank to report the details of its regulatory capital. It is designed to meet the Basel III requirement to disclose all regulatory adjustments.

(ii) Reconciliation requirements: To meet the reconciliation requirements as envisaged under Basel III, a three-step approach has been devised. This step-by-step approach to reconciliation ensures that the Basel III requirement to provide a full reconciliation of all regulatory capital elements back to the published financial statements is met in a consistent manner.

(iii) Main features template: A common template has been prescribed to capture the main features of all regulatory capital instruments issued by a bank at one place. This disclosure requirement is intended to meet the Basel III requirement to provide a description of the main features of capital instruments.

(iv) Other disclosure requirements: This disclosure enables a bank in meeting the Basel III requirement to provide the full terms and conditions of capital instruments on its websites.

(v) Pillar 3 disclosure requirements also include certain aspects that are not specifically required to compute capital requirements under Pillar 1. It may be noted that beyond disclosure requirements as set forth in these Directions, a bank is responsible for conveying its actual risk profile to market participants. The information a bank disclose shall be adequate to fulfil this objective. In addition to the specific disclosure requirements as set out in these Directions, a bank operating in India shall also make additional disclosures in the following areas:

(a) Securitisation exposures in the trading book;

(b) Sponsorship of off-balance sheet vehicles;

(c) Valuation with regard to securitisation exposures; and

(d) Pipeline and warehousing risks with regard to securitisation exposures.

(2) The templates are described in detail as under:

(i) Disclosure template

(a) The common template which a bank shall use is set out in Table DF-11 of Annex III, along with explanations.

(b) A bank shall not add or delete any rows / columns from the common reporting template. The template shall retain the same row numbering used in its first column such that market participants can easily map the Indian version of templates to the common version designed by the BCBS.

(ii) Reconciliation requirements

(a) A bank shall disclose a full reconciliation of all regulatory capital elements back to the balance sheet in the audited (or unaudited) financial statements.

(b) A bank shall follow a three-step approach to show the link between its balance sheet and the numbers which are used in the composition of capital disclosure template set out in Annex III (Table DF-11 whichever applicable). The three steps are mentioned below and also illustrated in Table DF-12 of Annex III:

(i) Step 1: A bank shall disclose the reported balance sheet under the regulatory scope of consolidation (Table DF-12 of Annex III);

(ii) Step 2: A bank shall expand the lines of the balance sheet under regulatory scope of consolidation (Table DF-12 of Annex III) to display all components which are used in the composition of capital disclosure template (Table DF-11 of Annex III); and

(iii) Step 3: finally, a bank shall map each of the components that are disclosed in Step 2 to the composition of capital disclosure template set out in Table DF-11 of Annex III whichever, applicable.

(c) Step 1: Disclose the reported balance sheet under the regulatory scope of consolidation

(i) The scope of consolidation for accounting purposes is often different from that applied for the regulatory purposes. Usually, there will be difference between the financial statements of a bank specifically, the bank's balance sheet in published financial statements and the balance sheet considered for the calculation of

regulatory capital. Therefore, the reconciliation process involves disclosing how the balance sheet changes when the regulatory scope of consolidation is applied for the purpose of calculation of regulatory capital on a consolidated basis.

(ii) Accordingly, a bank is required to disclose the list of the legal entities which have been included within accounting scope of consolidation but excluded from the regulatory scope of consolidation. Similarly, a bank is required to list the legal entities which have been included in the regulatory consolidation but not in the accounting scope of consolidation. Finally, it is possible that some entities are included in both the regulatory scope of consolidation and accounting scope of consolidation, but the method of consolidation differs between these two scopes. In such cases, a bank is required to list these legal entities and explain the differences in the consolidation methods.

(iii) If the scope of regulatory consolidation and accounting consolidation is identical for a particular banking group, it would not be required to undertake Step 1. The banking group would state that there is no difference between the regulatory consolidation and the accounting consolidation and move to Step 2.

(iv) In addition to the above requirements, a bank shall disclose for each legal entity, its total balance sheet assets, total balance sheet equity (as stated on the accounting balance sheet of the legal entity), method of consolidation and a description of the principle activities of the entity. These disclosures are required to be made as indicated in the revised templates namely Table DF-1: Scope of Application of Annex III.

(d) Step 2: Expand the lines of the regulatory balance sheet to display all of the components used in the definition of capital disclosure template (Table DF-11 of Annex III)

(i) A bank should expand the rows of the balance sheet under regulatory scope of consolidation such that all the components used

in the definition of capital disclosure template (Table DF-11 of Annex III) are displayed separately.

(ii) For example, paid-up share capital may be reported as one line on the balance sheet. However, some elements of this may meet the requirements for inclusion in CET1 capital and other elements may only meet the requirements for AT1 or Tier 2 capital, or may not meet the requirements for inclusion in regulatory capital at all. Therefore, if a bank has some amount of paid-up capital which goes into the calculation of CET1 and some amount which goes into the calculation of AT1, it should expand the 'paid-up share capital' line of the balance sheet in the following way:

Paid-up share capital		Ref
of which amount eligible for CET1		e
of which amount eligible for AT1		f

(iii) In addition, as illustrated above, each element of the expanded balance sheet shall be given a reference number / letter for use in Step 3.

(iv) Another example is regulatory adjustments of the deduction of intangible assets. Firstly, there could be a possibility that the intangible assets may not be readily identifiable in the balance sheet. There is a possibility that the amount on the balance sheet may combine goodwill and other intangibles. Secondly, the amount to be deducted is net of any related deferred tax liability. This deferred tax liability is likely to be reported in combination with other deferred tax liabilities which have no relation to goodwill or intangibles. Therefore, a bank should expand the balance sheet in the following way:

Goodwill and intangible assets		Ref
of which goodwill		a
of which other intangibles		b

Current and deferred tax liabilities (DTLs)		Ref
of which DTLs related to goodwill		c
of which DTLs related to other intangible assets		d

(v) A bank shall need to expand elements of the balance sheet only to the extent required to reach the components which are used in the definition of capital disclosure template. For example, if entire paid-up capital of the bank met the requirements to be included in CET1, the bank would not need to expand this line.

(e) Step 3: Map each of the components that are disclosed in Step 2 to the composition of capital disclosure templates

(i) When reporting the disclosure template (i.e., Table DF-11 of Annex III), a bank is required to use the reference numbers / letters from Step 2 to show the source of every input.

(ii) For example, if the composition of capital disclosure template includes the line 'goodwill net of related deferred tax liability', then next to this item the bank should put 'a - c'. This is required to illustrate how these components of the balance sheet under the regulatory scope of consolidation have been used to calculate this item in the disclosure template.

(iii) Main features template

(a) A bank shall disclose a description of the main features of capital instruments issued by them. The template in Table DF-13 of Annex III represents the minimum level of summary disclosure which the bank is required to report in respect of each regulatory capital instrument issued.

(b) The main feature disclosure template is set out in Table DF-13 of Annex III along with a description of each of the items to be reported. A bank shall report each capital instrument (including common shares) in a separate column of the template, such that the completed template would provide a 'main features report' that summarises all of the regulatory capital instruments of the banking group.

(c) A bank shall keep the completed main features report up to date. A bank shall ensure that the report is updated and made publicly available, whenever a bank issues or repays a capital instrument and

whenever there is redemption, conversion / write-down or other material change in the nature of an existing capital instrument.

(iv) Other disclosure requirements

In addition to the disclosure requirements set out in above paragraphs, a bank is required to make the following disclosure in respect of the composition of capital:

(a) Full terms and conditions: A bank is required to make available on its websites, under the regulatory disclosure section, the full terms and conditions of all instruments included in regulatory capital (Table DF-14 of Annex III); and

(b) A bank shall keep the terms and conditions of all capital instruments up to date. Whenever there is a change in the terms and conditions of a capital instrument, a bank shall update them promptly and make publicly available such updated disclosure.

249. Format of disclosure template

All Pillar 3 disclosure templates as set out in these guidelines are furnished in tabular form in Annex III. Additional relevant definitions and explanations are also provided for the Pillar 3 disclosures.

Chapter VI

Capital buffers

A Capital Conservation Buffer (CCB) Framework

250. CCB is designed to ensure that a bank builds up capital buffers during normal times (i.e., outside periods of stress) which can be drawn down as losses are incurred during a stressed period. The requirement is based on simple capital conservation rules designed to avoid breaches of minimum capital requirements.

251. The Framework

(1) A bank is required to maintain a CCB of 2.5 per cent which shall comprise of CET1 capital, above the regulatory minimum capital requirement of 9 per cent.

Explanation – CET1 shall first be used to meet the minimum capital requirements (including the 7 per cent Tier 1 and 9 per cent total capital requirements, if necessary), before the remainder can contribute to the CCB requirement.

(2) Capital distribution constraints shall be imposed on a bank when capital level falls within this range. However, a bank shall be able to conduct business as normal when its capital levels fall into the conservation range as it experiences losses. Therefore, the constraints imposed are related to the distributions only and are not related to the operations of banks.

(3) Elements subject to the restrictions on distributions: Dividends and share buybacks, discretionary payments on other Tier 1 capital instruments and discretionary bonus payments to staff shall constitute items considered to be distributions. Payments which do not result in depletion of CET1 capital, (for example certain scrip dividends) are not considered distributions. Earnings are defined as distributable profits before the deduction of elements subject to the restriction on distributions mentioned above. Earnings are calculated after the tax which would have been reported had none of the distributable items been paid. As such, any tax impact of making such distributions is reversed out. If a bank does not have positive earnings and has a CET1 ratio less than 8 per cent, it shall not make positive net distributions.

Note - A scrip dividend is a scrip issue made in lieu of a cash dividend. The term ‘scrip dividends’ also includes bonus shares.

(4) The distribution constraints imposed on a bank when its capital levels fall into the range increase as the bank's capital levels approach the minimum requirements. The Table 46 below shows the minimum capital conservation ratios a bank shall meet at various levels of the CET1 capital ratios:

Table 46: Minimum capital conservation standards for individual bank

CET1 ratio after including the current periods retained earnings	Minimum capital conservation ratios (expressed as a percentage of earnings)
5.5% - 6.125%	100%
>6.125% - 6.75%	80%
>6.75% - 7.375%	60%
>7.375% - 8.0%	40%
>8.0%	0%

For example, a bank with a CET1 capital ratio in the range of 6.125 per cent to 6.75 per cent shall be required to conserve 80 per cent of its earnings in the subsequent financial year (i.e., payout no more than 20 per cent in terms of dividends, share buybacks and discretionary bonus payments is allowed).

(5) The CET1 ratio includes amounts used to meet the minimum CET1 capital requirement of 5.5 per cent but excludes any additional CET1 needed to meet the 7 per cent Tier 1 and 9 per cent total capital requirements. For example, a bank maintains CET1 capital of 9 per cent and has no AT1 or Tier 2 capital. Therefore, the bank shall meet all minimum capital requirements, but shall have a zero-conservation buffer and therefore, the bank shall be subject to 100 per cent constraint on distributions of capital by way of dividends, share-buybacks and discretionary bonuses.

(6) The capital conservation buffer can be drawn down only when a bank faces a systemic or idiosyncratic stress.

(7) A bank shall not choose in normal times to operate in the buffer range simply to compete with other banks and win market share. This aspect shall be specifically looked into by the Reserve Bank during the SREP. If, at any time, a bank is found to have allowed its CCB to fall in normal times, particularly by increasing its risk weighted assets without a commensurate increase in the CET1 Ratio (although adhering to the restrictions on distributions), this shall be viewed seriously. Such

a bank shall be required to bring the buffer to the desired level within a time limit prescribed by the Reserve Bank.

(8) A bank which draws down its CCB during a stressed period shall also have a definite plan to replenish the buffer as part of ICAAP and strive to bring the buffer to the desired level within a time limit agreed to with the Reserve Bank during the SREP.

(9) A bank may also choose to raise new capital from the market as an alternative to conserving internally generated capital. However, if a bank decides to make payments in excess of the constraints imposed as explained above, the bank, with the prior approval of the Reserve Bank, shall have to use the option of raising capital from the market equal to the amount above the constraint which it wishes to distribute.

252. Application of the CCB

CCB is applicable both at the solo level (global position) as well as at the consolidated level, i.e., restrictions shall be imposed on distributions at the level of both the solo bank and the consolidated group. In all cases where the bank is the parent of the group, it shall mean that distributions by the bank can be made only in accordance with the lower of its CET1 ratio at solo level or consolidated level. For example, if a bank's CET1 ratio at solo level is 6.8 per cent and that at consolidated level is 7.4 per cent, it shall be subject to a capital conservation requirement of 60 per cent consistent with the CET1 range of >6.75 - 7.375 per cent as per Table 46 in paragraph 251(4) above. Suppose a bank's CET1 ratio at solo level is 6.6 per cent and that at consolidated level is 6 per cent. It shall be subject to a capital conservation requirement of 100 per cent consistent with the CET1 range of >5.5 per cent - 6.125 per cent as per Table 46 on minimum capital conservation standards for individual bank.

Explanation **-** If a subsidiary is a bank, it shall naturally be subject to the provisions of CCB. If it is not a bank, even then the parent bank shall not allow the subsidiary to distribute dividend which is inconsistent with the position of CCB at the consolidated level.

B Capital requirements applicable to banks designated as Domestic Systemically Important Banks (D-SIB)

253. The D-SIBs Framework aims at enhancing the loss absorbency of D-SIBs over and above the minimum Basel III capital adequacy requirement. The Reserve Bank vide press release dated July 22, 2014 has issued the 'Framework for Dealing with Domestic Systemically Important Banks (D-SIBs)'. In terms of this Framework, the process of identification of D-SIBs is a two-step process under which, first, the sample of banks to be assessed for their systemic importance shall be decided by the Reserve Bank and then based on a range of indicators (size, interconnectedness, substitutability, and complexity) a composite score of systemic importance for each bank in the sample shall be computed. Based on the score arrived under this framework, the Reserve Bank shall identify and disclose the names of banks designated as D-SIBs annually. These D-SIBs shall be segregated into different buckets based on their systemic importance scores and subject to loss absorbency capital surcharge in a graded manner depending on the buckets in which they are placed. A D-SIB in the lower bucket will attract a lower capital charge, and a D-SIB in the higher bucket will attract a higher capital charge. The additional capital charge imposed on DSIBs, as identified by the Reserve Bank, shall be maintained in the form of CET1 capital. A table showing the additional CET1 capital requirement for D-SIBs is presented below:

Table 47: Additional CET1 capital requirement for D-SIBs

Bucket	Additional CET1 requirement (as a percentage of RWAs)
5 (Empty)	1.00%
4	0.80%
3	0.60%
2	0.40%
1	0.20%

254. The additional CET1 requirements shall be applicable at the level of both solo as well as consolidated level of the D-SIB, in line with extant capital adequacy provisions.

255. The higher CET1 requirements shall be applicable as an extension of CCB. If a D-SIB is not able to meet the additional CET1 requirement, it shall be subject to restrictions on distribution of profits and other restrictions as applicable under the

CCB framework of these Directions. For example, a D-SIB falling in Bucket 1 shall be required to maintain a CET1 capital of 8.2 per cent of the RWAs if it does not want to have any restrictions on it with regard to dividend / capital distribution applicable under the capital buffer regime.

Requirements specific to a foreign bank

256. The maintenance of additional CET1 by a foreign bank in India whether operating as a branch or a WOS, and as a Globally - Systemically Important Bank (G-SIB) or D-SIB, shall be guided by following rules:

(1) In case a foreign bank having branch presence in India is a G-SIB, it shall maintain additional CET1 capital surcharge in India as applicable to it as G-SIB, proportionate to its RWAs in India. Additional CET1 requirement for such bank in India shall be computed as additional CET1 buffer prescribed by the home regulator multiplied by (India RWA as per consolidated global group books / total consolidated global group RWA). Additional CET1 may be phased in India in accordance with the phase-in prescribed by the home regulator;

(2) In case a foreign bank having branch presence in India is not a G-SIB, but a D-SIB in India, it has to maintain D-SIB additional capital surcharge in India;

(3) In case a foreign bank having branch presence in India is both a G-SIB and a D- SIB in India, it has to maintain capital surcharge in India, at a rate which is higher of the two (G-SIB additional CET1 surcharge or D-SIB additional CET1 surcharge); and

(4) In case of a foreign bank having presence in India as a WOS of its parent bank which is a G-SIB, it shall not maintain G-SIB capital surcharge in India as it will have the status of a domestic bank. However, if the WOS is designated as a D-SIB in India, it shall maintain D-SIB capital surcharge in India.

257. Banks may note that the Reserve Bank has carried out a review of the assessment methodology vide press release ‘Domestic Systemically Important Bank (D-SIB) Framework - Review of the Assessment Methodology’ dated December 28, 2023.

C Countercyclical Capital Buffer (CCCB)

258. The aim of the CCCB regime is twofold. Firstly, it requires a bank to build up a buffer of capital in good times which may be used to maintain flow of credit to the real sector in difficult times. Secondly, it achieves the broader macro-prudential goal of restricting the banking sector from indiscriminate lending in the periods of excess credit growth that have often been associated with the building up of system-wide risk.

259. The Framework

(1) A bank shall maintain CCCB in the form of CET1 capital only, and the amount of the CCCB may vary from 0 to 2.5 per cent of RWA of the bank, depending on the assessment of the Reserve Bank.

(2) If, as per the Reserve Bank directives, a bank is required to hold CCCB at a given point in time, the same shall be disclosed in table DF-11 of Annex III.

(3) The CCCB decision shall normally be pre-announced by the Reserve Bank with a lead time of four quarters. However, depending on the CCCB indicators, a bank may be advised to build up requisite buffer in a shorter span of time.

(4) Indicators considered by the Reserve Bank for invoking CCCB

(i) The credit-to-GDP gap shall be the main indicator in the CCCB framework in India. However, it shall not be the only reference point and shall be used in conjunction with GNPA growth.

Explanation - Credit-to-GDP gap is the difference between credit-to-GDP ratio and the long-term trend value of credit-to-GDP ratio at any point in time.

(ii) The Reserve Bank shall also look at other supplementary indicators for CCCB decision such as incremental credit to deposit (C-D) ratio for a moving period of three years (along with its correlation with credit-to-GDP gap and Gross NPA (GNPA) growth), Industry outlook (IO) assessment index (along with its correlation with GNPA growth) and interest coverage ratio (along with its correlation with credit-to-GDP gap).

(iii) While taking the final decision on CCCB, the Reserve Bank may use its discretion to use all or some of the indicators along with the credit-to-GDP gap.

(5) The CCCB framework shall have two thresholds, viz., lower threshold and upper threshold, with respect to credit-to-GDP gap.

(i) The lower threshold (L) of the credit-to-GDP gap where the CCCB is activated shall be set at 3 percentage points, provided its relationship with GNPA remains significant. The buffer activation decision shall also depend upon other supplementary indicators as detailed in paragraph 259(4) above.

(ii) The upper threshold (H) where the CCCB reaches its maximum shall be kept at 15 percentage points of the credit-to-GDP gap. Once the upper threshold of the credit-to-GDP gap is reached, the CCCB shall remain at its maximum value of 2.5 per cent of RWA, till the time a withdrawal is signalled by the Reserve Bank.

(iii) In between 3 and 15 percentage points of credit-to-GDP gap, the CCCB shall increase gradually from 0 to 2.5 per cent of the RWA of the bank but the rate of increase would be different based on the level / position of credit-to-GDP gap between 3 and 15 percentage points. If the credit-to-GDP gap is below 3 percentage points, there will not be any CCCB requirement.

Explanation - The CCCB requirement shall increase linearly from 0 to 20 basis points when credit-to-GDP gap moves from 3 to 7 percentage points. Similarly, for above 7 and up to 11 percentage points range of credit-to-GDP gap, CCCB requirement shall increase linearly from above 20 to 90 basis points. Finally, for above 11 and up to 15 percentage points range of credit-to-GDP gap, the CCCB requirement shall increase linearly from above 90 to 250 basis points. However, if the credit-to-GDP gap exceeds 15 percentage points, the buffer shall remain at 2.5 per cent of the RWA.

(6) The same set of indicators that are used for activating CCCB may be used to arrive at the decision for the release phase of the CCCB. However, discretion shall be with the Reserve Bank for operating the release phase of CCCB. Further, the entire CCCB accumulated may be released at a single point in time but the

use of the same by a bank shall not be unfettered and shall need to be decided only after discussion with the Reserve Bank.

(7) For a bank operating in India, CCCB shall be maintained on a solo basis as well as on consolidated basis.

(8) A bank operating in India (both foreign and domestic bank) shall maintain capital for Indian operations under CCCB framework based on its exposures in India.

(9) A bank incorporated in India having international presence shall maintain adequate capital under CCCB as prescribed by the host supervisors in respective jurisdictions. The bank, based on the geographic location of its private sector credit exposures (including non-bank financial sector exposures), shall calculate its bank specific CCCB requirement as a weighted average of the requirements that are being applied in respective jurisdictions.

Explanation - Weight = (bank's total credit risk charge that relates to private sector credit exposures in that jurisdiction / bank's total credit risk charge that relates to private sector credit exposures across all jurisdictions), where credit includes all private sector credit exposures that attract a credit risk capital charge, or the risk weighted equivalent trading book capital charges for specific risk, Incremental Risk Charge (IRC) (as per applicability in a jurisdiction) and securitisation.

(10) The Reserve Bank may also ask an Indian bank to keep excess capital under CCCB framework for exposures in any of the host countries they are operating if it feels the CCCB requirement in host country is not adequate.

(11) A bank shall be subject to restrictions on discretionary distributions (may include dividend payments, share buybacks and staff bonus payments) if it does not meet the requirement on CCCB which is an extension of the requirement for the CCB. Assuming a concurrent requirement of CCB of 2.5 per cent and CCCB of 2.5 per cent of RWAs, the required conservation ratio (restriction on discretionary distribution) of a bank, at various levels of CET1 capital held is illustrated in table below:

Table 48: Individual bank minimum capital conservation ratios, assuming a requirement of 2.5 per cent each of CCB and CCCB

CET1 ratio bands	Minimum capital conservation ratios (expressed as % of earnings)
>5.5%-6.75%	100%
>6.75%-8.0%	80%
>8.0%-9.25%	60%
>9.25%-10.50%	40%
>10.50%	0%

The CET1 ratio bands are structured in increments of 25 per cent of the required CCB and CCCB prescribed by the Reserve Bank at that point in time.

Explanation - First CET1 ratio band = Minimum CET1 ratio + 25 per cent of CCB + 25 per cent of applicable CCCB. For subsequent bands, starting point will be the upper limit of previous band. However, it may be mentioned that CET1 ratio band may change depending on various capital / buffer requirements (e.g., D-SIB buffer) as prescribed by the Reserve Bank from time to time. Accordingly, lower and upper values of the bands as given in Table 32 will undergo changes.

A separate illustrative table is given below with an assumption of CCCB requirement at 1 per cent.

Table 49: Individual bank minimum capital conservation standards, when a bank is subject to a 2.5 per cent CCB and 1 per cent CCCB

CET1 ratio bands	Minimum capital conservation ratios (expressed as % of earnings)
> 5.5% - 6.375%*	100%
> 6.375% - 7.25%	80%
> 7.25% - 8.125%	60%
> 8.125% - 9.00%	40%
> 9.00%	0%

*(6.375 = 5.50+0.625+0.250)

As the total requirement of CCB and CCCB is 2.5 per cent and 1 per cent respectively, at each band, 0.625 per cent and 0.250 per cent of RWA are being added for CCB and CCCB respectively.

(12) A bank shall ensure that its CCCB requirements are calculated and publicly disclosed with at least the same frequency as its minimum capital requirements as applicable in various jurisdictions. The buffer shall be based on the latest relevant jurisdictional CCCB requirements that are applicable on the date that it

calculate its minimum capital requirement. When disclosing its buffer requirement, a bank shall also disclose the geographic breakdown of its private sector credit exposures used in the calculation of the buffer requirement.

260. The CCCB decisions may form a part of the first bi-monthly monetary policy statement of the Reserve Bank for the year. However, more frequent communications in this regard may be made by the Reserve Bank, if warranted by changes in economic conditions.

261. The indicators and thresholds for CCCB decisions mentioned above shall be subject to continuous review and empirical testing for their usefulness and other indicators may also be used by the Reserve Bank to support CCCB decisions.

Chapter VII

Leverage Ratio framework

A Definition, minimum requirement, and scope of application of the Leverage Ratio

262. The Basel III leverage ratio is defined as the capital measure (the numerator) divided by the exposure measure (the denominator), with this ratio expressed as a percentage.

$$\text{Leverage Ratio} = \frac{\text{Capital Measure}}{\text{Exposure Measure}}$$

The minimum leverage ratio for a Domestic Systemically Important Bank (D- SIB) shall be 4 per cent and 3.5 per cent for other banks. Both the capital measure and the exposure measure along with leverage ratio are to be disclosed on a quarter-end basis. However, a bank shall meet the minimum leverage ratio requirement at all times.

B Scope of consolidation

263. The scope of consolidation of leverage ratio shall be as under:

(1) The Basel III leverage ratio framework shall follow the same scope of regulatory consolidation as is used for the risk-based capital framework.

(2) In cases where a banking, financial, insurance or commercial entity is outside the scope of regulatory consolidation, only the investment in the capital of such entities (i.e., only the carrying value of the investment, as opposed to the underlying assets and other exposures of the investee) shall be included in the leverage ratio exposure measure. However, investments in the capital of such entities that are deducted from Tier 1 capital (i.e., either deduction from CET1 capital or deduction from AT1 capital following corresponding deduction approach) as set out in paragraph 28 - Regulatory adjustments / deductions shall be excluded from the leverage ratio exposure measure.

C Capital measure

264. The capital measure for the leverage ratio is the Tier 1 capital (as defined under paragraph 10) of the risk-based capital framework, taking into account various regulatory adjustments / deductions. In other words, the capital measure used

for the leverage ratio at any particular point in time is the Tier 1 capital measure applied at that time under the risk-based framework.

D Exposure measure

265. General measurement principle

(1) The exposure measure for the leverage ratio shall follow the accounting value, subject to the following:

(i) on-balance sheet, non-derivative exposures shall be included in the exposure measure net of specific provisions or accounting valuation adjustments (e.g., accounting credit valuation adjustments, prudent valuation adjustments); and

(ii) netting of loans and deposits is not allowed.

(2) Unless specified differently below, a bank shall not take account of physical or financial collateral, guarantees or other credit risk mitigation techniques to reduce the exposure measure.

(3) A bank's total exposure measure shall be the sum of the following exposures:

(i) on-balance sheet exposures;

(ii) derivative exposures;

(iii) securities financing transaction (SFT) exposures; and

(iv) off-balance sheet (OBS) items.

The specific treatments for these four main exposure types are defined in paragraphs 266 to 269 below.

266. On-balance sheet exposures

(1) A bank shall include all balance sheet assets in its exposure measure, including on-balance sheet derivatives collateral and collateral for SFTs, with the exception of on-balance sheet derivative and SFT assets that are covered in paragraphs 267 and 268 below.

Note - where a bank according to its operative accounting framework recognises fiduciary assets on the balance sheet, these assets can be excluded from the leverage ratio exposure measure if the assets meet the criteria for derecognition

and, where applicable for deconsolidation as per applicable Accounting Standards. When disclosing the leverage ratio, a bank shall also disclose the extent of such derecognised fiduciary items.

(2) To ensure consistency, balance sheet assets deducted from Tier 1 capital as set out in paragraph 28 - Regulatory adjustments / deductions shall be deducted from the exposure measure. For example, where a banking, financial or insurance entity is not included in the regulatory scope of consolidation [as set out in paragraph 263], the amount of any investment in the capital of that entity that is totally or partially deducted from CET1 capital or from AT1 capital of the bank [in terms of paragraphs 8(6) and 28(8)(ii)] shall also be deducted from the exposure measure.

(3) Liability items shall not be deducted from the exposure measure.

Explanation – For example, gains / losses on fair valued liabilities or accounting value adjustments on derivative liabilities due to changes in the bank's own credit risk as described in paragraph 28(5) shall not be deducted from the exposure measure.

267. Derivative exposures

(1) A bank shall calculate its derivative exposures, including where it sells protection using a credit derivative, as the Replacement Cost (RC) for the current exposure plus an add-on for Potential Future Exposure (PFE), as described in paragraph 267(2) below. If the derivative exposure is covered by an eligible bilateral netting contract as specified in the paragraph 87(2), an alternative treatment as indicated in paragraph 267(3) below may be applied. Written credit derivatives shall be subjected to an additional treatment, as set out in paragraphs 267(7).

Note -

(1) To calculate CCR exposure amounts associated with derivative exposure, a bank shall use the CEM.

(2) If, under the relevant Accounting Standards, there is no accounting measure of exposure for certain derivative instruments because they are held (completely) off-balance sheet, a bank shall use the sum of positive fair values of these derivatives as the RC.

(3) With reference to the alternative treatment as indicated in paragraph 267(3), netting rules are with the exception of cross-product netting i.e., cross-product netting shall not be permitted in determining the leverage ratio exposure measure. However, where a bank has a cross-product netting agreement in place that meets the eligibility criteria of paragraph 87(2) it may choose to perform netting separately in each product category provided that all other conditions for netting in this product category that are applicable to the Basel III leverage ratio are met.

(2) For a single derivative contract, not covered by an eligible bilateral netting contract as specified in paragraph 87(2), the amount to be included in the exposure measure shall be determined as follows:

Exposure measure = RC + Add-on

Where:

RC = the replacement cost of the contract (obtained by marking to market), where the contract has a positive value; and

Add-on = an amount for PFE over the remaining life of the contract calculated by applying an add-on factor to the notional principal amount of the derivative. The add-on factors are given in Table 16 of paragraph 85(2) and Tables 41 and 42 under paragraphs 204.

(3) Bilateral netting

When an eligible bilateral netting contract is in place as specified in paragraph 87(2), the RC for the set of derivative exposures covered by the contract shall be the sum of net RC and the add-on factors as described in paragraph 267(2) above shall be A_{Net} as calculated below:

(i) Credit exposure on bilaterally netted forward transactions shall be calculated as the sum of the net mark-to-market RC, if positive, plus an add-on based on the notional underlying principal. The add-on for netted transactions (A_{Net}) shall be equal to the weighted average of the gross add-on (A_{Gross}) and the gross add-on adjusted by the ratio of net current RC to gross current RC (NGR). This is expressed through the following formula:

$$A_{Net} = 0.4 \cdot A_{Gross} + 0.6 \cdot NGR \cdot A_{Gross}$$

where:

NGR = level of net RC / level of gross RC for transactions subject to legally enforceable netting agreements. A bank shall calculate NGR on a counterparty-by-counterparty basis for all transactions that are subject to legally enforceable netting agreements; and

A_{Gross} = sum of individual add-on amounts [calculated by multiplying the notional principal amount by the appropriate add-on factors set out in Table 16 of paragraph 85(2) and Tables 41 and 42 under paragraphs 204 of all transactions subject to legally enforceable netting agreements with one counterparty.

(ii) For calculating potential future credit exposure to a netting counterparty for forward foreign exchange contracts and other similar contracts in which the notional principal amount is equivalent to cash flows, the notional principal is defined as the net receipts falling due on each value date in each currency. The reason for this is that offsetting contracts in the same currency maturing on the same date shall have lower PFE as well as lower current exposure.

(4) Treatment of related collateral

(i) As a general rule, collateral received shall not be netted against derivative exposures whether or not netting is permitted under the bank's operative accounting or risk-based framework. Therefore, when calculating the exposure amount by applying paragraphs 267(1) to 267(3), a bank shall not reduce the exposure amount by any collateral received from the counterparty.

(ii) With regard to collateral provided, a bank shall gross up its exposure measure by the amount of any derivatives collateral provided where the effect of providing collateral has reduced the value of its balance sheet assets under its operative accounting framework.

(5) Treatment of cash variation margin

(i) In the treatment of derivative exposures for the purpose of the leverage ratio, the cash portion of variation margin exchanged between

counterparties shall be viewed as a form of pre-settlement payment, if the following conditions are met:

(a) For trades not cleared through a qualifying central counterparty (QCCP), the cash received by the recipient counterparty is not segregated.

Explanation - Cash variation margin will satisfy the non-segregation criterion if the recipient counterparty has no restrictions on the ability to use the cash received (i.e., the cash variation margin received is used as its own cash). Further, this criterion will be met if the cash received by the recipient counterparty is not required to be segregated by law, regulation, or any agreement with the counterparty;

(b) Variation margin is calculated and exchanged on a daily basis based on mark-to-market valuation of derivatives positions.

Explanation - To meet this criterion, derivative positions shall be valued daily and cash variation margin shall be transferred daily to the counterparty or to the counterparty's account, as appropriate;

(c) The cash variation margin is received in the same currency as the currency of settlement of the derivative contract.

Explanation - Currency of settlement means any currency of settlement specified in the derivative contract, governing qualifying master netting agreement (MNA), or the credit support annex (CSA) to the qualifying MNA;

(d) Variation margin exchanged shall be the full amount that would be necessary to fully extinguish the mark-to-market exposure of the derivative subject to the threshold and minimum transfer amounts applicable to the counterparty.

Explanation - Cash variation margin exchanged on the morning of the subsequent trading day based on the previous, end-of-day market values will meet this criterion, provided that the variation margin exchanged is the full amount that will be necessary to fully extinguish

the mark-to-market exposure of the derivative subject to applicable threshold and minimum transfer amounts; and

(e) Derivatives transactions and variation margins are covered by a single MNA between the legal entities that are the counterparties in the derivatives transaction. The MNA shall explicitly stipulate that the counterparties agree to settle net any payment obligations covered by such a netting agreement, taking into account any variation margin received or provided if a credit event occurs involving either counterparty. The MNA shall be legally enforceable and effective in all relevant jurisdictions, including in the event of default and bankruptcy or insolvency.

Note -

(1) A Master MNA may be deemed to be a single MNA for this purpose.

(2) To the extent that the criteria in this paragraph include the term 'master netting agreement', this term shall be read as including any 'netting agreement' that provides legally enforceable rights of offsets. This is to take account of the fact that no standardisation has currently emerged for netting agreements employed by CCPs.

(3) An MNA shall deemed to be legally enforceable and effective if it satisfies the conditions as specified in paragraph 87(2).

(ii) If the conditions in paragraph (i) above are met, the cash portion of variation margin received may be used to reduce the RC portion of the leverage ratio exposure measure, and the receivables assets from cash variation margin provided may be deducted from the leverage ratio exposure measure as follows:

(a) In the case of cash variation margin received, the receiving bank may reduce the RC (but not the add-on portion) of the exposure amount of the derivative asset by the amount of cash received if the positive mark-to-market value of the derivative contract(s) has not already been reduced by the same amount of cash variation margin received under the bank's operative Accounting Standards.

(b) In the case of cash variation margin provided to a counterparty, the posting bank may deduct the resulting receivable from its leverage ratio exposure measure, where the cash variation margin has been recognised as an asset under the bank's operative accounting framework.

Cash variation margin may not be used to reduce the PFE amount (including the calculation of the net-to-gross ratio (NGR) as defined in paragraph 267(3)).

(6) Treatment of clearing services

(i) Where a bank acting as a clearing member offers clearing services to clients, the clearing member's trade exposures to the central counterparty (CCP) that arise when the clearing member is obligated to reimburse the client for any losses suffered due to changes in the value of its transactions in the event that the CCP defaults, shall be captured by applying the same treatment that applies to any other type of derivatives transactions. However, if the clearing member, based on the contractual arrangements with the client, is not obligated to reimburse the client for any losses suffered due to changes in the value of its transactions in the event that a QCCP defaults, the clearing member need not recognise the resulting trade exposures to the QCCP in the leverage ratio exposure measure.

Explanation -

(1) For the purposes of this paragraph, 'trade exposures' includes initial margin irrespective of whether or not it is posted in a manner that makes it remote from the insolvency of the CCP.

(2) An affiliated entity to the bank acting as a clearing member shall be considered a client for the purpose of this paragraph, if it is outside the relevant scope of regulatory consolidation at the level at which the Basel III leverage ratio is applied. In contrast, if an affiliate entity falls within the regulatory scope of consolidation, the trade between the affiliate entity and the clearing member is eliminated in the course of consolidation, but the clearing member still has a trade exposure to

the QCCP, which shall be considered proprietary and the exemption in this paragraph shall not apply.

(ii) Where a client enters directly into a derivatives transaction with the CCP and the clearing member guarantees the performance of its clients' derivative trade exposures to the CCP, a bank acting as the clearing member for the client to the CCP shall calculate its related leverage ratio exposure resulting from the guarantee as a derivative exposure as set out in paragraphs 267(1) to 267(5), as if it had entered directly into the transaction with the client, including with regard to the receipt or provision of cash variation margin.

(7) Additional treatment for written credit derivatives:

(i) In addition to the CCR exposure arising from the fair value of the contracts, written credit derivatives create a notional credit exposure arising from the creditworthiness of the reference entity. Accordingly, written credit derivatives shall be treated in consistent with cash instruments (e.g., loans, bonds) for the purposes of the exposure measure.

(ii) To capture the credit exposure to the underlying reference entity, in addition to the above CCR treatment for derivatives and related collateral, the effective notional amount referenced by a written credit derivative shall be included in the exposure measure. The effective notional amount of a written credit derivative shall be reduced by any negative change in fair value amount that has been incorporated into the calculation of Tier 1 capital with respect to the written credit derivative. The resulting amount shall be further reduced by the effective notional amount of a purchased credit derivative on the same reference name provided:

(a) the credit protection purchased is on a reference obligation which ranks *pari passu* with or is junior to the underlying reference obligation of the written credit derivative in the case of single name credit derivatives;

(b) For tranched products if applicable, the purchased protection shall be on a reference obligation with the same level of seniority; and

(c) the remaining maturity of the credit protection purchased is equal to or greater than the remaining maturity of the written credit derivative.

Explanation –

(1) The effective notional amount is obtained by adjusting the notional amount to reflect the true exposure of contracts that are leveraged or otherwise enhanced by the structure of the transaction.

(2) A negative change in fair value is meant to refer to a negative fair value of a credit derivative that is recognised in Tier 1 capital. This treatment is consistent with the rationale that the effective notional amounts included in the exposure measure may be capped at the level of the maximum potential loss, which means the maximum potential loss at the reporting date is the notional amount of the credit derivative minus any negative fair value that has already reduced Tier 1 capital. For example, if a written credit derivative had a positive fair value of 20 on one date and has a negative fair value of 10 on a subsequent reporting date, the effective notional amount of the credit derivative may be reduced by 10. The effective notional amount cannot be reduced by 30. However, if at the subsequent reporting date, the credit derivative has a positive fair value of 5, the effective notional amount cannot be reduced at all.

(3) Two reference names shall be considered identical only if they refer to the same legal entity. For single-name credit derivatives, protection purchased that references a subordinated position may offset protection sold on a more senior position of the same reference entity as long as a credit event on the senior reference asset would result in a credit event on the subordinated reference asset.

(4) The effective notional amount of a written credit derivative shall be reduced by any negative change in fair value reflected in the bank's Tier 1 capital provided the effective notional amount of the offsetting purchased credit protection is also reduced by any resulting positive change in fair value reflected in Tier 1 capital.

(iii) Since written credit derivatives are included in the exposure measure at their effective notional amounts, and are also subject to add-on amounts for PFE, the exposure measure for written credit derivatives may be overstated. A bank may therefore choose to deduct the individual PFE add-on amount relating to a written credit derivative (which is not offset according to paragraph 267(7)(ii) and whose effective notional amount is included in the exposure measure) from their gross add-on in paragraphs 267(1) to 267(3). Accordingly, where effective bilateral netting contracts are in place, and when calculating $A_{Net} = 0.4 \cdot A_{Gross} + 0.6 \cdot NGR \cdot A_{Gross}$ (as per paragraphs 267(1) to 267(3), A_{Gross} may be reduced by the individual add-on amounts (i.e., notional multiplied by the appropriate add-on factors) which relate to written credit derivatives whose notional amounts are included in the leverage ratio exposure measure. However, no adjustments shall be made to NGR. Where effective bilateral netting contracts are not in place, the PFE add-on may be set to zero to avoid the double-counting described in this paragraph.

268. Securities Financing Transaction (SFT) exposures

(1) SFTs shall be included in the exposure measure according to the treatment described in the following paragraphs. The treatment recognises that secured lending and borrowing in the form of SFTs is an important source of leverage and ensures consistent international implementation by providing a common measure for dealing with the main differences in the operative accounting frameworks.

Note - SFTs are transactions such as repurchase agreements, reverse repurchase agreements, security lending and borrowing, and margin lending transactions, where the value of the transactions depends on market valuations and the transactions are often subject to margin agreements.

(2) General treatment (bank acting as principal):

The sum of the amounts in sub-paragraphs (i) and (ii) below shall be included in the leverage ratio exposure measure:

(i) Gross SFT assets recognised for accounting purposes (i.e., with no recognition of accounting netting), adjusted as follows:

(a) excluding from the exposure measure the value of any securities received under an SFT, where the bank has recognised the securities as an asset on its balance sheet. This may apply, for example, under accounting standards where securities received under an SFT may be recognised as assets if the recipient has the right to rehypothecate but has not done so; and

(b) cash payables and cash receivables in SFTs with the same counterparty may be measured net if all the following criteria are met:

(i) Transactions have the same explicit final settlement date;

(ii) The right to set off the amount owed to the counterparty with the amount owed by the counterparty is legally enforceable both currently in the normal course of business and in the event of: (a) default; (b) insolvency; and (c) bankruptcy; and

(iii) The counterparties intend to settle net, settle simultaneously, or the transactions are subject to a settlement mechanism that results in the functional equivalent of net settlement, that is, the cash flows of the transactions are equivalent, in effect, to a single net amount on the settlement date. To achieve such equivalence, both transactions are settled through the same settlement system and the settlement arrangements are supported by cash and / or intraday credit facilities intended to ensure that settlement of both transactions will occur by the end of the business day and the linkages to collateral flows do not result in the unwinding of net cash settlement. This condition ensures that any issues arising from the securities leg of the SFTs do not interfere with the completion of the net settlement of the cash receivables and payables.

Explanation - To achieve functional equivalence, all transactions shall be settled through the same settlement mechanism. The failure of any single securities transaction in the settlement mechanism should delay settlement of only the matching cash leg or create an obligation to the settlement mechanism,

supported by an associated credit facility. Further, if there is a failure of the securities leg of a transaction in such a mechanism at the end of the window for settlement in the settlement mechanism, then this transaction and its matching cash leg shall be split out from the netting set and treated gross for the purposes of the Basel III leverage ratio exposure measure. Specifically, the criteria in this paragraph are not intended to preclude a Delivery-versus-Payment (DVP) settlement mechanism or other type of settlement mechanism, provided that the settlement mechanism meets the functional requirements set out in this paragraph. For example, a settlement mechanism may meet these functional requirements if any failed transaction (that is, the securities that failed to transfer and the related cash receivable or payable) can be re-entered in the settlement mechanism until they are settled.

Note -

(a) For SFT assets subject to novation and cleared through QCCPs, 'gross SFT assets recognised for accounting purposes' are replaced by the final contractual exposure, given that pre-existing contracts have been replaced by new legal obligations through the novation process.

(b) 'Gross SFT assets recognised for accounting purposes' shall not recognise any accounting netting of cash payables against cash receivables (e.g., as currently permitted under the IFRS and US GAAP accounting frameworks). This regulatory treatment has the benefit of avoiding inconsistencies from netting which may arise across different accounting regimes.

(ii) A measure of CCR calculated as the current exposure without an add-on for PFE, calculated as follows:

(a) Where a qualifying MNA is in place, the current exposure (E*) is the greater of zero and the total fair value of securities and cash lent to a

counterparty for all transactions included in the qualifying MNA ($\sum E_i$), less the total fair value of cash and securities received from the counterparty for those transactions ($\sum C_i$). This is illustrated in the following formula:

$$E^* = \max \{0, [\sum E_i - \sum C_i]\}$$

(b) Where no qualifying MNA is in place, the current exposure for transactions with a counterparty shall be calculated on a transaction-by-transaction basis i.e., each transaction is treated as its own netting set, as shown in the following formula:

$$E_i^* = \max \{0, [E_i - C_i]\}$$

Explanation - A 'qualifying' MNA is one that meets the requirements under paragraph 87(1).

(3) Sale accounting transactions

Leverage may remain with the lender of the security in an SFT whether or not sale accounting is achieved under the operative accounting framework. As such, where sale accounting is achieved for an SFT under the bank's operative accounting framework, a bank shall reverse all sales-related accounting entries, and then calculate its exposure as if the SFT had been treated as a financing transaction under the operative accounting framework (i.e., the bank shall include the sum of amounts in sub-paragraphs (i) and (ii) of paragraph 268(2) for such an SFT) for the purposes of determining its exposure measure.

(4) Bank acting as agent

(i) A bank acting as an agent in an SFT generally provides an indemnity or guarantee to only one of the two parties involved, and only for the difference between the value of the security or cash its customer has lent and the value of collateral the borrower has provided. In this situation, the bank is exposed to the counterparty of its customer for the difference in values rather than to the full exposure to the underlying security or cash of the transaction (as is the case where the bank is one of the principals in the transaction). Where the bank does not own / control the underlying cash or security resource, that resource cannot be leveraged by the bank.

(ii) Where a bank acting as an agent in an SFT provides an indemnity or guarantee to a customer or counterparty for any difference between the value of the security or cash the customer has lent and the value of collateral the borrower has provided, the bank shall calculate its exposure measure by applying only subparagraph (ii) of paragraph 268(2). Where, in addition to the conditions in paragraph 268(4), a bank acting as an agent in an SFT does not provide an indemnity or guarantee to any of the involved parties, the bank is not exposed to the SFT and therefore need not recognise those SFTs in its exposure measure.

(iii) A bank acting as agent in an SFT and providing an indemnity or guarantee to a customer or counterparty shall be considered eligible for the exceptional treatment set out in paragraph 268(4)(ii) only if the bank's exposure to the transaction is limited to the guaranteed difference between the value of the security or cash its customer has lent and the value of the collateral the borrower has provided. In situations where the bank is further economically exposed (i.e., beyond the guarantee for the difference) to the underlying security or cash in the transaction, a further exposure equal to the full amount of the security or cash shall be included in the exposure measure. An example of situations where the bank is economically exposed to the underlying security or cash in the transaction is bank managing collateral received in the bank's name or on its own account rather than on the customer's or borrower's account (e.g., by on-lending or managing unsegregated collateral, cash or securities).

(iv) An illustrative example of exposure measure for SFT transactions is as under.

Illustrative balance sheet of banks								
Bank A					**Bank B**			
Liabilities		**Assets**			**Liabilities**		**Assets**	
Item	**Amount**	**Item**	**Amount**		**Item**	**Amount**	**Item**	**Amount**
		Cash	100				Cash	0
Capital	153	Securities	53		Capital	104	Securities	**104**
Total	153	Total	153		Total	104	Total	104

SFT transactions									
Reverse repo of bank A with bank B	**Bank A lends cash of 100 to bank B against security of 104**								
	Capital	153	Cash	0		Capital	104	Cash	100
			Securities	53				Securities	104
			Receivable SFT	100		Payable SFT	100		
	Total	**153**	**Total**	**153**		**Total**	**204**	**Total**	**204**

Repo of bank A with bank B	**Bank A borrows cash of 50 from bank B against security of 53**								
	Capital	153	Cash	50		Capital	104	Cash	50
			Securities	53				Securities	104
	Payable SFT	50	Receivable SFT	100		Payable SFT	100	Receivable SFT	50
	Total	**203**	**Total**	**203**		**Total**	**204**	**Total**	**204**

Leverage Ratio Exposure					
Item	**Bank A**			**Bank B**	
	Exposure where netting of SFT exposures is not permissible	Exposure where netting of SFT exposures is permissible		Exposure where netting of SFT exposures is not permissible	Exposure where netting of SFT exposures is permissible
On-balance sheet items	103	103		154	154
Gross SFT assets	100	100		50	50
Netted amount of Gross SFT assets	-	50*		-	0*
CCR exposure for SFT assets	3	0#		4	1#
Total SFT exposures	103	50		54	1
Total Exposures	206	153		208	155

*Max ((SFT receivable -SFT payable), 0)

#CCR exposure = Max ((total cash / securities receivable - total cash / securities payable), 0)

269. Off-Balance Sheet (OBS) items

(1) OBS items include commitments (including liquidity facilities), whether or not unconditionally cancellable, direct credit substitutes, acceptances, standby letters of credit, trade letters of credit, etc.

(2) In the risk-based capital framework, OBS items are converted under the standardised approach into credit exposure equivalents through the use of credit conversion factors (CCFs) (refer to paragraph 82 and 83). To determine the exposure amount of OBS items for the leverage ratio, the CCFs set out in the following paragraphs shall be applied to the notional amount. These correspond to the CCFs of the standardised approach for credit risk under paragraph 84(2) (including Table 15), subject to a floor of 10 per cent. The floor of 10 per cent shall affect commitments that are unconditionally cancellable at any time by the bank without prior notice, or that effectively provide for automatic cancellation due to deterioration in a borrower's creditworthiness. These may receive a zero per cent CCF under the risk-based capital framework. For any OBS item not specifically mentioned under paragraph 269(2), the applicable CCF for that item will be as indicated in paragraph 84(2).

(i) Commitments other than securitisation liquidity facilities with an original maturity up to one year and commitments with an original maturity over one year shall receive a CCF of 20 per cent and 50 per cent, respectively. However, any commitments that are unconditionally cancellable at any time by a bank without prior notice, or that effectively provide for automatic cancellation due to deterioration in a borrower's creditworthiness, shall receive a 10 per cent CCF.

(ii) Direct credit substitutes, e.g., general guarantees of indebtedness (including standby letters of credit serving as financial guarantees for loans and securities) and acceptances (including endorsements with the character of acceptances) shall receive a CCF of 100 per cent.

(iii) Forward asset purchases, forward deposits and partly paid shares and securities, which represent commitments with certain drawdown, shall receive a CCF of 100 per cent.

(iv) Certain transaction-related contingent items (e.g., performance bonds, bid bonds, warranties and standby letters of credit related to particular transactions) shall receive a CCF of 50 per cent.

(v) Note Issuance Facilities (NIFs) and Revolving Underwriting Facilities (RUFs) shall receive a CCF of 50 per cent.

(vi) For short-term self-liquidating trade letters of credit arising from the movement of goods (e.g., documentary credits collateralised by the underlying shipment), a 20 per cent CCF shall be applied to both an issuing and a confirming bank.

(vii) Where there is an undertaking to provide a commitment on an OBS item, a bank shall apply the lower of the two applicable CCFs.

(viii) All off-balance sheet securitisation exposures shall receive a CCF of 100 per cent conversion factor.

E Disclosure and reporting requirements

270. A bank shall follow following norms for disclosure and reporting of leverage ratio:

(1) A bank shall publicly disclose its Basel III leverage ratio both on a standalone and consolidated basis;

(2) To enable market participants to reconcile leverage ratio disclosures with a bank's published financial statements from period to period, and to compare the capital adequacy of the bank, it shall adopt a consistent and common disclosure of the main components of the leverage ratio, while also reconciling these disclosures with its published financial statements;

(3) To facilitate consistency and ease of use of disclosures relating to the composition of the leverage ratio, and to mitigate the risk of inconsistent formats undermining the objective of enhanced disclosure, a bank shall publish its leverage ratio according to a common set of templates;

(4) The public disclosure requirements include:

(i) a summary comparison table that provides a comparison of a bank's total accounting assets amounts and leverage ratio exposures;

(ii) a common disclosure template that provides a breakdown of the main leverage ratio regulatory elements;

(iii) a reconciliation requirement that details the source(s) of material differences between a bank's total balance sheet assets in its financial statements and on-balance sheet exposures in the common disclosure template; and

(iv) other disclosures as set out below;

(5) A bank shall also report its leverage ratio to the Reserve Bank (DoS) along with detailed calculations of capital and exposure measures on a quarterly basis; and

(6) Frequency and location of disclosure

(i) With the exception of the mandatory quarterly frequency requirement in paragraph (ii) below, detailed disclosures required according to paragraph 271 shall be made by a bank, irrespective of whether financial statements are audited, at least on a half yearly basis (i.e., as on September 30 and March 31 of a financial year), along with other Pillar 3 disclosures as required in terms of paragraph 246.

(ii) As the leverage ratio is an important supplementary measure to the risk-based capital requirements, the same Pillar 3 disclosure requirement shall also apply to the leverage ratio. Therefore, a bank, at a minimum, shall disclose the following three items on a quarterly basis, irrespective of whether financial statements are audited:

(a) Tier 1 capital (as per paragraph 264);

(b) Exposure measure (as per paragraph 265); and

(c) Leverage ratio (as per paragraph 262).

(iii) At a minimum, these disclosures shall be made on a quarter-end basis (i.e., as on June 30, September 30, December 31 and March 31 of a financial year), along with the figures of the prior three quarter-ends.

(iv) The location of leverage ratio disclosures shall be as stipulated for Pillar 3 disclosures in terms of paragraphs 246(4) and 247. However, specific to leverage ratio disclosures, a bank shall make available on its websites, an

ongoing archive of all reconciliation templates, disclosure templates and explanatory tables relating to prior reporting periods, instead of an archive for at least three years as required in case of Pillar 3 disclosures.

F Disclosure templates

271. The summary comparison table (Table: DF-17), common disclosure template (Table: DF-18) and explanatory table, qualitative reconciliation and other requirements are set out in Annex III: Pillar 3 disclosure requirements.

Chapter VIII

Repeal and Other provisions

Repeal and Saving

272. With the issue of these Directions, the existing Directions, instructions, and guidelines relating to Prudential Norms on Capital Adequacy as applicable to Commercial Banks stand repealed, as communicated vide circular DOR.RRC.REC.302/33-01-010/2025-26 dated November 28, 2025. The Directions, instructions and guidelines repealed prior to the issuance of these Directions shall continue to remain repealed.

273. Notwithstanding such repeal, any action taken or purported to have been taken, or initiated under the repealed Directions, instructions, or guidelines shall continue to be governed by the provisions thereof. All approvals or acknowledgments granted under these repealed lists shall be deemed as governed by these Directions. Further, the repeal of these directions, instructions, or guidelines shall not in any way prejudicially affect:

(i) any right, obligation or liability acquired, accrued, or incurred thereunder;

(ii) any, penalty, forfeiture, or punishment incurred in respect of any contravention committed thereunder; and

(iii) any investigation, legal proceeding, or remedy in respect of any such right, privilege, obligation, liability, penalty, forfeiture, or punishment as aforesaid; and any such investigation, legal proceedings or remedy may be instituted, continued, or enforced and any such penalty, forfeiture or punishment may be imposed as if those directions, instructions, or guidelines had not been repealed.

Application of other laws not barred

274. The provisions of these Directions shall be in addition to, and not in derogation of the provisions of any other laws, rules, regulations or directions, for the time being in force.

Interpretations

275. For giving effect to the provisions of these Directions or to remove any difficulties in the application or interpretation of the provisions of these Directions, the

Reserve Bank may, if it considers necessary, issue necessary clarifications in respect of any matter covered herein and the interpretation of any provision of these Directions given by the Reserve Bank shall be final and binding.

(Sunil T S Nair)
Chief General Manager

Annex I

Reporting format for details of investments by FIIs and NRIs in PNCPS qualifying as AT1 capital

(i) Name of the bank:

(ii) Total issue size / amount raised (in ₹ crore):

(iii) Date of issue:

	FIIs			NRIs	
Number of FIIs	Amount raised		Number of NRIs	Amount raised	
	(in ₹ crore)	As a percentage of the total issue size		(in ₹ crore)	As a percentage of the total issue size

(iv) It is certified that:

(a) the aggregate investment by all FIIs does not exceed 49 per cent of the issue size and investment by no individual FII exceeds 10 per cent of the issue size.

(b) It is certified that the aggregate investment by all NRIs does not exceed 24 per cent of the issue size and investment by no individual NRI exceeds 5 per cent of the issue size.

Authorised Signatory

Date

Seal of the bank

Annex II

Format for reporting of capital issuances

Issuer	
Issue size	
Instrument	
Deemed date of allotment	
Coupon	
Tenor	
Credit rating	
Put Option	
Call Option	
Redemption / maturity	
Whether private placement or otherwise	

Note -

(i) A bank may also email a soft copy of such details to capdor@rbi.org.in.

(ii) The reporting shall be duly certified by the compliance officer of the bank.

(iii) The compliance of the capital issuances with the applicable norms shall continue to be examined in course of the supervisory evaluation.

Annex III

Pillar 3 Disclosure requirements

1. Scope of application and capital adequacy

Table DF-1: Scope of application

Name of the head of the banking group to which the framework applies_____

Name of the entity / Country of incorporation	Whether the entity is included under accounting scope of consolidation (yes / no)	Explain the method of consolidation	Whether the entity is included under regulatory scope of consolidation[1] (yes / no)	Explain the method of consolidation	Explain the reasons for difference in the method of consolidation	Explain the reasons if consolidated under only one of the scopes of consolidation[2]

(i) Qualitative disclosures

(a) List of group entities considered for consolidation

(b) List of group entities not considered for consolidation both under the accounting and regulatory scope of consolidation

Name of the entity / country of incorporation	Principle activity of the entity	Total balance sheet equity (as stated in the accounting balance sheet of the legal entity)	% of bank's holding in the total equity	Regulatory treatment of bank's investments in the capital instruments of the entity	Total balance sheet assets (as stated in the accounting balance sheet of the legal entity)

(ii) Quantitative disclosures:

(a) List of group entities considered for consolidation

[1] If the entity is not consolidated in such a way as to result in its assets being included in the calculation of consolidated risk-weighted assets of the group, then such an entity is considered as outside the regulatory scope of consolidation.

[2] Also explain the treatment given i.e., deduction or risk weighting of investments under regulatory scope of consolidation.

Name of the entity / country of incorporation (as indicated in (i)a. above)	Principle activity of the entity	Total balance sheet equity (as stated in the accounting balance sheet of the legal entity)	Total balance sheet assets (as stated in the accounting balance sheet of the legal entity)

(b) The aggregate amount of capital deficiencies[3] in all subsidiaries which are not included in the regulatory scope of consolidation i.e., that are deducted

Name of the subsidiaries / country of incorporation	Principle activity of the entity	Total balance sheet equity (as stated in the accounting balance sheet of the legal entity)	% of bank's holding in the total equity	Capital deficiencies

(c) The aggregate amounts (e.g., current book value) of the bank's total interests in insurance entities, which are risk-weighted:

Name of the insurance entities / country of incorporation	Principle activity of the entity	Total balance sheet equity (as stated in the accounting balance sheet of the legal entity)	% of bank's holding in the total equity / proportion of voting power	Quantitative impact on regulatory capital of using risk weighting method versus using the full deduction method

(d) Any restrictions or impediments on transfer of funds or regulatory capital within the banking group

[3]A capital deficiency is the amount by which actual capital is less than the regulatory capital requirement. Any deficiencies which have been deducted on a group level in addition to the investment in such subsidiaries are not to be included in the aggregate capital deficiency.

Table DF-2: Capital Adequacy

Qualitative disclosures
(a) A summary discussion of the bank's approach to assessing the adequacy of its capital to support current and future activities
Quantitative disclosures
(b) Capital requirements for credit risk: (i) Portfolios subject to standardised approach (ii) Securitisation exposures
(c) Capital requirements for market risk: Standardised duration approach (i) Interest rate risk (ii) Foreign exchange risk (including gold) (iii) Equity risk
(d) Capital requirements for operational risk: Basic Indicator Approach
(e) CET1, Tier 1, and total capital ratios: (i) For the top consolidated group; and (ii) For significant bank subsidiaries (stand alone or sub-consolidated depending on how the Framework is applied).

2. Risk exposure and assessment

The risks to which a bank is exposed and the techniques that the bank uses to identify, measure, monitor and control those risks are important factors market participants consider in their assessment of an institution. In this section, several key banking risks are considered: credit risk, market risk, and interest rate risk in the banking book and operational risk. Also included in this section are disclosures relating to credit risk mitigation and asset securitisation, both of which alter the risk profile of the institution. Where applicable, separate disclosures are set out for a bank using different approaches to the assessment of regulatory capital.

General qualitative disclosure requirement

For each separate risk area (e.g., credit, market, operational, banking book interest rate risk) a bank shall describe its risk management objectives and policies, including:

(i) strategies and processes;

(ii) the structure and organisation of the relevant risk management function;

(iii) the scope and nature of risk reporting and / or measurement systems; and

(iv) policies for hedging and / or mitigating risk and strategies and processes for monitoring the continuing effectiveness of hedges / mitigants.

Credit risk

General disclosures of credit risk provide market participants with a range of information about overall credit exposure and need not necessarily be based on information prepared for regulatory purposes. Disclosures on the capital assessment techniques give information on the specific nature of the exposures, the means of capital assessment and data to assess the reliability of the information disclosed.

Table DF-3: Credit risk: general disclosures for all banks

Qualitative Disclosures
(a) The general qualitative disclosure requirement with respect to credit risk, including:
(i) Definitions of past due and impaired (for accounting purposes);
(ii) Discussion of the bank's credit risk management policy.
Quantitative Disclosures
(b) Total gross credit risk exposures[4], Fund based, and Non-fund based separately.
(c) Geographic distribution of exposures[5], Fund based, and Non-fund based separately
(i) Overseas
(ii) Domestic
(d) Industry[6] type distribution of exposures, fund based and non-fund based separately
(e) Residual contractual maturity breakdown of assets[7]
(f) Amount of NPAs (Gross)
(i) Substandard
(ii) Doubtful 1
(iii) Doubtful 2
(iv) Doubtful 3
(v) Loss

4 That is after accounting offsets in accordance with the applicable accounting regime and without taking into account the effects of credit risk mitigation techniques, e.g., collateral and netting.

5 That is, on the same basis as adopted for Segment Reporting adopted for compliance with AS 17.

6 The industries break-up may be provided on the same lines as prescribed for DSB returns. If the exposure to any particular industry is more than 5 per cent of the gross credit exposure as computed under (b) above it should be disclosed separately.

7 A bank shall use the same maturity bands as used for reporting positions in the ALM returns.

(g) Net NPAs

(h) NPA Ratios

  (i) Gross NPAs to gross advances

  (ii) Net NPAs to net advances

(i) Movement of NPAs (Gross)

  (i) Opening balance

  (ii) Additions

  (iii) Reductions

  (iv) Closing balance

(j) Movement of provisions (Separate disclosure shall be made for specific provisions and general provisions held by the bank with a description of each type of provisions held)

  (i) Opening balance

  (ii) Provisions made during the period

  (iii) Write-off

  (iv) Write-back of excess provisions

  (v) Any other adjustments, including transfers between provisions

  (vi) Closing balance

In addition, write-offs and recoveries that have been booked directly to the income statement should be disclosed separately.

(k) Amount of Non-Performing Investments

(l) Amount of provisions held for non-performing investments

(m) Movement of provisions for depreciation on investments

  (i) Opening balance

  (ii) Provisions made during the period

  (iii) Write-off

  (iv) Write-back of excess provisions

  (v) Closing balance

(n) By major industry or counterparty type:

  (i) Amount of NPAs and if available, past due loans, provided separately;

  (ii) Specific and general provisions; and

  (iii) Specific provisions and write-offs during the current period.

In addition, a bank is encouraged also to provide an analysis of the ageing of past-due loans.

(o) Amount of NPAs and, if available, past due loans provided separately broken down by significant geographic areas including, if practical, the amounts of specific and general provisions related to each geographical area. The portion of general provisions that is not allocated to a geographical area should be disclosed separately.

Table DF-4 - Credit risk: disclosures for portfolios subject to the standardised approach

Qualitative disclosures (a) For portfolios under the standardised approach: (i) Names of credit rating agencies used, plus reasons for any changes; (ii) Types of exposure for which each agency is used; and (iii) A description of the process used to transfer public issue ratings onto comparable assets in the banking book.
Quantitative disclosures (b) For exposure[8] amounts after risk mitigation subject to the standardised approach, amount of a bank's outstanding (rated and unrated) in the following three major risk buckets as well as those that are deducted: (i) Below 100% risk weight (ii) 100% risk weight (iii) More than 100% risk weight (iv) Deducted

Table DF-5: Credit risk mitigation: disclosures for standardised approaches[9]

Qualitative Disclosures (a) The general qualitative disclosure requirement with respect to credit risk mitigation including: Policies and processes for, and an indication of the extent to which the bank makes use of, on- and off-balance sheet netting; • policies and processes for collateral valuation and management; • a description of the main types of collateral taken by the bank; • the main types of guarantor counterparty and their credit worthiness; and • information about (market or credit) risk concentrations within the mitigation taken.
Quantitative Disclosures (b) For each separately disclosed credit risk portfolio the total exposure (after, where applicable, on- or off-balance sheet netting) that is covered by eligible financial collateral after the application of haircuts.

[8] As defined for disclosures in Table DF-3.

[9] At a minimum, a bank shall give the disclosures in this Table in relation to credit risk mitigation that has been recognised for the purposes of reducing capital requirements under this Framework. Where relevant, a bank is encouraged to give further information about mitigants that have not been recognised for that purpose.

(c)	For each separately disclosed portfolio the total exposure (after, where applicable, on- or off-balance sheet netting) that is covered by guarantees / credit derivatives (whenever specifically permitted by the Reserve Bank).

Table DF-6: Securitisation exposures: disclosure for standardised approach

Qualitative disclosures	
(a)	The general qualitative disclosure requirement with respect to securitisation including a discussion of: (i) the bank's objectives in relation to securitisation activity, including the extent to which these activities transfer credit risk of the underlying securitised exposures away from the bank to other entities; (ii) the nature of other risks (e.g., liquidity risk) inherent in securitised assets; (iii) the various roles played by the bank in the securitisation process (For example: originator, investor, servicer, provider of credit enhancement, liquidity provider, swap provider@, protection provider#) and an indication of the extent of the bank's involvement in each of them; (iv) a description of the processes in place to monitor changes in the credit and market risk of securitisation exposures (for example, how the behaviour of the underlying assets impacts securitisation exposures); (v) a description of the bank's policy governing the use of credit risk mitigation to mitigate the risks retained through securitisation exposures. @ A bank may have provided support to a securitisation structure in the form of an interest rate swap or currency swap to mitigate the interest rate / currency risk of the underlying assets, if permitted as per regulatory rules. # A bank may provide credit protection to a securitisation transaction through guarantees, credit derivatives or any other similar product, if permitted as per regulatory rules.
(b)	**Summary of the bank's accounting policies for securitisation activities, including**: (i) whether the transactions are treated as sales or financings; (ii) methods and key assumptions (including inputs) applied in valuing positions retained or purchased; (iii) changes in methods and key assumptions from the previous period and impact of the changes; (iv) policies for recognising liabilities on the balance sheet for arrangements that could require the bank to provide financial support for securitised assets.
(c)	In the banking book, the names of ECAIs used for securitisations and the types of securitisation exposure for which each agency is used.
Quantitative disclosures: Banking Book	
(d)	The total amount of exposures securitised by the bank.
(e)	For exposures securitised losses recognised by the bank during the current period broken by the exposure type (e.g., Credit cards, housing loans, auto loans etc. detailed by underlying security).
(f)	Amount of assets intended to be securitised within a year.
(g)	Of (f), amount of assets originated within a year before securitisation.

(h)	The total amount of exposures securitised (by exposure type) and unrecognised gain or losses on sale by exposure type.
(i)	Aggregate amount of: (i) on-balance sheet securitisation exposures retained or purchased broken down by exposure type; and (ii) off-balance sheet securitisation exposures broken down by exposure type.
(j)	(i) Aggregate amount of securitisation exposures retained or purchased and the associated capital charges, broken down between exposures and further broken down into different risk weight bands for each regulatory capital approach. (ii) Exposures that have been deducted entirely from Tier 1 capital, credit enhancing I / Os deducted from total capital, and other exposures deducted from total capital (by exposure type).
Quantitative disclosures: Trading book	
(k)	Aggregate amount of exposures securitised by the bank for which the bank has retained some exposures and which is subject to the market risk approach, by exposure type.
(l)	Aggregate amount of: (i) on-balance sheet securitisation exposures retained or purchased broken down by exposure type; and (ii) off-balance sheet securitisation exposures broken down by exposure type.
(m)	**Aggregate amount of securitisation exposures retained or purchased separately for**: (i) securitisation exposures retained or purchased subject to Comprehensive Risk Measure for specific risk; and (ii) securitisation exposures subject to the securitisation framework for specific risk broken down into different risk weight bands.
(n)	Aggregate amount of: (i) the capital requirements for the securitisation exposures, subject to the securitisation framework broken down into different risk weight bands. (ii) securitisation exposures that are deducted entirely from Tier 1 capital, credit enhancing I / Os deducted from total capital, and other exposures deducted from total capital (by exposure type).

Table DF-7: Market risk in trading book

(a) Qualitative disclosures The general qualitative disclosure requirement for market risk including the portfolios covered by the standardised approach.
Quantitative disclosures (b) The capital requirements for: • interest rate risk; • equity position risk; and • foreign exchange risk.

Table DF-8: Operational risk

Qualitative disclosures: The general qualitative disclosure requirement for operational risk.

Table DF-9: Interest rate risk in the banking book (IRRBB)

Qualitative Disclosures (a) The general qualitative disclosure requirement including the nature of IRRBB and key assumptions, including assumptions regarding loan prepayments and behaviour of non-maturity deposits, and frequency of IRRBB measurement.
Quantitative Disclosures (b) The increase (decline) in earnings and economic value (or relevant measure used by management) for upward and downward rate shocks according to management's method for measuring IRRBB, broken down by currency (where the turnover is more than 5% of the total turnover).

Table DF-10: General disclosure for exposures related to counterparty credit risk

Qualitative Disclosures	(a)	The general qualitative disclosure requirement with respect to derivatives and CCR, including: (i) Discussion of methodology used to assign economic capital and credit limits for counterparty credit exposures; (ii) Discussion of policies for securing collateral and establishing credit reserves; (iii) Discussion of policies with respect to wrong-way risk exposures; and (iv) Discussion of the impact of the amount of collateral the bank would have to provide given a credit rating downgrade.
Quantitative Disclosures	(b)	Gross positive fair value of contracts, netting benefits, netted current credit exposure, collateral held (including type, e.g., cash, government securities, etc.), and net derivatives credit exposure[10]. Also report measures for exposure at default, or exposure amount, under CEM. The notional value of credit derivative hedges, and the distribution of current credit exposure by types of credit exposure[11].
	(c)	Credit derivative transactions that create exposures to CCR (notional value), segregated between use for the institution's own credit portfolio, as well as in its intermediation activities, including the distribution of the credit

[10] Net credit exposure is the credit exposure on derivatives transactions after considering both the benefits from legally enforceable netting agreements and collateral arrangements. The notional amount of credit derivative hedges alerts market participants to an additional source of credit risk mitigation.

[11] For example, interest rate contracts, FX contracts, credit derivatives, and other contracts.

		derivatives products used[12], broken down further by protection bought and sold within each product group.

3. Composition of capital disclosure templates

(1) Disclosure template

(i) The template is designed to capture the capital positions of a bank.

(ii) The reconciliation requirement in terms of paragraph 248(2)(ii) results in the decomposition of certain regulatory adjustments. For example, the disclosure template below includes the adjustment of 'Goodwill net of related tax liability'. The requirements will lead to the disclosure of both the goodwill component and the related tax liability component of this regulatory adjustment.

(iii) Certain rows of the template are shaded as explained below:

(a) each dark grey row introduces a new section detailing a certain component of regulatory capital;

(b) the light grey rows with no thick border represent the sum cells in the relevant section; and

(c) the light grey rows with a thick border show the main components of regulatory capital and the capital ratios.

Also provided along with the Table, an explanation of each line of the template, with references to the appropriate paragraphs of these Directions.

Table DF-11: Composition of capital

(₹ in crore)

Basel III common disclosure template			
Common Equity Tier 1 capital: instruments and reserves			Ref No
1	Directly issued qualifying common share capital plus related stock surplus (share premium)		
2	Retained earnings		
3	Accumulated other comprehensive income (and other reserves)		
3a	Revaluation Reserves		
4	Directly issued capital subject to phase out from CET1 (only applicable to non-joint stock companies[13])		

[12] For example, credit default swaps.

[13] Not Applicable to commercial banks in India.

Basel III common disclosure template			
Common Equity Tier 1 capital: instruments and reserves			Ref No
5	Common share capital issued by subsidiaries and held by third parties (amount allowed in group CET1)		
6	**Common Equity Tier 1 capital before regulatory adjustments**		
Common Equity Tier 1 capital: regulatory adjustments			
7	Prudential valuation adjustments		
8	Goodwill (net of related tax liability)		
9	Intangibles (net of related tax liability)		
10	Deferred tax assets[14]		
11	Cash-flow hedge reserve		
12	Shortfall of provisions to expected losses		
13	Securitisation gain on sale		
14	Gains and losses due to changes in own credit risk on fair valued liabilities		
15	Defined-benefit pension fund net assets		
16	Investments in own shares (if not already netted off paid-up capital on reported balance sheet)		
17	Reciprocal cross-holdings in common equity		
18	Investments in the capital of banking, financial, and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued share capital (amount above 10% threshold)		
19	Significant investments in the common stock of banking, financial, and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions (amount above 10% threshold)[15]		
20	Mortgage servicing rights[16] (amount above 10% threshold)		
21	Deferred tax assets arising from temporary differences[17] (amount above 10% threshold, net of related tax liability)		
22	Amount exceeding the 15% threshold		
23	of which: significant investments in the common stock of financial entities		
24	of which: mortgage servicing rights		

[14]In terms of Basel III rules text issued by the Basel Committee (December 2010), DTAs that rely on future profitability of the bank to be realized are to be deducted. DTAs which relate to temporary differences are to be treated under the 'threshold deductions' as set out in paragraph 28.

[15]Only significant investments other than in the insurance and non-financial subsidiaries should be reported here. The insurance and non-financial subsidiaries are not consolidated for the purpose of capital adequacy. The equity and other regulatory capital investments in insurance subsidiaries are fully deducted from consolidated regulatory capital of the banking group. However, in terms of Basel III rules text of the Basel Committee, insurance subsidiaries are included under significant investments and thus, deducted based on 10% threshold rule instead of full deduction.

[16]Not applicable in Indian context.

[17]Please refer to Footnote 14 above.

Basel III common disclosure template			
Common Equity Tier 1 capital: instruments and reserves			Ref No
25	of which: deferred tax assets arising from temporary differences		
26	National specific regulatory adjustments[18] (26a+26b+26c+26d+26e+26f+26g)		
26a	of which: Investments in the equity capital of unconsolidated insurance subsidiaries		
26b	of which: Investments in the equity capital of unconsolidated non-financial subsidiaries[19]		
26c	of which: Shortfall in the equity capital of majority owned financial entities which have not been consolidated with the bank[20]		
26d	of which: Unrealised profits arising because of transfer of loans		
26e	of which: deductions applicable on account of SRs guaranteed by the Government of India		
26f	of which: Intra-group exposures beyond permissible limits		
26g	of which: net unrealised gains arising on fair valuation of Level 3 financial instruments (including derivatives)		
26h	of which: contribution in the form of subordinated units of an AIF scheme		
26i	of which: full amount of the Default Loss Guarantee (DLG), if the bank is the DLG provider		
27	Regulatory adjustments applied to Common Equity Tier 1 due to insufficient Additional Tier 1 and Tier 2 to cover deductions		
28	**Total regulatory adjustments to Common equity Tier 1**		
29	**Common Equity Tier 1 capital (CET1)**		
Additional Tier 1 capital: instruments			
30	Directly issued qualifying Additional Tier 1 instruments plus related stock surplus (share premium) (31+32)		
31	of which: classified as equity under applicable accounting standards (Perpetual Non-Cumulative Preference Shares)		
32	of which: classified as liabilities under applicable accounting standards (Perpetual debt Instruments)		
33	Directly issued capital instruments subject to phase out from Additional Tier 1		
34	Additional Tier 1 instruments (and CET1 instruments not included in row 5) issued by subsidiaries and held by third parties (amount allowed in group AT1)		
35	of which: instruments issued by subsidiaries subject to phase out		
36	**Additional Tier 1 capital before regulatory adjustments**		

[18]Adjustments which are not specific to the Basel III regulatory adjustments (as prescribed by the Basel Committee) will be reported under this row. However, regulatory adjustments which are linked to Basel III i.e., where there is a change in the definition of the Basel III regulatory adjustments, the impact of these changes will be explained in the Notes of this disclosure template.

[19]Non-financial subsidiaries are not consolidated for the purpose of capital adequacy. The equity and other regulatory capital investments in the non-financial subsidiaries are deducted from consolidated regulatory capital of the group. These investments are not required to be deducted fully from capital under Basel III rules text of the Basel Committee.

[20]Please refer to paragraph 8(4).Please also refer to the Paragraph 34 of the Basel II Framework issued by the Basel Committee (June 2006). Though this is not national specific adjustment, it is reported here.

Basel III common disclosure template			
Common Equity Tier 1 capital: instruments and reserves			Ref No
Additional Tier 1 capital: regulatory adjustments			
37	Investments in own Additional Tier 1 instruments		
38	Reciprocal cross-holdings in Additional Tier 1 instruments		
39	Investments in the capital of banking, financial, and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued common share capital of the entity (amount above 10% threshold)		
40	Significant investments in the capital of banking, financial, and insurance entities that are outside the scope of regulatory consolidation (net of eligible short positions)[21]		
41	National specific regulatory adjustments (41a+41b)		
41a	of which: Investments in the Additional Tier 1 capital of unconsolidated insurance subsidiaries		
41b	of which: Shortfall in the Additional Tier 1 capital of majority owned financial entities which have not been consolidated with the bank		
42	Regulatory adjustments applied to Additional Tier 1 due to insufficient Tier 2 to cover deductions		
43	**Total regulatory adjustments to Additional Tier 1 capital**		
44	**Additional Tier 1 capital (AT1)**		
45	**Tier 1 capital (T1 = CET1 + AT1) (29 + 44)**		
Tier 2 capital: instruments and provisions			
46	Directly issued qualifying Tier 2 instruments plus related stock surplus		
47	Directly issued capital instruments subject to phase out from Tier 2		
48	Tier 2 instruments (and CET1 and AT1 instruments not included in rows 5 or 34) issued by subsidiaries and held by third parties (amount allowed in group Tier 2)		
49	of which: instruments issued by subsidiaries subject to phase out		
50	Provisions[22]		
51	**Tier 2 capital before regulatory adjustments**		
Tier 2 capital: regulatory adjustments			
52	Investments in own Tier 2 instruments		
53	Reciprocal cross-holdings in Tier 2 instruments		
54	Investments in the capital of banking, financial, and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued common share capital of the entity (amount above the 10% threshold)		
55	Significant investments[23] in the capital banking, financial, and insurance entities that are outside the scope of regulatory consolidation (net of eligible short positions)		

[21]Please refer to footnote 15 above.

[22]Eligible provisions and revaluation reserves in terms of paragraph 21 and 12 of these Directions, both to be reported and break-up of these two items to be furnished in Notes.

[23]Please refer to footnote 15 above.

Basel III common disclosure template			
Common Equity Tier 1 capital: instruments and reserves			Ref No
56	National specific regulatory adjustments (56a+56b)		
56a	of which: Investments in the Tier 2 capital of unconsolidated insurance subsidiaries		
56b	of which: Shortfall in the Tier 2 capital of majority owned financial entities which have not been consolidated with the bank		
57	**Total regulatory adjustments to Tier 2 capital**		
58	**Tier 2 capital (T2)**		
59	**Total capital (TC = T1 + T2) (45 + 58)**		
60	**Total risk weighted assets (60a + 60b + 60c)**		
60a	of which: total credit risk weighted assets		
60b	of which: total market risk weighted assets		
60c	of which: total operational risk weighted assets		
Capital ratios and buffers			
61	Common Equity Tier 1 (as a percentage of risk weighted assets)		
62	Tier 1 (as a percentage of risk weighted assets)		
63	Total capital (as a percentage of risk weighted assets)		
64	Institution specific buffer requirement (minimum CET1 requirement plus capital conservation plus countercyclical buffer requirements plus higher of G-SIB buffer requirement and D-SIB buffer requirement, expressed as a percentage of risk weighted assets)		
65	of which: capital conservation buffer requirement		
66	of which: bank specific countercyclical buffer requirement		
67	of which: higher of G-SIB and D-SIB buffer requirement		
68	Common Equity Tier 1 available to meet buffers (as a percentage of risk weighted assets)		
National minima (if different from Basel III)			
69	National Common Equity Tier 1 minimum ratio (if different from Basel III minimum)		
70	National Tier 1 minimum ratio (if different from Basel III minimum)		
71	National total capital minimum ratio (if different from Basel III minimum)		
Amounts below the thresholds for deduction (before risk weighting)			
72	Non-significant investments in the capital of other financial entities		
73	Significant investments in the common stock of financial entities		
74	Mortgage servicing rights (net of related tax liability)		
75	Deferred tax assets arising from temporary differences (net of related tax liability)		
Applicable caps on the inclusion of provisions in Tier 2			
76	Provisions eligible for inclusion in Tier 2 in respect of exposures subject to standardised approach (prior to application of cap)		
77	Cap on inclusion of provisions in Tier 2 under standardised approach		
78	Provisions eligible for inclusion in Tier 2 in respect of exposures subject to internal ratings-based approach (prior to application of cap)		
79	Cap for inclusion of provisions in Tier 2 under internal ratings-based approach		

Notes to the template

Row No. of the template	Particular	(₹ in crore)
10	Deferred tax assets associated with accumulated losses	
	Deferred tax assets (excluding those associated with accumulated losses) net of Deferred tax liability	
	Total as indicated in row 10	
19	If investments in insurance subsidiaries are not deducted fully from capital and instead considered under 10% threshold for deduction, the resultant increase in the capital of bank	
	of which: Increase in Common Equity Tier 1 capital	
	of which: Increase in Additional Tier 1 capital	
	of which: Increase in Tier 2 capital	
26b	If investments in the equity capital of unconsolidated non-financial subsidiaries are not deducted and hence, risk weighted then:	
	(i) Increase in Common Equity Tier 1 capital	
	(ii) Increase in risk weighted assets	
50	Eligible Provisions included in Tier 2 capital	
	Eligible Revaluation Reserves included in Tier 2 capital	
	Total of row 50	

Explanation of each row of the Common Disclosure Template	
Row No.	**Explanation**
1	Instruments issued by the parent bank of the reporting banking group which meet all of the CET1 entry criteria set out in paragraphs 12 and 14 (read with paragraphs 13 and 15). This should be equal to the sum of common shares (and related surplus only) which must meet the common shares criteria. This should be net of treasury stock and other investments in own shares to the extent that these are already derecognised on the balance sheet under the relevant accounting standards. Other paid-up capital elements must be excluded. All minority interest must be excluded.
2	Retained earnings, prior to all regulatory adjustments in accordance with paragraph 12.
3	Accumulated other comprehensive income and other disclosed reserves, prior to all regulatory adjustments.
3a	Revaluation Reserves in accordance with paragraph 12 (vi).
4	A bank shall report zero in this row.
5	Common share capital issued by subsidiaries and held by third parties. Only the amount that is eligible for inclusion in group CET1 should be reported here, as determined by the application of paragraph 27(2) (Also see illustration given in paragraph 27(5)).
6	Sum of rows 1 to 5.
7	Valuation adjustments according to the requirements of paragraph 213.
8	Goodwill net of related tax liability, as set out in paragraph 28(1).
9	Intangibles (net of related tax liability), as set out in paragraph 28(1)
10	Deferred tax assets (net of related tax liability), as set out in paragraph 28(2).

Explanation of each row of the Common Disclosure Template	
Row No.	**Explanation**
11	The element of the cash-flow hedge reserve described in paragraph 28(3).
12	Shortfall of provisions to expected losses.
13	Securitisation gain on sale as described in paragraph 28(4).
14	Gains and losses due to changes in own credit risk on fair valued liabilities as described in paragraph 28(5).
15	Defined benefit pension fund net assets, the amount to be deducted, as set out in paragraph 28(6).
16	Investments in own shares (if not already netted off paid-in capital on reported balance sheet), as set out in paragraph 28(7).
17	Reciprocal cross-holdings in common equity as set out in paragraph 28(8)(ii)(a).
18	Investments in the capital of banking, financial, and insurance entities that are outside the scope of regulatory consolidation where the bank does not own more than 10% of the issued share capital (amount above 10% threshold), amount to be deducted from CET1 in accordance with paragraph 28(8)(ii)(b).
19	Significant investments in the common stock of banking, financial, and insurance entities that are outside the scope of regulatory consolidation (amount above 10% threshold), amount to be deducted from CET1 in accordance with paragraph 28(8)(ii)(c).
20	Not relevant.
21	DTAs arising due to timing differences as per paragraph 28(2).
22	15% threshold as per paragraph 28(2)(iii).
23	Significant investments in the capital of financial entities as per paragraph 28(8)(ii)(c).
24	Not relevant.
25	DTAs arising due to timing differences as per paragraph 28(2).
26	Any national specific regulatory adjustments that are required by national authorities to be applied to CET1 in addition to the Basel III minimum set of adjustments [i.e., in terms of December 2010 (rev June 2011) document issued by the Basel Committee on Banking Supervision].
26d	Unrealised profits arising because of transfer of loans as described in paragraph 28(4).
26e	Deductions applicable on account of SRs guaranteed by the Government of India as described in paragraph 28(4).
26f	Intra-group exposures beyond permissible limits as described in paragraph 28(11).
26g	Net unrealised gains arising on fair valuation of Level 3 financial instruments (including derivatives) as described in paragraph 28(12).
26h	Contribution in the form of subordinated units of an AIF scheme as described in paragraph 28(13).
26i	Full amount of the Default Loss Guarantee (DLG), if the bank is the DLG provider as described in paragraph 28 (14).

Explanation of each row of the Common Disclosure Template	
Row No.	**Explanation**
27	Regulatory adjustments applied to Common Equity Tier 1 due to insufficient Additional Tier 1 to cover deductions. If the amount reported in row 43 exceeds the amount reported in row 36 the excess is to be reported here.
28	Total regulatory adjustments to Common equity Tier 1, to be calculated as the sum of rows 7 to 22 plus row 26 and 27.
29	Common Equity Tier 1 capital (CET1), to be calculated as row 6 minus row 28.
30	Instruments that meet all of the AT1 entry criteria set out in paragraph 16. All instruments issued of subsidiaries of the consolidated group should be excluded from this row.
31	The amount in row 30 classified as equity under applicable accounting standards.
32	The amount in row 30 classified as liabilities under applicable accounting standards.
33	Directly issued capital instruments subject to phase out from Additional Tier 1.
34	Additional Tier 1 instruments (and CET1 instruments not included in row 5) issued by subsidiaries and held by third parties, the amount allowed in group AT1 in accordance with paragraph 27(3) (please see paragraph 27(5) illustration).
35	The amount reported in row 34 that relates to instruments subject to phase out from AT1.
36	The sum of rows 30, 33, and 34.
37	Investments in own Additional Tier 1 instruments, amount to be deducted from AT1 in accordance with paragraph 28(7).
38	Reciprocal cross-holdings in Additional Tier 1 instruments, amount to be deducted from AT1 in accordance with paragraph 28(8)(ii)(a).
39	Investments in the capital of banking, financial, and insurance entities that are outside the scope of regulatory consolidation where the bank does not own more than 10% of the issued common share capital of the entity (net of eligible short positions), amount to be deducted from AT1 in accordance with paragraph 28(8)(ii)(b).
40	Significant investments in the capital of banking, financial, and insurance entities that are outside the scope of regulatory consolidation (net of eligible short positions), amount to be deducted from AT1 in accordance with paragraph 28(8)(ii)(c).
41	Any national specific regulatory adjustments that are required by national authorities to be applied to Additional Tier 1 in addition to the Basel III minimum set of adjustments [i.e., in terms of December 2010 (rev June 2011) document issued by the Basel Committee on Banking Supervision.
42	Regulatory adjustments applied to Additional Tier 1 due to insufficient Tier 2 to cover deductions. If the amount reported in row 57 exceeds the amount reported in row 51 the excess is to be reported here.
43	The sum of rows 37 to 42.
44	Additional Tier 1 capital, to be calculated as row 36 minus row 43.
45	Tier 1 capital, to be calculated as row 29 plus row 44.

Explanation of each row of the Common Disclosure Template	
Row No.	**Explanation**
46	Instruments that meet all of the Tier 2 entry criteria set out in paragraph 21. All instruments issued of subsidiaries of the consolidated group should be excluded from this row. Provisions and Revaluation Reserves should not be included in Tier 2 in this row.
47	Directly issued capital instruments subject to phase out from Tier 2.
48	Tier 2 instruments (and CET1 and AT1 instruments not included in rows 5 or 32) issued by subsidiaries and held by third parties (amount allowed in group Tier 2) in accordance with paragraph 27(4).
49	The amount reported in row 48 that relates to instruments subject to phase out from Tier 2
50	Provisions and Revaluation Reserves included in Tier 2 calculated in accordance with paragraph 21.
51	The sum of rows 46 to 48 and row 50.
52	Investments in own Tier 2 instruments, amount to be deducted from Tier 2 in accordance with paragraph 28(7).
53	Reciprocal cross-holdings in Tier 2 instruments, amount to be deducted from Tier 2 in accordance with paragraph 28(8)(ii)(a).
54	Investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation where the bank does not own more than 10% of the issued common share capital of the entity (net of eligible short positions), amount to be deducted from Tier 2 in accordance with paragraph 28(8)(ii)(b).
55	Significant investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation (net of eligible short positions), amount to be deducted from Tier 2 in accordance with paragraph 28(8)(ii)(c).
56	Any national specific regulatory adjustments that are required by national authorities to be applied to Tier 2 in addition to the Basel III minimum set of adjustments [i.e., in terms of December 2010 (rev June 2011) document issued by the Basel Committee on Banking Supervision].
57	The sum of rows 52 to 56.
58	Tier 2 capital, to be calculated as row 51 minus row 57.
59	Total capital, to be calculated as row 45 plus row 58.
60	Total risk weighted assets of the reporting group. Details to be furnished under rows 60a, 60b and 60c.
61	Common Equity Tier 1 ratio (as a percentage of risk weighted assets), to be calculated as row 29 divided by row 60 (expressed as a percentage).
62	Tier 1 ratio (as a percentage of risk weighted assets), to be calculated as row 45 divided by row 60 (expressed as a percentage).
63	Total capital ratio (as a percentage of risk weighted assets), to be calculated as row 59 divided by row 60 (expressed as a percentage).
64	Institution specific buffer requirement (minimum CET1 requirement plus capital conservation buffer plus countercyclical buffer requirements plus higher of G-SIB buffer requirement and D-SIB buffer requirement, expressed as a percentage of risk weighted

Explanation of each row of the Common Disclosure Template	
Row No.	**Explanation**
	assets). To be calculated as 5.5% plus 2.5% capital conservation buffer plus the bank specific countercyclical buffer requirement whenever activated plus the higher of bank D-SIB requirement (where applicable) and the bank G-SIB requirement (where applicable) as set out in *Global systemically important banks: assessment methodology and the additional loss absorbency requirement: Rules text (November 2011) issued by the Basel Committee*. This row will show the CET1 ratio below which the bank will become subject to constraints on distributions.
65	The amount in row 64 (expressed as a percentage of risk weighed assets) that relates to the capital conservation buffer), i.e., a bank shall report 2.5% here.
66	The amount in row 64 (expressed as a percentage of risk weighed assets) that relates to the bank specific countercyclical buffer requirement.
67	The amount in row 64 (expressed as a percentage of risk weighed assets) that relates to the higher of the bank's D-SIB requirement and G-SIB requirement.
68	Common Equity Tier 1 (as a percentage of risk-weighted assets) available to meet the buffers after meeting the bank's minimum capital requirements. To be calculated as the CET1 ratio of the bank, less any common equity (as a percentage of risk-weighted assets) used to meet the bank's minimum CET1, minimum Tier 1 and minimum Total capital requirements.
69	National Common Equity Tier 1 minimum ratio (if different from Basel III minimum). 5.5% should be reported.
70	National Tier 1 minimum ratio (if different from Basel III minimum). 7% should be reported.
71	National total capital minimum ratio (if different from Basel III minimum). 9% should be reported.
72	Non-significant investments in the capital of other financial entities, the total amount of such holdings that are not reported in row 18, row 39, and row 54.
73	Significant investments in the common stock of financial entities, the total amount of such holdings that are not reported in row 19.
74	Mortgage servicing rights, the total amount of such holdings that are not reported in row 19 and row 23. - Not Applicable in India.
75	Deferred tax assets arising from temporary differences, the total amount of such holdings that are not reported in row 21 and row 25.
76	Provisions eligible for inclusion in Tier 2 in respect of exposures subject to standardised approach calculated in accordance with paragraph 21, prior to the application of the cap.
77	Cap on inclusion of provisions in Tier 2 under standardised approach calculated in accordance with paragraph 21.
78	Provisions eligible for inclusion in Tier 2 in respect of exposures subject to internal ratings-based approach calculated in accordance with paragraph 21.
79	Cap for inclusion of provisions in Tier 2 under internal ratings-based approach calculated in accordance with paragraph 21.

(2) Three step approach to reconciliation requirements

(i) Step 1

Under Step 1, a bank is required to take its balance sheet in its financial statements (numbers reported in the middle column of Table DF-12 below) and report the numbers when the regulatory scope of consolidation is applied (numbers reported in the right hand column below). If there are rows in the regulatory consolidation balance sheet that are not present in the published financial statements, a bank is required to give a value of zero in the middle column and furnish the corresponding amount in the column meant for regulatory scope of consolidation. A bank may, however, indicate what the exact treatment is for such amount in the balance sheet.

Table DF-12: Composition of capital - reconciliation requirements

(₹ in crore)

		Balance sheet as in financial statements	**Balance sheet under regulatory scope of consolidation**
		As on reporting date	**As on reporting date**
A	**Capital & Liabilities**		
i	Paid-up Capital		
	Reserves & Surplus		
	Minority Interest		
	Total Capital		
ii	Deposits		
	of which: Deposits from banks		
	of which: Customer deposits		
	of which: Other deposits (pl. specify)		
iii	Borrowings		
	of which: From the Reserve Bank		
	of which: From banks		
	of which: From other institutions & agencies		
	of which: Others (pl. specify)		
	of which: Capital instruments		
iv	Other liabilities & provisions		
	Total		

		Balance sheet as in financial statements	Balance sheet under regulatory scope of consolidation
		As on reporting date	As on reporting date
B	**Assets**		
i	Cash and balances with Reserve Bank of India		
	Balance with banks and money at call and short notice		
ii	Investments:		
	of which: Government securities		
	of which: Other approved securities		
	of which: Shares		
	of which: Debentures & Bonds		
	of which: Subsidiaries / Joint Ventures / Associates		
	of which: Others (Commercial Papers, Mutual Funds etc.)		
iii	Loans and advances		
	of which: Loans and advances to banks		
	of which: Loans and advances to customers		
iv	Fixed assets		
v	Other assets		
	of which: Goodwill and intangible assets		
	of which: Deferred tax assets		
vi	Goodwill on consolidation		
vii	Debit balance in Profit & Loss account		
	Total Assets		

(ii) Step 2

A bank shall expand the regulatory-scope balance sheet (revealed in Step 1) to identify all the elements that are used in the definition of capital disclosure template set out in Table DF-11. Set out below are some examples of elements that may need to be expanded for a particular banking group. The more complex the balance sheet of the

bank, the more items would need to be disclosed. Each element shall be given a reference number / letter that can be used in Step 3.

(₹ in crore)

		Balance sheet as in financial statements	Balance sheet under regulatory scope of consolidation
		As on reporting date	As on reporting date
A	**Capital & Liabilities**		
i	Paid-up Capital		
	of which: Amount eligible for CET1		e
	of which: Amount eligible for AT1		f
	Reserves & Surplus		
	Minority Interest		
	Total Capital		
ii	Deposits		
	of which: Deposits from banks		
	of which: Customer deposits		
	of which: Other deposits (pl. specify)		
iii	Borrowings		
	of which: From the Reserve Bank		
	of which: From banks		
	of which: From other institutions & agencies		
	of which: Others (pl. specify)		
	of which: Capital instruments		
iv	Other liabilities & provisions		
	of which: DTLs related to goodwill		c
	of which: DTLs related to intangible assets		d
	Total		
B	**Assets**		
i	Cash and balances with Reserve Bank of India		
	Balance with banks and money at call and short notice		
ii	Investments		
	of which: Government securities		

		Balance sheet as in financial statements	Balance sheet under regulatory scope of consolidation
		As on reporting date	**As on reporting date**
	of which: Other approved securities		
	of which: Shares		
	of which: Debentures & Bonds		
	of which: Subsidiaries / Joint Ventures / Associates		
	of which: Others (Commercial Papers, Mutual Funds etc.)		
iii	Loans and advances		
	of which: Loans and advances to banks		
	of which: Loans and advances to customers		
iv	Fixed assets		
v	Other assets		
	of which: Goodwill and intangible assets Out of which:		
	Goodwill		a
	Other intangibles (excluding MSRs)		b
	Deferred tax assets		
vi	Goodwill on consolidation		
vii	Debit balance in Profit & Loss account		
	Total Assets		

(iii) Step 3

(a) Under Step 3 a bank is required to complete a column added to the Table DF-11 disclosure template to show the source of every input.

(b) For example, the definition of capital disclosure template includes the line 'goodwill net of related deferred tax liability'. Next to the disclosure of this item in the disclosure template under Table DF-11, a bank should put 'a - c' to show that row 8 of the template has been calculated as the difference between component 'a' of the balance sheet under the regulatory scope of consolidation, illustrated in step 2, and component 'c'.

Extract of Basel III common disclosure template (with added column) – Table DF-11 *			
Common Equity Tier 1 capital: instruments and reserves			
		Component of regulatory capital reported by bank	Source based on reference numbers / letters of the balance sheet under the regulatory scope of consolidation from step 2
1	Directly issued qualifying common share (and equivalent for non-joint stock companies) capital plus related stock surplus		e
2	Retained earnings		
3	Accumulated other comprehensive income (and other reserves)		
4	Directly issued capital subject to phase out from CET1 (only applicable to non-joint stock companies)		
5	Common share capital issued by subsidiaries and held by third parties (amount allowed in group CET1)		
6	**Common Equity Tier 1 capital before regulatory adjustments**		
7	Prudential valuation adjustments		
8	Goodwill (net of related tax liability)		a-c

*This table is not a separate disclosure requirement. Rather, this extract indicates how step 3 would be reflected in Table DF-11.

(3) Main features template

(i) Template which a bank shall use to ensure that the key features of regulatory capital instruments are disclosed is set out below. A bank shall be required to complete all of the shaded cells for each outstanding regulatory capital instrument (A bank shall insert 'NA' if the question is not applicable).

Table DF-13: Main features of regulatory capital instruments

Disclosure template for main features of regulatory capital instruments		
1	Issuer	
2	Unique identifier (e.g., CUSIP, ISIN or Bloomberg identifier for private placement)	
3	Governing law(s) of the instrument	
	Regulatory treatment	

Disclosure template for main features of regulatory capital instruments		
4	Transitional Basel III rules	
5	Post-transitional Basel III rules	
6	Eligible at solo / group / group & solo	
7	Instrument type	
8	Amount recognised in regulatory capital (₹ in crore, as of most recent reporting date)	
9	Par value of instrument	
10	Accounting classification	
11	Original date of issuance	
12	Perpetual or dated	
13	Original maturity date	
14	Issuer call subject to prior supervisory approval	
15	Optional call date, contingent call dates and redemption amount	
16	Subsequent call dates, if applicable	
	Coupons / dividends	
17	Fixed or floating dividend / coupon	
18	Coupon rate and any related index	
19	Existence of a dividend stopper	
20	Fully discretionary, partially discretionary or mandatory	
21	Existence of step up or other incentive to redeem	
22	Noncumulative or cumulative	
23	Convertible or non-convertible	
24	If convertible, conversion trigger(s)	
25	If convertible, fully or partially	
26	If convertible, conversion rate	
27	If convertible, mandatory or optional conversion	
28	If convertible, specify instrument type convertible into	
29	If convertible, specify issuer of instrument it converts into	
30	Write-down feature	
31	If write-down, write-down trigger(s)	
32	If write-down, full or partial	
33	If write-down, permanent or temporary	
34	If temporary write-down, description of write-up mechanism	
35	Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument)	
36	Non-compliant transitioned features	

Disclosure template for main features of regulatory capital instruments		
37	If yes, specify non-compliant features	

(ii) Using the reference numbers in the left column of the table above, the following table provides a more detailed explanation of what a bank shall be required to report in each of the grey cells, including, where relevant, the list of options contained in the spread sheet's drop-down menu.

Further explanation of items in main features disclosure template	
1	Identifies issuer legal entity. Free text
2	Unique identifier (e.g., CUSIP, ISIN or Bloomberg identifier for private placement). Free text
3	Specifies the governing law(s) of the instrument. Free text
4	Specifies transitional Basel III regulatory capital treatment. Select from menu: [Common Equity Tier 1] [Additional Tier 1] [Tier 2]
5	Specifies regulatory capital treatment under Basel III rules not taking into account transitional treatment. Select from menu: [Common Equity Tier 1] [Additional Tier 1] [Tier 2] [Ineligible]
6	Specifies the level(s) within the group at which the instrument is included in capital. Select from menu: [Solo] [Group] [Solo and Group]
7	Specifies instrument type, varying by jurisdiction. Helps provide more granular understanding of features, particularly during transition. Select from menu: [Common Shares] [Perpetual Non-cumulative Preference Shares] [Perpetual Debt Instruments] [Upper Tier 2 Capital Instruments] [Perpetual Cumulative Preference Shares] [Redeemable Non-cumulative Preference Shares] [Redeemable Cumulative Preference Shares] [Tier 2 Debt Instruments] [Others- specify]
8	Specifies amount recognised in regulatory capital. Free text
9	Par value of instrument. Free text
10	Specifies accounting classification. Helps to assess loss absorbency. Select from menu: [Shareholders' equity] [Liability] [Non-controlling interest in consolidated subsidiary]
11	Specifies date of issuance. Free text
12	Specifies whether dated or perpetual. Select from menu: [Perpetual] [Dated]
13	For dated instrument, specifies original maturity date (day, month and year). For perpetual instrument put "no maturity".

Further explanation of items in main features disclosure template	
	Free text
14	Specifies whether there is an issuer call option. Helps to assess permanence. Select from menu: [Yes] [No]
15	For instrument with issuer call option, specifies first date of call if the instrument has a call option on a specific date (day, month and year) and, in addition, specifies if the instrument has a tax and / or regulatory event call. Also specifies the redemption price. Helps to assess permanence. Free text
16	Specifies the existence and frequency of subsequent call dates, if applicable. Helps to assess permanence. Free text
17	Specifies whether the coupon / dividend is fixed over the life of the instrument, floating over the life of the instrument, currently fixed but will move to a floating rate in the future, currently floating but will move to a fixed rate in the future. Select from menu: [Fixed], [Floating] [Fixed to floating], [Floating to fixed]
18	Specifies the coupon rate of the instrument and any related index that the coupon / dividend rate references. Free text
19	Specifies whether the non-payment of a coupon or dividend on the instrument prohibits the payment of dividends on common shares (i.e., whether there is a dividend stopper). Select from menu: [Yes], [No]
20	Specifies whether the issuer has full discretion, partial discretion or no discretion over whether a coupon / dividend is paid. If the bank has full discretion to cancel coupon / dividend payments under all circumstances it must select 'fully discretionary' (including when there is a dividend stopper that does not have the effect of preventing the bank from cancelling payments on the instrument). If there are conditions that must be met before payment can be cancelled (e.g., capital below a certain threshold), the bank must select 'partially discretionary'. If the bank is unable to cancel the payment outside of insolvency the bank must select 'mandatory'. Select from menu: [Fully discretionary] [Partially discretionary] [Mandatory]
21	Specifies whether there is a step-up or other incentive to redeem. Select from menu: [Yes] [No]
22	Specifies whether dividends / coupons are cumulative or noncumulative. Select from menu: [Noncumulative] [Cumulative]
23	Specifies whether instrument is convertible or not. Helps to assess loss absorbency. Select from menu: [Convertible] [Nonconvertible]
24	Specifies the conditions under which the instrument will convert, including point of non-viability. Where one or more authorities have the ability to trigger conversion, the authorities should be listed. For each of the authorities it should be stated whether it is the terms of the contract of the instrument that provide the legal basis for the authority to trigger conversion (a contractual approach) or whether the legal basis is provided by statutory means (a statutory approach). Free text
25	Specifies whether the instrument will always convert fully, may convert fully or partially, or will always convert partially.

Further explanation of items in main features disclosure template	
	Select from menu: [Always Fully] [Fully or Partially] [Always partially]
26	Specifies rate of conversion into the more loss absorbent instrument. Helps to assess the degree of loss absorbency. Free text
27	For convertible instruments, specifies whether conversion is mandatory or optional. Helps to assess loss absorbency. Select from menu: [Mandatory] [Optional] [NA]
28	For convertible instruments, specifies instrument type convertible into. Helps to assess loss absorbency. Select from menu: [Common Equity Tier 1] [Additional Tier 1] [Tier 2] [Other]
29	If convertible, specify issuer of instrument into which it converts. Free text
30	Specifies whether there is a write down feature. Helps to assess loss absorbency. Select from menu: [Yes] [No]
31	Specifies the trigger at which write-down occurs, including point of non-viability. Where one or more authorities have the ability to trigger write-down, the authorities should be listed. For each of the authorities it should be stated whether it is the terms of the contract of the instrument that provide the legal basis for the authority to trigger write-down (a contractual approach) or whether the legal basis is provided by statutory means (a statutory approach). Free text
32	Specifies whether the instrument will always be written down fully, may be written down partially, or will always be written down partially. Helps assess the level of loss absorbency at write-down. Select from menu: [Always Fully] [Fully or Partially] [Always partially]
33	For write down instrument, specifies whether write down is permanent or temporary. Helps to assess loss absorbency. Select from menu: [Permanent] [Temporary] [NA]
34	For instrument that has a temporary write-down, description of write-up mechanism. Free text
35	Specifies instrument to which it is most immediately subordinate. Helps to assess loss absorbency on gone-concern basis. Where applicable, banks should specify the column numbers of the instruments in the completed main features template to which the instrument is most immediately subordinate. Free text
36	Specifies whether there are non-compliant features. Select from menu: [Yes] [No]
37	If there are non-compliant features, banks to specify which ones. Helps to assess instrument loss absorbency. Free text

(4) Full terms and conditions of regulatory capital instruments

Under this template, a bank is required to disclose the full terms and conditions of all instruments included in the regulatory capital.

Table DF-14: Full terms and conditions of regulatory capital instruments

Instruments	Full terms and conditions

(5) Disclosure requirements for remuneration

Please refer to the Guidelines on Compensation of Whole Time Directors/ Chief Executive Officers/ Material Risk Takers and Control Function staff issued vide Reserve Bank of India (Commercial Banks – Governance) Directions, 2025 addressed to all private sector and foreign banks operating in India. A private sector and foreign bank operating in India is required to make disclosure on remuneration on an annual basis at the minimum, in its Annual Financial Statements in the following template:

Table DF-15: Disclosure requirements for remuneration

Remuneration		
Qualitative disclosures	(a)	Information relating to the bodies that oversee remuneration. Disclosure should include: • Name, composition and mandate of the main body overseeing remuneration. • External consultants whose advice has been sought, the body by which they were commissioned, and in what areas of the remuneration process. • A description of the scope of the bank's remuneration policy (e.g., by regions, business lines), including the extent to which it is applicable to foreign subsidiaries and branches. • A description of the type of employees covered and number of such employees.
	(b)	Information relating to the design and structure of remuneration processes. Disclosure should include: • An overview of the key features and objectives of remuneration policy. • Whether the remuneration committee reviewed the bank's remuneration policy during the past year, and if so, an overview of any changes that were made. • A discussion of how the bank ensures that risk and compliance employees are remunerated independently of the businesses they oversee.
	(c)	Description of the ways in which current and future risks are taken into account in the remuneration processes. Disclosure should include:

			• An overview of the key risks that the bank takes into account when implementing remuneration measures. • An overview of the nature and type of key measures used to take account of these risks, including risk difficult to measure (values need not be disclosed). • A discussion of the ways in which these measures affect remuneration. • A discussion of how the nature and type of these measures have changed over the past year and reasons for the changes, as well as the impact of changes on remuneration.
	(d)		Description of the ways in which the bank seeks to link performance during a performance measurement period with levels of remuneration. Disclosure should include: • An overview of main performance metrics for bank, top level business lines and individuals**.** • A discussion of how amounts of individual remuneration are linked to the bank-wide and individual performance. • A discussion of the measures the bank will in general implement to adjust remuneration in the event that performance metrics are weak. This should include the bank's criteria for determining 'weak' performance metrics.
	(e)		Description of the ways in which the bank seeks to adjust remuneration to take account of the longer-term performance. Disclosure should include: • A discussion of the bank's policy on deferral and vesting of variable remuneration and, if the fraction of variable remuneration that is deferred differs across employees or groups of employees, a description of the factors that determine the fraction and their relative importance. • A discussion of the bank's policy and criteria for adjusting deferred remuneration before vesting and (if permitted by national law) after.
	(f)		Description of the different forms of variable remuneration that the bank utilizes and the rationale for using these different forms. Disclosure should include: • An overview of the forms of variable remuneration offered. • A discussion of the use of different forms of variable remuneration and, if the mix of different forms of variable remuneration differs across employees or group of employees, a description of the factors that determine the mix and their relative importance.
Quantitative disclosures (The quantitative disclosures should only cover Whole	(g)	*	Number of meetings held by the main body overseeing remuneration during the financial year and remuneration paid to its member.
	(h)	*	Number of employees having received a variable remuneration award during the financial year.
		*	Number and total amount of sign-on awards made during the financial year.

Time Directors / Chief Executive Officer / Other Risk Takers)		*	Number and total amount of guaranteed bonuses awarded during the financial year.
		*	Details of severance pay, in addition to accrued benefits, if any.
	(i)	*	Total amount of outstanding deferred remuneration, split into cash, shares and share-linked instruments and other forms.
		*	Total amount of deferred remuneration paid out in the financial year.
	(j)	*	Breakdown of amount of remuneration awards for the financial year to show • fixed and variable • deferred and non-deferred • different forms used
	(k)	*	Total amount of outstanding deferred remuneration and retained remuneration exposed to ex post explicit and / or implicit adjustments.
		*	Total amount of reductions during the financial year due to ex- post explicit adjustments.
		*	Total amount of reductions during the financial year due to ex- post implicit adjustments.

Table DF-16: Equities – Disclosure for banking book positions

Qualitative Disclosures	
1	The general qualitative disclosure requirement (paragraph 2 of this Annex) with respect to equity risk, including: • differentiation between holdings on which capital gains are expected and those taken under other objectives including for relationship and strategic reasons; and • discussion of important policies covering the valuation and accounting of equity holdings in the banking book. This includes the accounting techniques and valuation methodologies used, including key assumptions and practices affecting valuation as well as significant changes in these practices.
Quantitative Disclosures	
1	Value disclosed in the balance sheet of investments, as well as the fair value of those investments; for quoted securities, a comparison to publicly quoted share values where the share price is materially different from fair value.
2	The types and nature of investments, including the amount that can be classified as: • Publicly traded; and • Privately held.
3	The cumulative realised gains (losses) arising from sales and liquidations in the reporting period.

4	Total unrealised gains (losses).[24]
5	Total latent revaluation gains (losses).[25]
6	Any amounts of the above included in Tier 1 and / or Tier 2 capital.
7	Capital requirements broken down by appropriate equity groupings, consistent with the bank's methodology, as well as the aggregate amounts and the type of equity investments subject to any supervisory transition or grandfathering provisions regarding regulatory capital requirements.

4. Leverage ratio disclosures

(1) The scope of consolidation of the Basel III leverage ratio as set out in paragraph 263 may be different from the scope of consolidation of the published financial statements. Also, there may be differences between the measurement criteria of assets on the accounting balance sheet in the published financial statements relative to measurement criteria of the leverage ratio (e.g., due to differences of eligible hedges, netting or the recognition of credit risk mitigation). Further, in order to adequately capture embedded leverage, the framework incorporates both on- and off-balance sheet exposures.

(2) The templates set out below are designed to be flexible enough to be used under any accounting standards, and are consistent yet proportionate, varying with the complexity of the balance sheet of the reporting bank[26].

(3) Summary comparison table

Applying values at the end of period (e.g., quarter-end), a bank shall report a reconciliation of its balance sheet assets from its published financial statements with the leverage ratio exposure measure as shown in Table DF-17 below. Specifically:

(i) line 1 should show the bank's total consolidated assets as per published financial statements;

[24]Unrealised gains (losses) recognised in the balance sheet but not through the profit and loss account.

[25]Unrealised gains (losses) not recognised either in the balance sheet or through the profit and loss account.

[26]Specifically, a common template is set out. However, with respect to reconciliation, banks are to qualitatively reconcile any material difference between total balance sheet assets in their reported financial statements and on-balance sheet exposures as prescribed in the leverage ratio.

(ii) line 2 should show adjustments related to investments in banking, financial, insurance or commercial entities that are consolidated for accounting purposes, but outside the scope of regulatory consolidation as set out in paragraphs 263(2) and 266(2);

(iii) line 3 should show adjustments related to any fiduciary assets recognised on the balance sheet pursuant to the bank's operative accounting framework but excluded from the leverage ratio exposure measure, as described in paragraph 266(1);

(iv) lines 4 and 5 should show adjustments related to derivative financial instruments and securities financing transactions (i.e., repos and other similar secured lending), respectively;

(v) line 6 should show the credit equivalent amount of OBS items, as determined under paragraph 269(2);

(vi) line 7 should show any other adjustments; and

(vii) line 8 should show the leverage ratio exposure, which should be the sum of the previous items. This should also be consistent with line 22 of Table DF-18 below:

Table DF 17- Summary comparison of accounting assets vs. leverage ratio exposure measure

	Item	(₹ in Crore)
1	Total consolidated assets as per published financial statements	
2	Adjustment for investments in banking, financial, insurance or commercial entities that are consolidated for accounting purposes but outside the scope of regulatory consolidation	
3	Adjustment for fiduciary assets recognised on the balance sheet pursuant to the operative accounting framework but excluded from the leverage ratio exposure measure	
4	Adjustments for derivative financial instruments	
5	Adjustment for securities financing transactions (i.e., repos and similar secured lending)	
6	Adjustment for off-balance sheet items (i.e., conversion to credit equivalent amounts of off- balance sheet exposures)	
7	Other adjustments	
8	**Leverage ratio exposure**	

(4) Common disclosure template and explanatory table, reconciliation, and other requirements

(i) A bank shall report, in accordance with Table DF-18 below, and applying values at the end of period (e.g., quarter-end), a breakdown of the following exposures under the leverage ratio framework: (i) on-balance sheet exposures; (ii) derivative exposures; (iii) SFT exposures; and (iv) OBS items. A bank shall also report its Tier 1 capital, total exposures and the leverage ratio.

(ii) The Basel III leverage ratio for the quarter, expressed as a percentage and calculated according to paragraph 4(20), is to be reported in line 22.

(iii) Reconciliation with public financial statements: A bank is required to disclose and detail the source of material differences between its total balance sheet assets (net of on-balance sheet derivative and SFT assets) as reported in its financial statements and its on-balance sheet exposures in line 1 of the common disclosure template.

(iv) Material periodic changes in the leverage ratio: A bank shall explain the key drivers of material changes in its Basel III leverage ratio observed from the end of the previous reporting period to the end of the current reporting period (whether these changes stem from changes in the numerator and / or from changes in the denominator).

Table DF-18: Leverage ratio common disclosure template		
	Item	Leverage ratio framework (₹ in crore)
On-balance sheet exposures		
1	On-balance sheet items (excluding derivatives and SFTs, but including collateral)	
2	(Asset amounts deducted in determining Basel III Tier 1 capital)	
3	**Total on-balance sheet exposures** (excluding derivatives and SFTs) (sum of lines 1 and 2)	
Derivative exposures		
4	Replacement cost associated with all *derivatives* transactions (i.e., net of eligible cash variation margin)	
5	Add-on amounts for PFE associated with *all* derivatives transactions	

6	Gross-up for derivatives collateral provided where deducted from the balance sheet assets pursuant to the operative accounting framework	
7	(Deductions of receivables assets for cash variation margin provided in derivatives transactions)	
8	(Exempted CCP leg of client-cleared trade exposures)	
9	Adjusted effective notional amount of written credit derivatives	
10	(Adjusted effective notional offsets and add-on deductions for written credit derivatives)	
11	**Total derivative exposures (sum of lines 4 to 10)**	
Securities financing transaction exposures		
12	Gross SFT *assets* (with no recognition of netting), after adjusting for sale accounting transactions	
13	(Netted amounts of cash payables and cash receivables of gross SFT assets)	
14	CCR exposure for SFT assets	
15	Agent transaction exposures	
16	**Total securities financing transaction exposures (sum of lines 12 to 15)**	
Other off-balance sheet exposures		
17	Off-balance sheet exposure at gross notional amount	
18	(Adjustments for conversion to credit equivalent amounts)	
19	**Off-balance sheet items (sum of lines 17 and 18)**	
Capital and total exposures		
20	**Tier 1 capital**	
21	**Total exposures (sum of lines 3, 11, 16 and 19)**	
Leverage ratio		
22	**Basel III leverage ratio**	

(v) The following table sets out explanations for each row of the disclosure template referencing the relevant paragraphs of the Basel III leverage ratio framework detailed in this document.

Explanation of each row of the common disclosure template	
Row number	**Explanation**
1	On-balance sheet assets according to paragraph 266(1).
2	Deductions from Basel III Tier 1 capital determined by paragraphs 263(2) and 266(2) and excluded from the leverage ratio exposure measure, reported as negative amounts.
3	Sum of lines 1 and 2.

Explanation of each row of the common disclosure template	
Row number	**Explanation**
4	Replacement cost (RC) associated with *all* derivatives transactions [including exposures resulting from transactions described in paragraph 267(6)(ii)], net of cash variation margin received and with, where applicable, bilateral netting according to paragraphs 267(1)-267(3) and 267(5)(ii).
5	Add-on amount for all derivative exposures according to paragraphs 267(1) - 267(3).
6	Grossed-up amount for collateral provided according to paragraph 267(4)(ii).
7	Deductions of receivables assets from cash variation margin provided in derivatives transactions according to paragraph 267(5)(ii), reported as negative amounts.
8	Exempted trade exposures associated with the CCP leg of derivatives transactions resulting from client-cleared transactions according to paragraph 267(6)(i), reported as negative amounts.
9	Adjusted effective notional amount (i.e., the effective notional amount reduced by any negative change in fair value) for written credit derivatives according to paragraph 267(7)(ii).
10	Adjusted effective notional offsets of written credit derivatives according to paragraph 267(7)(ii) and deducted add-on amounts relating to written credit derivatives according to paragraph 267(7)(ii) reported as negative amounts.
11	Sum of lines 4–10.
12	Gross SFT assets with no recognition of any netting other than novation with QCCPs as set out in paragraph 267(2)(i), removing certain securities received as determined by paragraph 268(2)(i) and adjusting for any sales accounting transactions as determined by paragraph 268(3).
13	Cash payables and cash receivables of gross SFT assets netted according to paragraph 268(2)(i) reported as negative amounts.
14	Measure of counterparty credit risk for SFTs as determined by paragraph 268(2)(ii).
15	Agent transaction exposure amount determined according to paragraphs 268(4)(i) - 268(4)(iii).
16	Sum of lines 12–15.
17	Total off-balance sheet exposure amounts on a gross notional basis, before any adjustment for credit conversion factors according to paragraph 269(2).
18	Reduction in gross amount of off-balance sheet exposures due to the application of credit conversion factors in paragraph 269(2).
19	Sum of lines 17 and 18.
20	Tier 1 capital as determined by paragraph 264.
21	Sum of lines 3, 11, 16 and 19.
22	Basel III leverage ratio according to paragraph 4(20).

(vi) To ensure that the summary comparison table, common disclosure template and explanatory table remain comparable across jurisdictions, there should be no

adjustments made by a bank to disclose its leverage ratio. A bank shall not add, delete or change the definitions of any rows from the summary comparison table and common disclosure template implemented in its jurisdiction. This will prevent a divergence of tables and templates that could undermine the objectives of consistency and comparability.

Annex IV

Guidelines on Stress Testing

A. General

1. Stress testing is commonly described as the evaluation of a bank's financial position under a severe but plausible scenario to assist in decision making within the bank. It enables a bank in forward looking assessment of risks, which overcomes the limitations of statistical risk measures or models based mainly on historical data and assumptions. It also facilitates internal and external communication and helps senior management understand the condition of the bank in the stressed time. Moreover, stress testing outputs are used by a bank in decision making process in terms of potential actions like risk mitigation techniques, contingency plans, capital and liquidity management in stressed conditions.

2. This Annex contains guidelines on overall objectives, governance, design, and implementation of stress testing programmes to be implemented by a bank. A bank shall carry out the stress tests involving shocks prescribed in paragraph 63 of this Annex, at a minimum. Though a bank shall assess its resilience to withstand shocks of all levels of severity indicated therein, the bank should be able to survive, at least the baseline shocks.

3. The Reserve Bank expects the degree of sophistication adopted by a bank in its stress testing programmes to be commensurate with the nature, scope, scale and the degree of complexity in the bank's business operations and the risks associated with those operations. The broad approach which could be considered by a bank in formulating its stress testing programmes is enumerated in paragraph 10 to 14 of this Annex, which classifies banks into three groups based on the size.

4. Stress testing shall form an integral part of the ICAAP, which requires a bank to undertake rigorous, forward-looking stress testing that identifies severe events or changes in market conditions that could adversely impact the bank. The ICAAP shall demonstrate that stress testing reports provide the senior management with a thorough understanding of the material risks to which the bank may be exposed. Stress testing shall also be a central tool in identifying,

measuring and controlling funding liquidity risks, in particular for assessing the bank's liquidity profile and the adequacy of liquidity buffers in case of both bank-specific and market-wide stress event.

5. The instructions contained in this Annex would be considered by the Reserve Bank to review the suitability of stress testing programmes and resultant actions including the requirement of additional capital and liquidity buffers as part of Supervisory Review and Evaluation Process (SREP) under the Basel capital framework. A bank shall perform the stress tests in terms of this Annex at least at half yearly intervals.

B. Level of application

6. The guidelines on stress testing under this Annex shall be applicable both at solo as well as group level.

C. Objective

7. The development and implementation of a stress-testing programme shall require defining the main objectives of stress-testing, which should cover, among other things, assisting in risk identification and control, complementing other risk management tools, improving capital and liquidity planning, and facilitating business decision-making.

8. Stress testing which is based on forward looking approach should provide a complementary and independent risk perspective to other risk management tools such as value-at-risk (VaR) and economic capital. Stress tests should complement risk management approaches that are based on complex, quantitative models using backward looking data and estimated statistical relationships. It should be used to assess the robustness of models to possible changes in the economic and financial environment. In particular, appropriate stress tests should challenge the projected risk characteristics of new products where limited historical data are available. A bank should also simulate stress scenarios in which the model-embedded statistical relationships break down as has been observed during the financial market crisis.

9. Stress tests should play an important role in the communication of risk within the bank and external communication with supervisors to provide support for internal and regulatory capital adequacy assessments.

D. Classification of banks for the purpose of stress testing

10. For stress testing, a bank can be classified into one of following three groups:

    (i) Group A - Bank with Total Risk Weighted Assets of more than ₹2000 billion;

    (ii) Group B - Bank with Total Risk Weighted Assets between ₹500 billion and ₹2000 billion; and

    (iii) Group C - Bank with Total Risk Weighted Assets less than ₹500 billion.

11. A bank that falls under Group C should, at least, conduct simple sensitivity analyses of the specific risk types to which it is most exposed. This will allow such a bank to identify, assess and test its resilience to shocks relating to the material risks to which its portfolios are exposed. However, in developing its stress testing programmes, the bank should still consider interactions between risks, for example intra or inter-risk concentrations, rather than focus on the analysis of risk factors in isolation. Even if the complexities of correlation among many of risk types are not clearly understood, an attempt should be made to qualitatively analyse the interactions among risk types and their impact on the portfolios. It is also expected that though the bank may not be able to perform complex firm-wide scenario-based stress tests, it should at least, address firm-wide stress testing in a qualitative manner.

12. A bank that falls under Group B, in addition to what is described in paragraph 11 of this Annex, should conduct multifactor sensitivity analysis and simple scenario analyses of the portfolios with respect to simultaneous movements in multiple risk factors caused by an event. The bank should select a sufficiently realistic scenario which can impact its portfolios. Such a bank may also do qualitative analysis with respect to reverse stress testing as discussed in this Annex. Moreover, the bank is expected to carry out both qualitative and quantitative analysis of correlations among risk types, feedback effects, etc. to get meaningful results from stress testing programmes.

13. A bank that falls under Group A should carry on stress testing programmes with all the complexities and severities required for programmes to be realistic and meaningful. The bank is expected to have an appropriate infrastructure in place to undertake a variety of stress testing approaches that are covered in this Annex from simple portfolio-based sensitivity analyses to complex macro scenario driven firm-wide exercises. Moreover, the bank is expected to include in its stress testing programmes rigorous firm-wide stress tests covering all material risks and entities, as well as the interactions between different risk types. The bank is expected to conduct reverse stress testing on a regular basis.

14. There may be a bank in any of the above categories, which may be part of the group or/ and operating internationally. Additional firm-wide stress testing programmes for such groups should be conducted at consolidated level to understand the risk at aggregate level and implications for the group. As other domestic and foreign regulators would be involved in such consolidated entities, they are expected to discuss the stress testing issues with the concerned regulators.

E. Governance

E.1 Board and senior management involvement

15. The ultimate responsibility for overall stress testing programme in a bank rests with the Board of Directors of the bank and with the Chief Executive Officer in the case of a foreign bank with branch presence in India. Senior management may be accountable for the programme's implementation, management and oversight. The involvement of the Board and Senior management is critical for the success and effectiveness of stress testing programme.

16. On practical considerations, some aspects of stress testing, such as design of methodologies, identification of risk factors, implementation, potential actions, etc., may be delegated. However, the Board shall actively participate in setting stress testing objectives, defining scenarios, discussing the results of stress tests in the context of bank’s risk profile, assessing potential actions and decision making. The Board / committees of Board shall therefore engage in the discussion of modelling assumptions and are expected to question assumptions

underlying the stress tests from a common/ business sense perspective e.g. whether assumptions about correlations in a stressed environment are reasonable. The Board shall also take responsibility for identifying and agreeing credible management intervention and mitigating actions.

E.2 Integration of stress testing in risk governance and risk management processes of a bank

17. To promote risk identification and control, stress testing should be included in the risk management activities of a bank at various levels of aggregation or complexity. This includes the use of stress testing for the risk management of an individual or groups of borrowers and transactions, for portfolio risk management, as well as for risk management of business lines or business strategy. It should be used to address existing or potential firm-wide risk exposures and concentrations.

18. Stress tests should be used to support a range of decisions. Board and senior management should be made aware of the limitations of the underlying assumptions of stress tests, the methodologies used and an evaluation of the impact of stress tests. It is thus important that senior management participates in the review and identification of potential stress scenarios and contributes to risk mitigating strategies. Stress tests should be used as an input for setting the risk appetite of the firm or setting exposure limits and to support the evaluation of strategic choices when undertaking and discussing longer term business planning. Importantly, stress tests should feed into the capital and liquidity planning process.

E.3 Internal policies and procedures and documentation

19. The stress testing programme should be governed by internal policies and procedures that are appropriately documented.

20. The following aspects should be detailed in policies and procedures governing the stress testing programme:

    (i) the type and specification of stress testing and scenarios and the main purpose / objective of each component of the programme;

(ii) frequency of stress testing exercises which is likely to vary depending on type and purpose;

(iii) the methodological details of each component, including the definition of relevant scenarios and the role of expert judgement; and

(iv) the range of remedial actions envisaged, based on the purpose, type and result of the stress testing, including an assessment of the feasibility of corrective actions in stress situations.

21. A bank shall document the underlying assumptions and fundamental elements for each stress testing exercise. These include the reasoning and judgments underlying the chosen scenarios and the sensitivity of stress testing results to the range and severity of the scenarios. An evaluation of such fundamental assumptions should be performed regularly or in light of changes in the risk characteristics of the bank or its external conditions and documented.

E.4 An appropriate and flexible infrastructure

22. Commensurate with the principle of proportionality, a bank should have suitably flexible infrastructure like IT system, qualified professionals, as well as data of appropriate quality and granularity. A bank should have adequate MIS in place to support the stress testing framework. A bank shall ensure that it devotes sufficient resources to developing and maintaining such infrastructures to enable the bank on a timely basis to modify methodologies to apply new scenarios as needed. The infrastructure should also be sufficiently flexible to allow for targeted or ad-hoc stress tests at the business line or firm-wide level to assess specific risks in times of stress.

F. Design

23. The identification of relevant stress events, the application of sound modelling approaches and the appropriate use of stress testing results require the collaboration of different senior experts within a bank. The unit with responsibility for implementing the stress testing programme should organise appropriate dialogue among these experts, challenge their opinions, check them for consistency (e.g., with other relevant stress tests) and decide on the design and

the implementation of the stress tests, ensuring an adequate balance between usefulness, accuracy, comprehensiveness and tractability.

24. There are broadly two categories of stress tests used in a bank viz. sensitivity tests and scenario tests.

25. Sensitivity analysis estimates the impact on a bank's financial position due to predefined movements in a single risk factor like interest rate, foreign exchange rate or equity prices, shifts in probabilities of defaults (PDs), etc. In the sensitivity analysis, generally, the source of the shock on risk factors is not identified and usually, the underlying relationship between different risk factors or correlation is not considered or ignored. For example, the impact of adverse movement in interest rate or foreign exchange rate on profitability is considered separately but the fact that movement in interest rate and foreign exchange rate is inter-related is ignored to keep the stress test simple. These tests can be run relatively quickly and form an approximation of the impact on the bank of a move in a risk driver.

26. A bank should identify relevant risk drivers in particular: macro-economic risk drivers (e.g. interest rates, foreign exchange rates), credit risk drivers (e.g. impact of monsoon or a shift in PDs), financial risk drivers (e.g. increased volatility in financial markets), operational risk drivers (e.g. natural disaster, terrorist attack, collapse of communication systems across the entire region/ country, etc.), and external events other than operational risk events (e.g. sudden drying up of external funding, sovereign downgrade, market events, events affecting regional areas or industry, global events, etc).

27. A bank should then stress the identified risk drivers using different degrees of severity. For example, a sensitivity test might explore the impact of varying declines in equity prices such as by 40 per cent, 50 per cent, 60 per cent or a range of increases in interest rates such as by 100, 200, 300 basis points. The severity of a single risk factor is likely to be influenced by long-term historical experience but a bank is advised to supplement this with hypothetical assumptions of a wide range of possibilities to test its vulnerability to specific risk factors.

28. A bank can conduct sensitivity analyses at the level of individual exposures, portfolios or business units, as well as firm-wide, against specific risk areas as sensitivity analysis is likely to lend itself to risk-specific stress testing. It is likely to be influenced by the purpose of stress testing.

29. Single factor analysis can be supplemented by simple multi-factor sensitivity analyses, where a combined occurrence of some risk drivers is assumed, without necessarily having a scenario in mind. While a bank classified under Group C may use multi-factor sensitivity analysis as an option, a bank classified under Group B and Group A shall invariably use multi-factor sensitivity analysis as part of its stress testing.

30. In utilising this technique, a bank shall be mindful of the correlations between the various risk factors and ensure that these are taken into consideration when developing the underlying assumptions used in the stress scenarios.

31. An effective stress testing programme should comprise scenarios along a spectrum of events and severity levels. It helps deepen management's understanding of vulnerabilities and the effect of non-linear loss profiles.

G. Review of stress testing

32. As the environment in which banks are operating is quite dynamic, the stress testing framework should be reviewed periodically, both qualitatively and quantitatively, to determine its efficacy and to consider the need for modifying any of the elements. The framework should be subjected to at least annual reviews which shall cover, among others, the following aspects:

    (i) the effectiveness of the programme in meeting its intended purposes;

    (ii) integration of the stress testing in the risk management processes;

    (iii) realistic levels of stress applied;

    (iv) systems implementation;

    (v) management oversight;

    (vi) data quality and MIS;

    (vii) documentation;

(viii) business and/or managerial assumptions used; and

(ix) any other assumptions used.

33. The quantitative processes should include benchmarking with other stress tests within and outside the bank.

34. Since the stress test development and maintenance processes often imply judgmental and expert decisions (e.g., assumptions to be tested, calibration of the stress, etc.), the independent control functions such as risk management and internal audit should also play a key role in the process.

35. An important corollary of review and assessment of stress testing programmes involves updating of the processes to keep them relevant and meaningful and suitable to the requirements of the bank.

H. Coverage

H.1 Use of a suite of techniques and methodologies

36. A bank in general should use multiple perspectives and a range of techniques and methodologies to achieve comprehensive coverage in its stress testing programme.

37. The suite may include quantitative and qualitative techniques to support and complement the use of models and to extend stress testing to areas where effective risk management requires greater use of judgments. For example, it may contain a narrative scenario which should include various trigger events, such as monetary policy, financial sector developments, commodity prices, political events, global events, monsoon and natural disasters.

38. Stress tests should range from simple sensitivity analysis to more complex stress tests like scenario analysis with system-wide interactions and feedback effects. Some stress tests should be run at regular intervals while the stress testing programme should also allow for the possibility of ad hoc stress testing. Stress testing should include various time horizons depending on the risk characteristics of the analysed exposures and purposes.

39. A bank is expected to employ a combination of stress testing techniques that are most appropriate to the size and complexity of its business activities, as also the objectives in mind.

H.2 Forward looking scenario

40. The stress testing programme should cover forward-looking scenarios to incorporate different possibilities of multi-level stress tests, changes in portfolio composition, new information and emerging risk possibilities. These are generally not covered by relying on historical risk management or replicating previous stress episodes. However, historical scenarios (where a range of risk drivers are moved simultaneously) may provide useful information on the way risk drivers behave collectively in a crisis and they may therefore be useful to assess the assumptions of an internal capital model, and in particular correlation estimates.

41. The compilation of forward-looking scenarios requires combining the knowledge and judgment of experts across the organisation. Further, as the statistical relationships used to derive the probability tend to break down in stressed conditions, giving appropriate weight to expert judgment in defining relevant scenarios with a forward-looking perspective thus becomes critical.

42. Forward looking scenarios of varying severity and for various purposes can be designed by calibrating historically observed macro-economic and financial variables, internal risk parameters, losses, etc. The formulation of realistic and imaginative scenarios requires at minimum the following two steps indicated in paragraphs 43 and 44 of this Annex.

43. A bank should take into account both the systematic and institution-specific changes in the present and near future scenarios to be forward-looking. For this purpose, the following aspects are relevant:

    (i) All the material risk factors e.g., credit risk, market risk, operational risk, interest rate risk, liquidity risk, etc. that a bank may be exposed to should be stressed. In this regard, the results obtained from single factor analyses may be used to identify scenarios that include a set of highly plausible risk factors. No material risk factor should be left unstressed or unconsidered.

(ii) Identified risk drivers should behave in ways which are consistent with the other risk drivers in a stress.

(iii) All bank-specific vulnerabilities should be identified and analysed. These should take the regional and sectoral characteristics of a bank into account as well as consider specific product or business line exposures and funding policies.

(iv) A bank should take into account developments in technology such as newly developed and sophisticated financial products and their interaction with the valuation of more traditional products.

(v) The chosen scenario should be applied to all positions e.g., on- and off-balance sheet exposure of a bank.

44. A bank should identify and develop appropriate and meaningful mechanisms to convert scenarios into relevant internal risk parameters and potential losses. They should also be tested regularly to check their reliability. For this purpose, the following aspects are relevant:

(i) A bank should make realistic explicit estimates/ assumptions about the correlation between underlying macro-economic and financial variables such as interest rates, exchange rate, global oil prices, GDP, monsoon, equity, consumer and asset prices, capital flows, etc;

(ii) The transformation of external variables or institution-specific events into internal losses or increased risk measures on consistent basis is a challenging task. A bank should be aware of the possible dynamic interactions among risk drivers, the effects on earnings and on- and off-balance sheet position;

(iii) The links between underlying economic factors and internal risk parameters are likely to be based primarily on institutional experience and analysis, which may be supplemented by external research. Benchmarks, such as those based on external research, may be quantitative or qualitative;

(iv) Considering the complexity involved in modelling hypothetical and macro-economic based scenarios, a bank should be aware of the model risk

involved. A regular and conservative expert review of the model's assumptions and mechanics are important as well as a conservative modelling approach to account for model risk; and

(v) Where a wide variety of models, supporting formulas and varying assumptions are used, a bank should consider ways to streamline its stress testing programmes to improve transparency and simplicity.

H.3 System-wide interactions and feedback effects

45. The strong links between the real economy and financial economy as well as the process of globalisation have amplified the need to look at system-wide interactions and feedback effects. The stress test should explicitly identify interdependences, e.g., among regions, among sectors and among markets. The overall scenario should take into account system-wide dynamics – such as leverage building up across the system, closure of certain markets, risk concentrations in a whole asset class such as mortgages, and adverse feedback dynamics, for example through interactions among valuations, losses, margining requirements and insurance relations.

46. The above analysis can be very difficult to model quantitatively. Thus, a bank may make qualitative assessments of the second order effects of stress. Such assumptions should be documented and reviewed by senior management.

H.4 Levels of severity in scenarios

47. Stress testing should be based on exceptional but plausible events. However, the stress testing programme should cover a range of scenarios with different severities including scenarios calibrated against the most adverse movements in individual risk drivers experienced over a long historical period. Where appropriate, a bank might consider a scenario with a severe economic downturn and/ or a system-wide shock to liquidity.

48. In developing severe downturn scenarios, a bank should also consider plausibility. For example, as an economy enters recession, a bank should not necessarily always assume a further specific level of stress. There may be times when the stressed scenario is close to the base case scenario but supplemented

with specific shocks (e.g., interest rates, exchange rates), which should be reflected in the scenarios.

49. Some of the scenarios that can be constructed from historical disturbances or events of significance may be the 1973 world oil crisis, 1973-74 stock market crisis, the secondary banking crisis of 1973-75 in UK, the default of Latin American countries on their debt in the early 1980s, the Japanese property bubble of the 1980s, the 1987 Market Crash, the Scandinavian banking crisis of 1990s, the 1991 external payments crisis in India, the securities scam of 1991-92 in India, the ERM crises of 1992 and 1993, the fall in bond markets in 1994, the 1994 economic crisis in Mexico, the 1997 Asian Crisis, the 1998 Russian Crisis, 26/11 2001 U.S. Crisis, the sub-prime mortgage crisis of 2007-2008 turning into severe recession, debt crisis of Greece in 2010, etc. Scenarios may also contain some risk factors or variables which were specially observed during financial crisis of 2007-08:

(i) Scenarios to include significant strategic or reputational risk in particular for significant business lines;

(ii) Scenarios to include, where relevant, an episode of financial market turbulence or a shock to market liquidity;

(iii) Scenarios under which capital might not be freely transferable within banking groups in periods of severe downturn or extended market disruption;

(iv) Scenarios under which a crisis impairs the ability of even very healthy banks to raise funds at reasonable cost;

(v) Scenarios under which model-embedded statistical relationships break down;

(vi) Scenarios under which risk characteristics of new products projected on the basis of limited historical data are challenged; and

(vii) Scenarios to include simultaneous pressures in funding and asset markets, and the impact of a reduction in market liquidity on exposure valuation, etc.

50. Some of the scenarios can be designed from the specific observed/ imaginative risk parameters or events like:

(i) domestic economic downturn, economic downturn of major economies to which a bank is directly exposed or to which the domestic economy is related;

(ii) decline in the prospects of sectors to which a bank is having significant exposures, increase in level of NPAs and provisioning levels, rating downgrades, failure of major counterparties;

(iii) timing difference in interest rate changes (repricing risk), unfavourable differential changes in key interest rates (basis risk), parallel / non-parallel yield curve shifts (yield curve risk), changes in the values of standalone and embedded options (option risk), adverse changes in exchange rates of major currencies, decline in market liquidity for financial instruments, stock market declines, tightening of market liquidity; and

(iv) significant operational risk events viz. bank-specific or market-wide cyber-attacks, increasing fraud risk in an economic downturn like increase in credit card frauds, internet banking frauds and litigation, rogue trader scenarios, damage to tangible assets due to a natural disaster say tsunami.

H.5 Reverse stress testing

51. Reverse stress testing is a technique that involves assuming worst stressed outcome and tracing the extreme event/ shocks that bring the maximum impact. Reverse stress testing starts from an outcome of business failure and identifies circumstances where this might occur. It is seen as one of the risk management tools usefully complementing the “usual” stress testing, which examines outcomes of predetermined scenarios. Reverse stress testing is not expected to result in capital planning instead it is primarily designed as a risk management tool in identifying scenarios and underlying dynamism of risk drivers in those scenarios, that could cause an institution’s business model to fail.

52. It is a useful tool in risk management as it helps understand potential vulnerabilities and fault lines in the business, including ‘tail risks’. It will also be useful in assessing assumptions made about the business model, business

strategy and the capital plan. The results of reverse stress test may be used for monitoring and contingency planning.

53. Reverse stress testing shall be carried out regularly by a large and complex bank i.e., Group A bank, to investigate the risk factors that wipe out its capital resources and also make its business unviable. As a starting point reverse stress testing is likely to be carried out in a more qualitative manner than other types of stress testing. As experience is developed this should then be mapped into more sophisticated qualitative and quantitative approaches developed for other stress testing.

H.6 Complex and bespoke products

54. A bank may mistakenly assess the risk of some products by relying on external credit ratings or historically observed credit spreads related to (seemingly) similar products like corporate bonds with the same external rating. Such approaches cannot capture relevant risk characteristics of complex, structured products under severely stressed conditions.

55. Stress tests for securitised assets should consider the underlying asset pools, their exposure to systematic market factors, relevant contractual arrangements and embedded triggers, and the impact of leverage, particularly as it relates to the subordination level of the specific tranches in the issue structure.

I. Pipeline and warehousing risk

56. The stress testing programme should cover pipeline and warehousing risks associated with securitization activities. A bank should include such exposures in its stress tests regardless of their probability of being securitised.

J. Reputational and other off-balance sheet risks

57. To mitigate reputational spill-over effects and maintain market confidence, a bank should develop methodologies to measure the effect of reputational risk on other risk types, with a particular focus on credit, liquidity and market risks. For instance, a bank should include non-contractual off-balance sheet exposures in its stress tests to determine the effect on its credit, liquidity and market risk profiles.

58. A bank should carefully assess the risks associated with commitments to off-balance sheet vehicles e.g., structured credit securities and the possibility that asset will need to be taken on balance sheet for reputational reasons. Therefore, in its stress testing programme, a bank should include scenarios assessing the size and soundness of such vehicles relative to its own financial, liquidity and regulatory capital positions. This analysis should include structural, solvency, liquidity and other risk issues, including the effects of covenants and triggers.

K. Risks from leveraged counterparties

59. A bank may have large gross exposures to leveraged counterparties including financial guarantors, investment banks and derivatives counterparties that may be particularly exposed to specific asset types and market movements. In case of severe market shocks, these exposures may increase abruptly and potential cross-correlation of the creditworthiness of such counterparties with the risks of assets being hedged may emerge (i.e., wrong-way risk). The bank should enhance its stress testing approaches related to these counterparties to capture adequately such correlated tail risks.

L. Management intervention action

60. The performance of risk mitigating techniques like hedging, netting and the use of collateral should be challenged and assessed systematically under stressed conditions when markets may not be fully functioning, and multiple institutions could simultaneously be pursuing similar risk mitigating strategies.

M. Single factor stress tests to be carried out by a bank

61. The stress testing framework and methodology in each bank should be tailored to suit the size, complexity, risk philosophy, risk perceptions and skills in each bank. However, a bank shall necessarily apply the shocks indicated in this annex to its portfolios. Most of the shocks are indicated in three levels of severity - Baseline, Medium and Severe.

62. A bank may also endeavour to assess its resilience to the possibility of more than one shock materialising simultaneously. A bank which has already realised shocks more severe than the ones indicated here should have them built into its stress testing framework as baseline shocks and apply more stringent shocks to

make the stress testing exercise meaningful. A bank with advanced capabilities may adopt more sophisticated methodologies for stress testing.

N. Sensitivity analysis – shocks

63. Credit Risk

(1) The stress test for credit risk aims to assess the impact of macro-economic cycles as well as bank specific factors on bank's financial performance – be it capital adequacy or profitability. In an economic downturn, the major risk factors facing a bank are the credit downgrades of the counterparties, deterioration in the asset quality and erosion in the collateral value. On the other hand, in an economic upturn, there is likely to be a sense of exuberance on the backup of under-pricing of risk, leading to excessive credit growth in select sensitive sectors. To address this excessive sectoral credit growth, provisioning and/ or risk weights on the exposure to these select sensitive sectors may be increased and the bank should be in a position to factor in such a rise during the economic upturn. Against this backdrop, a bank may at the minimum carry out stress tests, given in the following paragraphs, on its credit portfolio.

(2) Shock 1: Increase in NPAs - Credit quality generally tends to deteriorate during economic downturn as debtors begin to experience cash flow problems which in turn affect smooth servicing of debt leading to a possible deterioration in asset quality.

Net NPA increase by 50 (Baseline), 100 (Medium), and 150 (Severe) percent, and simultaneous increase in provisioning to 1 percent for standard loans; 30 percent - for substandard loans; and 100 percent for doubtful loans over one-year period.

(3) Shock 2: Increase in NPA in Top Five Industries – Some industries are more affected by economic downturn and experience problems in servicing of debt.

Additional 3 (Baseline) and 5 (Medium) percentage points increase in Net NPAs in top five industries.

(4) Shock 3: Increase in NPA in Specific Sectors – Some sectors undergo stress due to idiosyncratic factors.

Additional 3 (Baseline) and 5 (Medium) percentage points increase in Net NPAs in specific sectors: Agriculture, Power, Real Estate, Telecom and Roads.

(5) Shock 4: Slippage of Restructured Standard Assets – Assets which have undergone stress and are restructured are more prone to deterioration in asset quality.

Additional slippages in restructured standard assets – 20 per cent (Baseline), 30 per cent (Medium) and 40 per cent (Severe) of restructured standard assets.

(6) Shock 5: Depletion in collateral value by 10 per cent (Baseline), 15 per cent (Medium), 20 per cent (Severe).

(7) Shock 6: Downgrade in counter-party rating - In a downturn, bank's counterparties may suffer credit downgrade awarded by an external CRA or internally.

Uniform downgrade of borrowers by one notch across all rating grades – 5 per cent (Baseline), 10 per cent (Medium), 20 per cent (Severe) of all borrowers.

(8) Shock 7: Concentration Risk – Individual borrowers

Default by largest single borrowers – Default by top one (Baseline), top two (Medium), top three (Severe) borrower

(9) Shock 8: Concentration Risk – Group

Default by largest group borrower – Default by top three company-member of the group (Baseline), top five company-members of the group (Medium), all company-members of the group (Severe)

(10) Shock 9: Concentration Risk – Industries / Sectors

Default in all exposures to largest industries/sectors – Default by topmost industry/ sector (Baseline), top three industries/sectors (Medium), top five industries/sectors (Severe).

64. Market risk

The prime objective is to study the impact of stress test on Profit and Loss account.

(1) Foreign exchange risk

(i) Forex risk arises from exchange rate changes adversely impacting the local currency denominated a bank’s assets and liabilities. The stress test evaluates the impact of exchange rate variations on the bank’s net open position and also on bank’s profitability.

(ii) Shock 1: Depreciation of Indian rupee

(a) Baseline: 15 per cent depreciation in 30 days

(b) Medium: 20 per cent depreciation in 30 days

(c) Severe: 25 per cent depreciation in 30 days

(iii) Shock 2: Appreciation of Indian rupee

(a) Baseline: 15 per cent appreciation in 30 days

(b) Medium: 20 per cent appreciation in 30 days

(c) Severe: 25 per cent appreciation in 30 days

(iv) Reverse stress testing: how much depreciation would be necessary for Tier 1 capital to move down to 3 per cent over 60 days?

(2) Interest rate risk

(i) Interest rate risk is the risk where changes in market interest rates might adversely affect a bank's financial condition. The immediate impact of changes in interest rates is on bank's earnings through changes in its Net Interest Income (NII). A long-term impact of changes in interest rates is on bank's Market Value of Equity (MVE) or net worth through changes in the economic value of its liabilities and off-balance sheet positions. The interest rate risk, when viewed from these two perspectives, is known as 'earnings perspective' and 'economic value' perspective, respectively.

(ii) A bank should conduct sensitivity analysis using methods that reflect its specific interest rate risk characteristics using gap analyses or simulation techniques. A bank should at a minimum assess its resilience using the baseline factors given below:

Interest rate risk for both trading and banking book

(a) Shock 1: Parallel upward/downward shift of IND yield curve in bps

Baseline 250; Medium: 300; Severe 400

(b) Shock 2: Steepening of IND yield curve

100 bps linearly spread between 15-day and over 25-year maturities

(c) Shock 3: An Inversion of the yield curve

One -year rates up 250 bps and 10-year rates down 100 bps

(3) Equity price risk

Shock: Decline in equity prices across the board

Baseline: 40 per cent; Medium: 50 per cent; Severe: 60 per cent

65. Liquidity risk

(1) Whether a bank can be regarded as having sufficient liquidity depends to a great extent on its ability to meet obligations under a funding crisis. Therefore, in addition to conducting cash-flow projections to monitor net funding requirements under normal business conditions, a bank should perform stress tests regularly by conducting projections based on “what if” scenarios on its liquidity positions to:

(i) identify sources of potential liquidity strain;

(ii) ensure that current liquidity risk exposures remain in accordance with the established liquidity risk tolerance; and

(iii) analyse any possible impact of future liquidity stresses on its cash flows, liquidity position, profitability and solvency.

(2) Institution-specific crisis scenarios

(i) An institution-specific crisis scenario should cover situations that could arise from a bank experiencing either real or perceived problems which affect public confidence in the bank and its firm-wide or group-wide operations. It should represent the bank’s view of the behaviour of its cash flows in a severe crisis. A key assumption is that many of the bank’s liabilities cannot be rolled over or replaced, resulting in the need to utilise its liquidity cushion.

(ii) For a retail bank, this scenario will likely entail an acute deposit run. Such a scenario would typically include the following characteristics:

(a) significant daily run-off rates for deposits, with increasing requests from customers to redeem their time deposits before maturity;

(b) interbank deposits repaid at maturity;

(c) no new unsecured or secured funding obtainable from the market; and

(d) forced sale of marketable securities at discounted prices.

(iii) A foreign bank (including branches and subsidiaries of foreign banking groups) should, in particular, assess the effects of a group-wide crisis scenario on its liquidity positions. This scenario assumes that an institution-specific stress event is affecting the global operations of the banking group (i.e., with problems spilling over the whole banking group). In a group-wide crisis, a default position would be that no intragroup or head office funding support can be assumed to be available.

(iv) There are other institution-specific scenarios that are less severe in the short term but may subject a bank to longer-term liquidity pressures. These scenarios may be triggered by possible changes in the market and public perceptions of a bank that affect its access to funds or cause a gradual drain on its liquidity. A bank is encouraged to take account of different scenarios applicable to its own circumstances as part of the ongoing liquidity risk management process.

(3) General market crisis scenarios

(i) A general market crisis scenario is one where liquidity at a large number of financial institutions in one or more markets is affected. Characteristics of this scenario may include –

(a) a market-wide liquidity squeeze, with severe contraction in the availability of secured and unsecured funding sources, and a simultaneous drying up of market liquidity in some previously highly liquid markets;

(b) counterparty defaults;

(c) substantial discounts needed to sell or repo assets and wide differences in funding access among banks due to the occurrence of a severe tiering of their perceived credit quality (i.e., flight to quality);

(d) restrictions on currency convertibility; and

(e) severe operational or settlement disruptions affecting one or more payment or settlement systems.

(ii) A bank should be aware that the cash-flow patterns of certain assets and liabilities may behave quite differently in the case of a general market crisis scenario as compared with the institution-specific crisis scenario. For example, a bank may have less control over the level and timing of future cash flows from the sale of marketable debt securities under a general market crisis scenario. This could be due to the fact that only very few market participants would be willing or would have sufficient liquidity to purchase securities. Hence, a bank should assign appropriate discount factors to such assets to reflect the price risk associated with different stress scenarios. Moreover, the impact of a general market crisis on individual bank may differ. For example, a bank with a strong market reputation may benefit from a flight to quality as depositors seek a safe haven for their funds.

(4) Combined scenarios

(i) A bank is expected to incorporate a third type of scenario into its stress tests which bears the characteristics of both an institution-specific crisis and a general market crisis. Although this combined scenario may reflect a set of very adverse circumstances that could plausibly happen to any bank in terms of liquidity impact, it will generally be inappropriate for a bank to adopt an “additive approach” in designing the scenario, viz., simply by summing up the underlying assumptions and estimated impacts of an institution-specific scenario and a general market risk scenario. A bank should consider making appropriate adjustments under the combined scenario to modulate the severity of assumptions used commonly for the institution-

specific and the general market crisis scenarios, having regard to how the various stress circumstances may interact in the scenario.

(ii) The following are some relevant factors that can be considered:

(a) As a greater number of financial institutions in the market will be affected by the crisis, this may change the way in which some institution-specific stress elements are to be structured. For example, instead of a quick but severe bank run, there may be a less acute, but more persistent and protracted run-off of customer deposits;

(b) Even lower realisable values of assets may result as the bank concerned seeks to sell or repo large quantities of assets when the relevant asset markets become less liquid and market participants are generally in need of liquidity.

(5) Minimum stress period

The ability of a bank to honour its immediate commitments at least for the initial period when the stress is likely to be most acute is crucial for its later survival. As such, it is expected that a bank should have sufficient funds (including those that can be generated from its available liquid assets and other funding sources) to cover its liquidity needs and to enable it to continue its business for a certain minimum stress period under each of the crisis scenarios, without resorting to emergency liquidity assistance from the Reserve Bank. A bank should assume the minimum stress period for an institution-specific crisis scenario to last for no less than five business days, and that for a general market crisis scenario and a combined scenario, no less than one calendar month. A bank should adopt longer minimum stress periods if its liquidity risk profile warrants this.

(6) Liquidity risk stress test

(i) Outflows

		Run-off factor		
		Baseline	**Medium**	**Severe**
1.	Partial loss of retail deposits[1]			
	Stable[2]	5%	10%	20%
	Unstable[3]	10%	20%	40%
2.	Partial loss of wholesale deposits[4]			

	Stable	5%	10%	20%
	Unstable	10%	20%	40%
3.	Partial loss of secured short-term financing like Repo and CBLO			
	Non-financial corporate bonds with any counterparty	15%	30%	60%
	Non- Level 1 asset[5] or non- Level 2A asset[6] with domestic sovereigns, multilateral development banks or domestic PSEs as a counterparty.	25%	50%	100%
	Securitised instrument including RMBS	25%	50%	100%
	Other level 2B asset[7]	50%	75%	100%
	All other assets	100%	100%	100%
4.	Market valuation changes on derivative transaction including change in collateral value posted for derivative transactions	Look back approach[8]		
5.	Unscheduled draws on committed but unused credit and liquidity facilities			
	Retail and small[9] business customers	5%	10%	20%
	Credit facility to non-financial corporates, PSEs, and MDBs	10%	20%	40%
	Credit facilities to banks subject to prudential supervision	40%	70%	100%
	Credit facilities to other financial institutions	40%	80%	100%
	Liquidity facilities to other financial institutions	100%	100%	100%
	Liquidity facility to non-financial corporates, PSEs and MDBs.	30%	60%	100%
	Credit and liquidity facilities to other legal entities	100%	100%	100%

(ii) Inflows

	Instruments	Haircut		
Securities held under HFT				
		Baseline	Medium	Severe
1.	Corporate bond with rating AA- or higher	15%	30%	60%
2.	Corporate bond with rating between A+ and BBB-	50%	75%	100%
3.	Securitised instruments including RMBS	25%	50%	100%
4.	Equity shares	50%	100%	100%

5.	Securities/loans maturing within 30 days and held under AFS and HTM category.	As above

[1]Retail deposits are defined as deposits placed with a bank by a natural person.

[2]Stable deposits are insured deposits in transactional accounts (e.g., Accounts where salaries are automatically credited/ deposits are in accounts where salaries are paid out from) or relationship-based accounts (e.g. The deposit customer has another relationship with the bank say a loan).

[3]All deposits other than stable deposits are unstable deposits.

[4]Unsecured wholesale funding is defined as funding/deposits from non-natural persons i.e., legal entities including sole proprietorship and partnerships.

[5]Level 1 asset include cash, Government securities and a portion (to be notified separately) of SLR deposits

[6]Level 2A assets includes marketable non-financial sector corporate bonds rated AA- or better and marketable securities assigned 20 per cent risk weight.

[7]Level 2B assets includes securitised instrument including RMBS, corporate bond rated between A+ and BBB-, equity shares, and commercial paper.

[8] Cash outflows arising out of margin and collateral requirements in the derivative exposures may be quite significant. A Bank should identify the risk factors impacting the valuation of derivatives contracts in its portfolio (like interest rates, forex rates, volatilities, etc.) and generate the movements in these risk factors based on past distribution of movement of these risk factors. For base line scenario movements in the risk factors projections could be at 95 per cent confidence interval, for medium scenarios movements in the risk factors projections could be based on 99 per cent confidence interval and for severe scenarios, projections should be based on 99.9 per cent confidence interval. Collateral/Margin requirements based on these scenarios should then be calculated.

[9]Small business is one where the total average annual turnover is less than ₹50 crore as defined in paragraph 52 of these Directions.